

BANK OF NOVA SCOTIA /
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Prospectus Supplement

(to the Prospectus Dated December 28, 2012)

THE BANK OF NOVA SCOTIA

U.S.\$1,250,000,000 1.450% Senior Notes due 2018

The U.S.\$1,250,000,000 Senior Notes due 2018 (the “Notes”) offered by this prospectus supplement (this “Prospectus Supplement”) will bear interest at a rate of 1.450% from April 25, 2013 and will mature on April 25, 2018. Interest on the Notes will be payable in arrears on April 25 and October 25 of each year, commencing October 25, 2013 and continuing until April 25, 2018. The Notes will be unsecured and unsubordinated obligations of The Bank of Nova Scotia (the “Bank”) and will constitute deposit liabilities of the Bank for purposes of the *Bank Act* (Canada) (the “Bank Act”).

Investing in the notes involves risks. See “Risk Factors” beginning on page S-1 of this Prospectus Supplement and page 6 of the accompanying prospectus of the Bank dated December 28, 2012 (the “Prospectus”).

Prospective investors should be aware that the acquisition of the Notes described herein may have tax consequences both in the United States and in Canada. Such consequences for investors who are resident in, or citizens of, the United States may not be described fully herein.

The enforcement by investors of civil liabilities under the United States federal securities laws may be affected adversely by the fact that the Bank is a Canadian bank, that many of its officers and directors, and some of the experts named in this Prospectus Supplement, may be residents of Canada and that all or a substantial portion of the assets of the Bank and such persons may be located outside the United States.

Neither the U.S. Securities and Exchange Commission (the “SEC”) nor any state securities regulator has approved or disapproved of the Notes, or determined if this Prospectus Supplement or the accompanying Prospectus is truthful or complete. Any representation to the contrary is a criminal offense.

| | Price to the Public(1) | Underwriters’ FeesNet Proceeds to the Bank(1)(2) | |
|-----------------|-----------------------------------|---------------------------------------------------------|---------------------|
| Per Note | 99.784% | 0.350% | 99.434% |
| Total | U.S.\$1,247,300,000 | U.S.\$4,375,000 | U.S.\$1,242,925,000 |

(1) Plus accrued interest, if any, from April 25, 2013 to the date of delivery. Accrued interest must be paid by the purchasers.

(2) Before deduction of expenses estimated at U.S.\$100,000.

The underwriters, as principals, conditionally offer the Notes, subject to prior sale, if, as and when issued by the Bank, and accepted by the underwriters in accordance with the conditions contained in the underwriting agreement referred to under “Plan of Distribution” in this Prospectus Supplement. The underwriters may sell Notes for less than the initial offering price in circumstances described under “Plan of Distribution.” In addition, the underwriters may effect transactions which stabilize or maintain the market price of the Notes at levels other than those that might otherwise prevail in the open market. Such transactions, if commenced, may be discontinued at any time. See “Plan of Distribution.”

The Notes will not constitute deposits that are insured under the *Canada Deposit Insurance Corporation Act (Canada)* or by the United States Federal Deposit Insurance Corporation or any other Canadian or U.S. government agency or instrumentality.

The principal executive office of the Bank is located at 1709 Hollis Street, Halifax, Nova Scotia, B3J 3B7 and its executive offices are at Scotia Plaza, 44 King Street West, Toronto, Ontario, M5H 1H1. The Notes will be ready for delivery through the book-entry facilities of The Depository Trust Company and its direct and indirect participants, including Euroclear Bank S.A./N.V. and Clearstream Banking, société anonyme, on or about April 25, 2013.

Joint Book-Running Managers

Citigroup Scotiabank Barclays
BofA Merrill Lynch J.P. Morgan
Co-Managers

Deutsche Bank Securities Goldman, Sachs & Co. HSBC
Morgan Stanley RBS Standard Chartered Bank
UBS Investment Bank Wells Fargo Securities

April 18, 2013

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ABOUT THIS PROSPECTUS SUPPLEMENT

This document consists of two parts. The first part is this Prospectus Supplement, which describes the specific terms of this offering. The second part, the accompanying Prospectus, gives more general information, some of which may not apply to this offering. If information in this Prospectus Supplement is inconsistent with the accompanying Prospectus, investors should rely on the information in this Prospectus Supplement. This Prospectus Supplement, the accompanying Prospectus and the documents incorporated by reference into each of them include important information about the Bank, the Notes being offered and other information investors should know before investing in the Notes.

Risk Factors

An investment in Notes of the Bank is subject to certain risks. Before deciding whether to invest in the Notes, investors should carefully consider the risks set out herein and incorporated by reference in this Prospectus Supplement (including subsequently filed documents incorporated by reference herein).

The value of the Notes will be affected by the general creditworthiness of the Bank. Prospective investors should consider the categories of risks identified in the Bank's most recent annual report filed on Form 40-F and quarterly report to shareholders filed on Form 6-K, which are incorporated by reference herein, including credit risk, market risk, liquidity risk, operational risk, reputational risk and environmental risk.

The Notes will be unsecured and unsubordinated obligations of the Bank and will rank on a parity with all of the Bank's other senior unsecured debt including deposit liabilities, other than certain governmental claims in accordance with applicable law. Except to the extent regulatory requirements affect the Bank's decisions to issue more senior debt, there is no limit on the Bank's ability to incur additional senior debt. Any payment to be made on the Notes depends on the ability of the Bank to satisfy its obligations as they come due. As a result, the actual and perceived creditworthiness of the Bank may affect the market value of the Notes and, in the event the Bank was to default on its obligations, holders of the Notes may not receive the amounts owed to them under the terms of the Notes.

Real or anticipated changes in credit ratings on the Bank's deposit liabilities may affect the market value of the Notes. In addition, real or anticipated changes in credit ratings can affect the cost at which the Bank can transact or obtain funding, and thereby affect the Bank's liquidity, business, financial condition or results of operations and, therefore, the Bank's ability to make payments on the Notes could be adversely affected.

The value of the Notes may be affected by market value fluctuations resulting from factors which influence the Bank's operations, including regulatory developments, competition and global market activity.

Prevailing interest rates will affect the market value of the Notes. Assuming all other factors remain unchanged, the market value of the Notes will decline as prevailing interest rates for similar debt instruments rise, and increase as prevailing interest rates for comparable debt instruments decline.

The Notes are a new issue of securities and there may be no market through which the Notes may be sold and purchasers may therefore be unable to resell such Notes. In addition, the Bank does not intend to apply for listing or quotation of the Notes on any securities exchange or automated quotation system. These factors may affect the pricing of the Notes in any secondary market, the transparency and availability of trading prices and the liquidity of the Notes.

There can be no assurance that an active trading market will develop for the Notes after this offering, or if developed, that such a market will be sustained at the offering price of the Notes. While certain of the underwriters intend to make a market in the Notes, the underwriters will not be obligated to do so and may stop their market-making at any time. In addition, any market-making activities will be

subject to limits of the U.S. Securities Act of 1933, as amended (the “Securities Act”), and the Exchange Act.

If any of the Notes are traded after their initial issuance, they may trade at a discount from their initial offering price. Future trading prices of the Notes will depend on many factors, including prevailing interest rates, the market for similar securities, general economic conditions and our financial condition, performance, prospects and other factors. Accordingly, you may be required to bear the financial risk of an investment in the Notes for an indefinite period of time.

The senior debt indenture governing the Notes does not contain any financial covenants and contains only limited restrictive covenants. In addition, the senior debt indenture will not limit the Bank’s or its subsidiaries’ ability to incur additional indebtedness, issue or repurchase securities, pay dividends or engage in transactions with affiliates. The Bank’s ability to incur additional indebtedness and use its funds for any purpose in the Bank’s discretion may increase the risk that the Bank may be unable to service its debt, including paying its obligations under the Notes.

The Notes and the related senior debt indenture will be governed by, and construed in accordance with, the laws of the State of New York (other than certain limited provisions that will be governed by the law of the Province of Ontario and applicable laws of Canada). Generally, in an action commenced in a Canadian court for the enforcement of the senior debt indenture or the Notes, a plaintiff will be required to prove those non-Canadian laws as a matter of fact by the evidence of persons who are experts in those laws.

This paragraph is relevant only if you are a fiduciary within the meaning of Section 3(21) of the U.S. Employee Retirement Income Security Act of 1974, as amended (“ERISA”) (including an insurance company and any fund manager treated as a fiduciary under the U.S. Department of Labor’s Regulations Section 2510.3-101 as modified by Section 3(42) of ERISA (the “Plan Asset Regulation”) of a pension or employee benefit plan (as defined in Section 3(3) of ERISA), including certain governmental, church and non-U.S. plans and IRAs and Keogh plans. These persons should consult with their counsel regarding the deemed representations they are required to make. See “Employee Retirement Income Security Act” in the accompanying Prospectus.

The Notes will be denominated in U.S. dollars. If you are a non-U.S. investor who purchases the Notes with a currency other than U.S. dollars, changes in rates of exchange may have an adverse effect on the value, price or returns of your investment. This Prospectus Supplement contains a general description of certain U.S. tax considerations and certain Canadian tax considerations relevant to Non-Resident Holders (as defined) relating to the Notes. If you are a non-U.S. investor, you should consult your tax advisors as to the consequences, under the tax laws of the country where you are resident for tax purposes, of acquiring, holding and disposing of the Notes and receiving the payments that might be due under the Notes.

We will have the right to redeem the Notes and if we redeem your Notes, depending on the market conditions at the time of redemption, you may not be able to reinvest the redemption proceeds in a security with a comparable return.

Foreign Account Tax Compliance Act Withholding

The U.S. “Foreign Account Tax Compliance Act” (or “FATCA”) imposes a new reporting regime and, potentially, a 30% withholding tax with respect to (i) certain payments from sources within the United States, (ii) “foreign passthru payments” made to certain non-U.S. financial institutions that do not comply with this new reporting regime, and (iii) payments to certain investors that do not provide identification information with respect to interests issued by a participating non-U.S. financial institution. The Bank is classified as a financial institution for these purposes. If an amount in respect of such withholding tax were to be deducted or withheld from interest, principal or other payments made in respect of the Notes, neither the Bank nor any paying agent nor any other person would, pursuant to the conditions of the Notes, be required to pay additional amounts as a result of the deduction or withholding. As a result, investors may receive less interest or principal than expected. Prospective investors should refer to the section “United

States Taxation—Foreign Account Tax Compliance Act Withholding.”

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Use of Proceeds

The net proceeds to the Bank from the sale of the Notes, after deducting the estimated expenses of the issue and the underwriters' discounts and commissions, will amount to approximately U.S.\$1,242,825,000. Such net proceeds will be added to the Bank's funds and will be used for general business purposes.

Details of the Offering

The following description of the terms of the Notes supplements, and to the extent inconsistent therewith replaces, the description set forth under the heading "Description of the Debt Securities We May Offer" in the accompanying Prospectus and should be read in conjunction with such description. As used in this description, the terms the "Bank," "we," "us" and "our" refer only to The Bank of Nova Scotia and not to any of its subsidiaries. All capitalized terms used under this heading "Details of the Offering" that are not defined herein have the meanings ascribed thereto in the accompanying Prospectus.

General

The following is a description of the terms of the U.S.\$1,250,000,000 1.450% Senior Notes due 2018 offered by this Prospectus Supplement (which are referred to in this Prospectus Supplement as the "Notes" and in the accompanying Prospectus as "Debt Securities"). The Notes are part of the Debt Securities registered by us with the SEC and which are to be issued on terms that will be determined at the time of sale. The Notes will constitute our unsecured and unsubordinated obligations and will constitute deposit liabilities of the Bank for purposes of the Bank Act and will rank on a parity with all of our other senior unsecured debt including deposit liabilities, other than certain governmental claims in accordance with applicable law, and prior to all of our subordinated debt. The Notes are to be issued under a senior debt indenture among us, Computershare Trust Company, N.A., as United States trustee, and Computershare Trust Company of Canada, as Canadian trustee, which is more fully described in the Prospectus under the heading "Description of the Debt Securities We May Offer."

Payment of the principal and interest on the Notes will be made in U.S. dollars. We will pay interest, principal and any other money due on the Notes at the corporate trust office of Computershare Trust Company, N.A., 350 Indiana St., Suite 750, Golden, Colorado 80401, or such other office as may be agreed upon. Holders of Notes must make arrangements to have their payments picked up at or wired from that office or such other office as may be agreed upon. We may also choose to pay interest by mailing checks.

The Notes are not entitled to the benefits of any sinking fund.

The provisions of the senior debt indenture relating to defeasance and covenant defeasance (described under the heading "Description of the Debt Securities We May Offer — Defeasance" in the accompanying Prospectus) will apply to the Notes.

The Notes will be issued in denominations of U.S.\$2,000 and integral multiples of U.S.\$1,000 in excess of such amount. Upon issuance, the Notes will be represented by one or more fully registered global notes. Each global note will be deposited with, or on behalf of, The Depository Trust Company, as depository. You may elect to hold interests in the global notes through either the depository (in the United States), Clearstream or Euroclear, or indirectly through organizations that are participants in such systems. See "Description of the Debt Securities We May Offer — Legal Ownership and Book-Entry Issuance" in the accompanying Prospectus.

Maturity

The Notes will mature on April 25, 2018.

Interest

The Notes will bear interest from and including April 25, 2013 at a rate equal to 1.450%. We will pay interest in arrears on April 25 and October 25 of each year, beginning October 25, 2013 (each, an “Interest Payment Date”), and on the maturity date. Interest will be payable on each Interest Payment Date to the persons in whose name the Notes are registered at the close of business on the preceding April 10 or October 10, whether or not a business day. However, we will pay interest on the maturity date to the same persons to whom the principal will be payable. If any Interest Payment Date or the maturity date falls on a day that is not a business day, we will postpone the making of such interest payment to the next succeeding business day (and no interest will be paid in respect of the delay). A “business day” means each Monday, Tuesday, Wednesday, Thursday or Friday that is not a day on which banking institutions are authorized or required by law or executive order to close in The City of New York, New York or Toronto, Ontario.

Interest on the Notes will accrue from and including April 25, 2013 to but excluding the first Interest Payment Date and then from and including each Interest Payment Date to which interest has been paid or duly provided for to, but excluding, the next Interest Payment Date or the maturity date, as the case may be.

Interest on the Notes will be computed on the basis of a 360-day year consisting of twelve 30-day months.

Payment of Additional Amounts

All payments made by or on behalf of the Bank under or with respect to the Notes will be made free and clear of and without withholding or deduction for or on account of any present or future tax, duty, levy, impost, assessment or other governmental charge (including penalties, interest and other liabilities related thereto) imposed or levied by or on behalf of the Government of Canada or any province or territory thereof or by any authority or agency therein or thereof having power to tax (hereafter “Canadian taxes”), unless the Bank is required to withhold or deduct Canadian taxes by law or by the interpretation or administration thereof. If the Bank is so required to withhold or deduct any amount for or on account of Canadian taxes from any payment made under or with respect to the Notes, we will pay to each holder of Notes as additional interest such additional amounts (“additional amounts”) as may be necessary so that the net amount received by each such holder after such withholding or deduction (and after deducting any Canadian taxes on such additional amounts) will not be less than the amount such holder would have received if such Canadian taxes had not been withheld or deducted, except as described below. However, no additional amounts will be payable with respect to a payment made to a holder (such holder, an “excluded holder”) in respect of the beneficial owner thereof:

- with which the Bank does not deal at arm’s length (for the purposes of the *Income Tax Act* (Canada)) at the time of the making of such payment;
- which is subject to such Canadian taxes by reason of the holder being a resident, domiciliary or national of, engaged in business or maintaining a permanent establishment or other physical presence in or otherwise having some connection with Canada or any province or territory thereof otherwise than by the mere holding of the Notes or the receipt of payments thereunder;
- which is subject to such Canadian taxes by reason of the holder’s failure to comply with any certification, identification, documentation or other reporting requirements if compliance is required by law, regulation, administrative practice or an applicable treaty as a precondition to exemption from, or a reduction in the rate of deduction or withholding of, such Canadian taxes (provided that the Bank advises the Trustees and the holders of the Notes then outstanding of any change in such requirements);
- with respect to any estate, inheritance, gift, sale, transfer, personal property or similar tax or other governmental charge; or

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which is a fiduciary or partnership or person other than the sole beneficial owner of such payment to the extent that the Canadian taxes would not have been imposed on such payment had such holder been the sole beneficial owner of such Notes.

The Bank will also:

make such withholding or deduction; and

remit the full amount deducted or withheld to the relevant authority in accordance with applicable law.

The Bank will furnish to the holders of the Notes, within 60 days after the date the payment of any Canadian taxes is due pursuant to applicable law, certified copies of tax receipts or other documents evidencing such payment by such person.

The Bank will indemnify and hold harmless each holder of Notes (other than an excluded holder) from and against, and upon written request reimburse each such holder for the amount (excluding any additional amounts that have previously been paid by the Bank with respect thereto) of:

any Canadian taxes so levied or imposed and paid by such holder as a result of payments made by or on behalf of the Bank under or with respect to the Notes;

any liability (including penalties, interest and expenses) arising therefrom or with respect thereto; and

any Canadian taxes imposed with respect to any reimbursement under the preceding two bullet points, but excluding any such Canadian taxes on such holder's net income.

In any event, no additional amounts or indemnity amounts will be payable under the provisions described above in respect of any Note in excess of the additional amounts and the indemnity amounts which would be required if, at all relevant times, the holder of such Note were a resident of the United States for purposes of and was entitled to the benefits of the Canada-U.S. Income Tax Convention (1980), as amended, including any protocols thereto. As a result of the limitation on the payment of additional amounts and indemnity amounts discussed in the preceding sentence, the additional amounts or indemnity amounts received by certain holders of Notes may be less than the amount of Canadian taxes withheld or deducted or the amount of Canadian taxes (and related amounts) levied or imposed giving rise to the obligation to pay the indemnity amounts, as the case may be, and, accordingly, the net amount received by such holders of Notes will be less than the amount such holders would have received had there been no such withholding or deduction in respect of Canadian taxes or had such Canadian taxes (and related amounts) not been levied or imposed.

Wherever in the senior debt indenture governing the terms of the Notes there is mentioned, in any context, the payment of principal, interest, if any, or any other amount payable under or with respect to a Note, such mention shall be deemed to include mention of the payment of additional amounts to the extent that, in such context, additional amounts are, were or would be payable in respect thereof.

In the event of the occurrence of any transaction or event resulting in a successor to the Bank, all references to Canada in the preceding paragraphs of this subsection shall be deemed to be references to the jurisdiction of organization of the successor entity.

Payments of principal and interest in respect of the Notes are subject in all cases to any withholding or deduction required pursuant to an agreement described in Section 1471(b) of the U.S. Internal Revenue Code of 1986 (the Code) or otherwise imposed pursuant to Sections 1471 through 1474 of the Code, any regulations or agreements thereunder, official interpretations thereof, or any law implementing an intergovernmental approach thereto.

Tax Redemption

The Bank (or its successor) may redeem the Notes, in whole but not in part, at a redemption price equal to the principal amount thereof together with accrued and unpaid interest to the date fixed for redemption, upon the giving of a notice as described below, if:

as a result of any change (including any announced prospective change) in or amendment to the laws (or any regulations or rulings promulgated thereunder) of Canada (or the jurisdiction of organization of the successor to the Bank) or of any political subdivision or taxing authority thereof or therein affecting taxation, or any change in official position regarding the application or interpretation of such laws, regulations or rulings (including a holding by a court of competent jurisdiction), which change or amendment is announced or becomes effective on or after the date of this Prospectus Supplement (or, in the case of a successor to the Bank, after the date of succession), and which in the written opinion to the Bank (or its successor) of legal counsel of recognized standing has resulted or will result (assuming, in the case of any announced prospective change, that such announced change will become effective as of the date specified in such announcement and in the form announced) in the Bank (or its successor) becoming obligated to pay, on the next succeeding date on which interest is due, additional amounts with respect to the Notes as described under “ — Payment of Additional Amounts;” or on or after the date of this Prospectus Supplement (or, in the case of a successor to the Bank, after the date of succession), any action has been taken by any taxing authority of, or any decision has been rendered by a court of competent jurisdiction in, Canada (or the jurisdiction of organization of the successor to the Bank) or any political subdivision or taxing authority thereof or therein, including any of those actions specified in the paragraph immediately above, whether or not such action was taken or decision was rendered with respect to the Bank (or its successor), or any change, amendment, application or interpretation shall be officially proposed, which, in any such case, in the written opinion to the Bank (or its successor) of legal counsel of recognized standing, will result (assuming that such change, amendment, application, interpretation or action is applied to the Notes by the taxing authority and that, in the case of any announced prospective change, such announced change will become effective as of the date specified in such announcement and in the form announced) in the Bank (or its successor) becoming obligated to pay, on the next succeeding date on which interest is due, additional amounts with respect to the Notes; and, in any such case, the Bank (or its successor), in its business judgment, determines that such obligation cannot be avoided by the use of reasonable measures available to it (or its successor).

In the event the Bank elects to redeem the Notes pursuant to the provisions set forth in the preceding paragraph, it shall deliver to the Trustees a certificate, signed by an authorized officer, stating (i) that the Bank is entitled to redeem such Notes pursuant to their terms and (ii) the principal amount of the Notes to be redeemed.

Notice of intention to redeem such Notes will be given to holders of the Notes not more than 45 nor less than 30 days prior to the date fixed for redemption and such notice will specify, among other things, the date fixed for redemption and the redemption price.

Further Issues

We may from time to time, without notice to or the consent of the registered holders of the Notes, create and issue further notes ranking *pari passu* with the Notes in all respects (or in all respects except for the payment of interest accruing prior to the issue date of such further notes or except for the first payment of interest following the issue date of such further notes) and so that such further notes may be consolidated and form a single series with the Notes and have the same terms as to status or otherwise as the Notes.

Certain U.S. Federal Income Tax Considerations

Prospective investors should refer to the section “United States Taxation” in the Prospectus for a discussion of the material United States federal income tax consequences to a United States holder (as defined therein).

In addition, the following sections replace the corresponding sections in the Prospectus:

Information with Respect to Foreign Financial Assets

Certain holders that own “specified foreign financial assets” with an aggregate value in excess of U.S.\$50,000 on the last day of the taxable year (or an aggregate value in excess of U.S.\$75,000 at any time during the taxable year) will generally be required to file an information report with respect to such assets with their tax returns. “Specified foreign financial assets” include any financial accounts maintained by foreign financial institutions, as well as any of the following, but only if they are not held in accounts maintained by financial institutions: (i) stock or securities issued by non–United States persons, (ii) financial instruments and contracts held for investment that have non–United States issuers or counterparties, and (iii) interests in foreign entities. The securities may be subject to these rules. United States holders are urged to consult their tax advisors regarding the application of this legislation to their ownership of the securities.

Foreign Account Tax Compliance Act Withholding

Sections 1471 through 1474 of the U.S. Internal Revenue Code of 1986 (“FATCA”) impose a new reporting regime and potentially a 30% withholding tax with respect to certain payments to (i) any non-U.S. financial institution (a “foreign financial institution”, or “FFI” (as defined by FATCA)) that does not become a “Participating FFI” by entering into an agreement with the U.S. Internal Revenue Service (“IRS”) to provide the IRS with certain information in respect of its account holders and investors or is not otherwise exempt from or in deemed compliance with FATCA and (ii) any investor (unless otherwise exempt from FATCA) that does not provide information sufficient to determine whether the investor is a U.S. person or should otherwise be treated as holding a “United States Account” (a “Recalcitrant Holder”). The Bank is classified as an FFI.

The new withholding regime will be phased in beginning January 1, 2014 for payments from sources within the United States and will apply to “foreign passthru payments” (a term not yet defined) no earlier than January 1, 2017. This withholding would potentially apply to payments in respect of any Notes that are issued on or after the “grandfathering date,” which is the later of (a) January 1, 2014 and (b) the date that is six months after the date on which final U.S. Treasury regulations defining the term foreign passthru payment are filed with the Federal Register, or which are materially modified on or after the grandfathering date. If Notes are issued before the grandfathering date, and additional Notes of the same series are issued on or after that date, the additional Notes may not be treated as grandfathered, which may have negative consequences for the existing Notes, including a negative impact on market price.

The United States and a number of other jurisdictions have announced their intention to negotiate intergovernmental agreements to facilitate the implementation of FATCA (each, an “IGA”). Pursuant to FATCA and the “Model 1” and

“Model 2” IGAs released by the United States, an FFI in an IGA signatory country could be treated as a “Reporting FI” not subject to withholding under FATCA on any payments it receives. Further, an FFI in a Model 1 IGA jurisdiction would not be required to withhold under FATCA or an IGA (or any law implementing an IGA) (any such withholding being “FATCA Withholding”) from

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payments it makes (unless it has agreed to do so under the U.S. “qualified intermediary,” “withholding foreign partnership,” or “withholding foreign trust” regimes). The Model 2 IGA leaves open the possibility that a Reporting FI might in the future be required to withhold as a Participating FFI on foreign passthru payments and payments that it makes to Recalcitrant Holders. Under each Model IGA, a Reporting FI would still be required to report certain information in respect of its account holders and investors to its home government or to the IRS. The United States and Canada have indicated an intention to enter into an agreement (a “US-Canada IGA”) however no assurance can be given that the United States and Canada will enter into such an agreement.

The Bank expects to be treated as a Reporting FI pursuant to a U.S.-Canada IGA and does not anticipate being obliged to deduct any FATCA Withholding on payments it makes. There can be no assurance, however, that the Bank will be treated as a Reporting FI, or that it would in the future not be required to deduct FATCA Withholding from payments it makes. Accordingly, the Bank and financial institutions through which payments on the Notes are made may be required to withhold FATCA Withholding if (i) any FFI through or to which payment on such Notes is made is not a Participating FFI, a Reporting FI, or otherwise exempt from or in deemed compliance with FATCA or (ii) an investor is a Recalcitrant Holder.

If an amount in respect of FATCA Withholding were to be deducted or withheld from interest, principal or other payments made in respect of the Notes, neither the Bank nor any paying agent nor any other person would, pursuant to the conditions of the Notes, be required to pay additional amounts as a result of the deduction or withholding. As a result, investors may receive less interest or principal than expected.

FATCA is particularly complex and its application is uncertain at this time. The above description is based in part on regulations, official guidance and model IGAs, all of which are subject to change or may be implemented in a materially different form.

Certain Canadian Federal Income Tax Considerations

The following is a summary of the principal Canadian federal income tax considerations generally applicable to a purchaser who acquires, as beneficial owner, Notes, including entitlements to all payments thereunder, pursuant to this offering and who, at all relevant times, for purposes of the application of the *Income Tax Act* (Canada) and the Income Tax Regulations (collectively, the “Act”) is not, and is not deemed to be, resident in Canada, deals at arm’s length with the Bank and with any transferee resident (or deemed to be resident) in Canada to whom the purchaser disposes of the Notes, does not use or hold the Notes in a business carried on in Canada, is not a “specified shareholder” and is not a person who does not deal at arm’s length with a “specified shareholder” (as defined for purposes of subsection 18(5) of the Act) of the Bank and does not receive any payment of interest on the Notes in respect of a debt or other obligation to pay an amount to a person with whom the Bank does not deal at arm’s length (a “Non-Resident Holder”). Special rules, which are not discussed in this summary, may apply to a Non-Resident Holder that is an insurer that carries on an insurance business in Canada and elsewhere.

This summary is based upon the current provisions of the Act and an understanding of the current administrative practices and assessing policies of the Canada Revenue Agency published in writing prior to the date hereof. This summary takes into account all specific proposals to amend the Act publicly announced by or on behalf of the Minister of Finance prior to the date hereof (the “Proposals”) and assumes that all Proposals will be enacted in the form proposed. However, no assurance can be given that the Proposals will be enacted as proposed or at all. This summary does not otherwise take into account any changes in law or in administrative practices or assessing policies, whether by legislative, administrative or judicial action, nor does it take into account any provincial, territorial or foreign income tax considerations, which may differ from those discussed herein.

This summary is of a general nature only and is not intended to be legal or tax advice to any particular purchaser. This summary is not exhaustive of all Canadian federal income tax considerations. Accordingly,

prospective purchasers should consult their own tax advisors with respect to their particular circumstances.

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No Canadian withholding tax will apply to interest or principal paid or credited to a Non-Resident Holder by the Bank or to proceeds received by a Non-Resident Holder on the disposition of a Note, including on a redemption, payment on maturity, repurchase or purchase for cancellation.

No other tax on income or gains will be payable by a Non-Resident Holder on interest or principal, or on proceeds received by a holder on the disposition of a Note, including on a redemption, payment on maturity, repurchase or purchase for cancellation.

Plan Of Distribution (Conflicts of Interest)

Under the terms and subject to the conditions contained in an underwriting agreement dated the date of this Prospectus Supplement, the underwriters listed in the table below have severally agreed to purchase, and we have agreed to sell to them, the principal amount of the Notes set forth opposite each underwriter's name below.

Total

| Underwriter | Principal Amount of Notes |
|-------------------------------------------------------|--------------------------------------|
| Citigroup Global Markets Inc. | U.S.\$ 775,000,000 |
| Scotia Capital (USA) Inc. | 775,000,000 |
| Barclays Capital Inc. | 700,000,000 |
| Merrill Lynch, Pierce, Fenner & Smith Incorporated | 187,500,000 |
| J.P. Morgan Securities LLC | 162,500,000 |
| Deutsche Bank Securities Inc. | 75,000,000 |
| Goldman, Sachs & Co. | 75,000,000 |
| HSBC Securities (USA) Inc. | 75,000,000 |
| Morgan Stanley & Co. LLC | 75,000,000 |
| RBS Securities Inc. | 12,500,000 |
| Standard Chartered Bank | 12,500,000 |
| UBS Securities LLC | 12,500,000 |
| Wells Fargo Securities, LLC | 12,500,000 |
| Total | U.S.\$ 1,250,000,000 |

The Notes are being offered by the underwriters subject to approval of legal matters by counsel for the underwriters and other conditions. The underwriting agreement provides that the underwriters are obligated to purchase all of the Notes if any are purchased. The underwriting agreement also provides that if an underwriter defaults, the purchase commitments of the non-defaulting underwriters may also be increased or the offering may be terminated.

The underwriters propose initially to offer the Notes to the public at the public offering price on the cover page of this Prospectus Supplement, and may offer the Notes to dealers at that price less a concession not in excess of 0.210% of the principal amount per Note. The underwriters may allow, and the dealers may reallow, a discount not in excess of 0.125% of the principal amount of the Notes to other dealers. After the initial public offering of the Notes, the underwriters may change the public offering price and discount to broker-dealers.

The expenses of the offering, not including the underwriting commissions, are estimated to be U.S.\$100,000 and are payable by the Bank.

The Notes are a new issue of securities with no established trading market. The underwriters intend to make a secondary market for the Notes. However, they are not obligated to do so and may discontinue making a secondary market for the Notes at any time without notice. If a trading market develops, no assurance can be given as to how liquid that trading market for the Notes will be.

The Bank has agreed to indemnify the underwriters against liabilities under the Securities Act, or contribute to payments that the underwriters may be required to make in that respect.

In connection with this offering, the underwriters may engage in stabilizing transactions, syndicate covering transactions and penalty bids in accordance with Regulation M under the Exchange Act. Stabilizing transactions permit bids to purchase the underlying security so long as the stabilizing bids do not exceed a specified maximum. Syndicate covering transactions involve purchases of the Notes in the open market after the distribution has been completed in order to cover syndicate short positions. A short position is more likely to be created if the underwriters are concerned that there may be downward pressure on the price of the Notes in the open market after pricing that could adversely affect investors who

purchase in the offering. Penalty bids permit the underwriters to reclaim a selling concession from a broker-dealer when the Notes originally sold by such broker/dealer are purchased in a stabilizing or covering transaction to cover short positions.

These stabilizing transactions, syndicate covering transactions and penalty bids may have the effect of raising or maintaining the market price of the Notes or preventing or retarding a decline in the market price of the Notes. As a result, the price of the Notes may be higher than the price that might otherwise exist in the open market. These transactions, if commenced, may be discontinued at any time.

In compliance with the guidelines of the Financial Industry Regulatory Authority (“FINRA”), the maximum commission or discount to be received by any FINRA member or independent broker-dealer may not exceed 8% of the aggregate principal amount of the Notes offered pursuant to this Prospectus Supplement. It is anticipated that the maximum commission or discount to be received in any particular offering of Notes will be significantly less than this amount.

In the ordinary course of business, the underwriters and their affiliates have provided financial advisory, investment banking and general financing and banking services for the Bank for customary fees. The underwriters and/or their affiliates may provide such services to the Bank in the future.

We expect that delivery of the Notes will be made against payment therefor on or about the fifth business day following the date of pricing of the Notes (this settlement cycle being referred to as “T+5”). Under Rule 15c6-1 of the Exchange Act, trades in the secondary market generally are required to settle in three business days, unless the parties to any such trade expressly agree otherwise. Accordingly, purchasers who wish to trade their Notes on the date of pricing or the next succeeding business day will be required, by virtue of the fact that the Notes initially will settle in T+5, to specify an alternate settlement cycle at the time of any such trade to prevent a failed settlement. Purchasers of Notes who wish to trade their Notes on the date of pricing or the next succeeding business day should consult their own advisor.

Conflicts of Interest

Because Scotia Capital (USA) Inc. is an affiliate of the Bank and is participating in the distribution of the Notes in this offering as an underwriter, Scotia Capital (USA) Inc. has a “conflict of interest” as defined in FINRA Rule 5121. Consequently, this offering is being conducted in compliance with FINRA Rule 5121. Pursuant to that rule, the appointment of a qualified independent underwriter is not necessary in connection with this offering, as the offering is of a class of securities rated Baa or better by Moody’s rating service or BBB or better by Standard & Poor’s rating service or rated in a comparable category by another rating service acceptable to FINRA. Scotia Capital (USA) Inc. is not permitted to sell Notes in this offering to accounts over which discretionary control is exercised without the prior specific written authority of the accountholder.

Offering Restrictions

This Prospectus Supplement does not constitute an offer of the Notes, directly or indirectly, in Canada or to residents of Canada. Each underwriter has represented and agreed that it has not offered or sold, directly or indirectly, and that it will not, directly or indirectly, offer, sell or deliver, any of the Notes in or from Canada or to any resident of Canada. Each underwriter has also agreed that it will include a comparable provision in any sub-underwriting, banking group or selling group agreement or similar arrangement with respect to the Notes that may be entered into by such underwriter.

Standard Chartered Bank will not effect any offers or sales of any Notes in the United States unless it is through one or more U.S. registered broker-dealers as permitted by the regulations of FINRA.

European Economic Area

Public offer selling restriction under the Prospectus Directive.

In relation to each Member State of the European Economic Area which has implemented the Prospectus Directive (each, a “Relevant Member State”), each Underwriter has represented and agreed that with effect from and including the date on which the Prospectus Directive is implemented in that Relevant Member State (the “Relevant Implementation Date”), it has not made and will not make an offer of Notes which are the subject of the offering contemplated by the Prospectus Supplement to the public in that Relevant Member State except that it may, with effect from and including the Relevant Implementation Date, make an offer of such Notes to the public in that Relevant Member State (a) at any time to any legal entity which is a qualified investor as defined in the Prospectus Directive; (b) at any time to fewer than 100, or, if the Relevant Member State has implemented the relevant provision of the 2010 PD Amending Directive, 150 natural or legal persons (other than qualified investors as defined in the Prospectus

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Directive), as permitted under the Prospectus Directive, subject to obtaining the prior consent of the relevant Manager or Managers nominated by the Issuer for any such offer; or (c) at any time in any other circumstances falling within Article 3(2) of the Prospectus Directive, provided that that no such offer of Notes referred to in (a) to (c) above shall require the Issuer or any Underwriter to publish a prospectus pursuant to Article 3 of the Prospectus Directive, or supplement a prospectus pursuant to Article 16 of the Prospectus Directive.

For the purposes of this provision, the expression an “offer of Notes to the public” in relation to any Notes in any Relevant Member State means the communication in any form and by any means of sufficient information on the terms of the offer and the Notes to be offered so as to enable an investor to decide to purchase or subscribe the Notes, as the same may be varied in that Member State by any measure implementing the Prospectus Directive in that Member State; the expression “Prospectus Directive” means Directive 2003/71/EC (and amendments thereto, including the 2010 PD Amending Directive, to the extent implemented in the Relevant Member State), and includes any relevant implementing measure in the Relevant Member State; and the expression “2010 PD Amending Directive” means Directive 2010/73/EU.

United Kingdom

This Prospectus Supplement and the accompanying Prospectus are only being distributed to, and are only directed at, persons in the United Kingdom that are qualified investors within the meaning of Article 2(1)(e) of the Prospectus Directive that are also (i) investment professionals falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (the “Order”) or (ii) high net worth entities, and other persons to whom it may lawfully be communicated, falling within Article 49(2)(a) to (d) of the Order (each such person being referred to as a “Relevant Person”). This Prospectus Supplement and the accompanying Prospectus and its contents are confidential and should not be distributed, published or reproduced (in whole or in part) or disclosed by recipients to any other persons in the United Kingdom. Any person in the United Kingdom that is not a Relevant Person should not act or rely on this document or any of its contents.

Hong Kong

The Notes may not be offered or sold in Hong Kong by means of any document other than (i) in circumstances which do not constitute an offer to the public within the meaning of the Companies Ordinance (Cap. 32, Laws of Hong Kong), or (ii) to “professional investors” within the meaning of the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made thereunder, or (iii) in other circumstances which do not result in the document being a “prospectus” within the meaning of the Companies Ordinance (Cap. 32, Laws of Hong Kong) and no advertisement, invitation or document relating to the Notes may be issued or may be in the possession of any person for the purpose of issue (in each case whether in Hong Kong or elsewhere), which is directed at, or the contents of which are likely to be accessed or read by, the public in Hong Kong (except if permitted to do so under the laws of Hong Kong) other than with respect to Notes which are or are intended to be disposed of only to persons outside Hong Kong or only to “professional investors” within the meaning of the Securities and Futures Ordinance (Cap. 571, Laws of Hong Kong) and any rules made thereunder.

Japan

The Notes offered in this Prospectus Supplement have not been registered under the Securities and Exchange Law of Japan. The Notes have not been offered or sold and will not be offered or sold, directly or indirectly, in Japan or to or for the account of any resident of Japan, except (i) pursuant to an exemption from the registration requirements of the Securities and Exchange Law and (ii) in compliance with any other applicable requirements of Japanese law.

Singapore

This Prospectus Supplement and the accompanying Prospectus have not been registered as a Prospectus with the Monetary Authority of Singapore. Accordingly, this Prospectus Supplement, the accompanying Prospectus, and any other document or material in connection with the offer or sale, or

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invitation for subscription or purchase, of the Notes may not be circulated or distributed, nor may the Notes be offered or sold, or be made the subject of an invitation for subscription or purchase, whether directly or indirectly, to persons in Singapore other than (i) to an institutional investor under Section 274 of the Securities and Futures Act, Chapter 289 of Singapore (the "SFA"), (ii) to a relevant person pursuant to Section 275(1), or any person pursuant to Section 275(1A), and in accordance with the conditions specified in Section 275 of the SFA or (iii) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA, in each case subject to compliance with conditions set forth in the SFA.

Where the Notes are subscribed or purchased under Section 275 of the SFA by a relevant person which is:

a corporation (which is not an accredited investor (as defined in Section 4A of the SFA)) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor; or

a trust (where the trustee is not an accredited investor) whose sole purpose is to hold investments and each beneficiary of the trust is an individual who is an accredited investor, shares, debentures and units of shares and debentures of that corporation or the beneficiaries' rights and interest (howsoever described) in that trust shall not be transferred within six months after that corporation or that trust has acquired the Notes pursuant to an offer made under Section 275 of the SFA except:

to an institutional investor (for corporations, under Section 274 of the SFA) or to a relevant person defined in Section 275(2) of the SFA, or to any person pursuant to an offer that is made on terms that such shares, debentures and units of shares and debentures of that corporation or such rights and interest in that trust are acquired at a consideration of not less than U.S.\$200,000 (or its equivalent in a foreign currency) for each transaction, whether such amount is to be paid for in cash or by exchange of securities or other assets, and further for corporations, in accordance with the conditions specified in Section 275 of the SFA;

where no consideration is or will be given for the transfer; or

where the transfer is by operation of law.

Legal Matters

Certain legal matters in connection with the offering of the Notes will be passed upon, on behalf of the Bank, by Allen & Overy LLP, the Bank's U.S. counsel, and Osler, Hoskin & Harcourt LLP, the Bank's Canadian counsel. Certain legal matters will be passed upon for the underwriters by Morrison & Foerster LLP, the underwriters' U.S. counsel.

Independent Registered Public Accounting Firm

KPMG LLP, Chartered Accountants, Toronto, Ontario, is the external auditor who prepared the Auditors' Report to Shareholders with respect to the consolidated statement of financial position of the Bank as at October 31, 2012, October 31, 2011 and November 1, 2010 and the consolidated statements of income, comprehensive income, changes in equity and cash flows for each of the years in the two-year period ended October 31, 2012 and notes, comprising a summary of significant accounting policies and other explanatory information. KPMG LLP is independent with respect to the Bank within the meaning of the Rules of Professional Conduct of the Institute of Chartered Accountants of Ontario and within the meaning of the Securities Act and the applicable rules and regulations thereunder.

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Common Shares

Preferred Shares

Senior Debt Securities

Subordinated Debt Securities

up to an aggregate initial offering price of U.S.\$18,000,000,000

or the equivalent thereof in other currencies.

The Bank of Nova Scotia (the **Bank**) may from time to time offer and issue common shares, preferred shares, senior debt securities or subordinated debt securities.

The securities offered hereby may be offered separately or together, in amounts, at prices and on terms to be set forth in an accompanying prospectus supplement. Information as to a particular offering that is omitted from this prospectus will be contained in one or more prospectus supplements that will be delivered to purchasers together with this prospectus. The Bank may sell up to U.S.\$18,000,000,000 in aggregate initial offering price of the securities (or the U.S. dollar equivalent thereof if any of the securities are denominated in a currency or currency unit other than U.S. dollars) during the period that this prospectus, including any amendments thereto, remains valid. The specific terms of the securities in respect of which this prospectus is being delivered will be set forth in the applicable prospectus supplement and may include, where applicable, the specific designation, aggregate principal amount, the currency or the currency unit for which the securities may be purchased, maturity, interest provisions, authorized denominations, offering price, any terms for redemption at the option of the Bank or the holder, any exchange or conversion terms and any other specific terms.

The securities may be sold through underwriters or dealers purchasing as principals, through agents designated by the Bank (such underwriters, dealers and agents are collectively referred to in this prospectus as **investment dealers** and individually as an **investment dealer**) or by the Bank directly pursuant to applicable statutory exemptions, from time to time. See **Plan of Distribution**. Each prospectus supplement will identify each investment dealer engaged in connection with the offering and sale of those securities to which the prospectus supplement relates, and will also set forth the terms of the offering of such securities, including the net proceeds to the Bank and, to the extent applicable, any fees payable to the investment dealers.

The common shares of the Bank are listed on the New York Stock Exchange and the Toronto Stock Exchange under the symbol **BNS**.

The head office of the Bank is located at 1709 Hollis Street, Halifax, Nova Scotia, B3J 3B7 and its executive offices are located at Scotia Plaza, 44 King Street West, Toronto, Ontario, M5H 1H1.

You should read this prospectus and any applicable prospectus supplement carefully before you invest in any of the securities of the Bank.

Investing in these securities involves certain risks. To read about certain factors you should consider before buying any of the securities, see the Risk Factors section on page 6 of this prospectus and in the most recent annual report on Form 40-F of the Bank, which is incorporated by reference herein, as well as any other reports on Form 6-K that are specifically incorporated by reference herein and, if any, in an applicable prospectus supplement.

NEITHER THE SECURITIES AND EXCHANGE COMMISSION (THE SEC) NOR ANY STATE SECURITIES COMMISSION HAS APPROVED OR DISAPPROVED OF THESE SECURITIES OR PASSED UPON THE ADEQUACY OR ACCURACY OF THIS PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

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Prospective investors should be aware that the acquisition of the securities described herein may have tax consequences both in the United States and in Canada. Such consequences for investors who are resident in, or citizens of, Canada or the United States may not be described fully herein or in any applicable prospectus supplement.

The enforcement by investors of civil liabilities under the United States federal securities laws may be affected adversely by the fact that the Bank is a Canadian bank, that many of its officers and directors, and some or all of the underwriters or experts named in this prospectus, may be residents of Canada and that all or a substantial portion of the assets of the Bank and such persons may be located outside the United States.

The securities will not constitute deposits that are insured under the Canada Deposit Insurance Corporation Act or by the United States Federal Deposit Insurance Corporation or any other Canadian or U.S. government agency or instrumentality.

This prospectus is dated December 28, 2012.

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ABOUT THIS PROSPECTUS

General

This document is called a prospectus and is part of a registration statement that we filed with the SEC using a shelf registration or continuous offering process. Under this shelf registration, we may from time to time sell any combination of the securities described in this prospectus in one or more offerings. The registration statement containing this prospectus, including exhibits to the registration statement, provides additional information about us and the securities offered under this prospectus. The registration statement can be read at the SEC website or at the SEC offices mentioned under the heading **Where You Can Find More Information**.

This prospectus provides you with a general description of the securities we may offer. Each time we sell securities under this shelf registration statement we will provide one or more supplements to this prospectus containing specific information about the terms of the securities being offered. Any such supplements, which we refer to in this prospectus as the applicable prospectus supplements, may include a discussion of any additional risk factors or other special considerations that apply to those securities and may also add to, update or change the information in this prospectus. The applicable prospectus supplements relating to each series of securities will be attached to the front of this prospectus. If there is any inconsistency between the information in this prospectus and any applicable prospectus supplement, you should rely on the information in the most recent applicable prospectus supplement. We urge you to read carefully both this prospectus and any applicable prospectus supplement accompanying this prospectus, together with the information incorporated herein and in any applicable prospectus supplement by reference under the heading **Where You Can Find More Information**, before deciding whether to invest in any of the securities being offered.

When acquiring any securities discussed in this prospectus, you should rely only on the information provided in this prospectus and the applicable prospectus supplements, including the information incorporated by reference. We have not authorized anyone to give any information or to make any representation different from or in addition to that contained or incorporated by reference in this prospectus and any applicable prospectus supplement. Therefore, if anyone does give you such different information, you should not rely on it. If you are in a jurisdiction where offers to sell, or solicitations of offers to purchase, the securities offered by this prospectus are unlawful, or if you are a person to whom it is unlawful to direct these types of activities, then the offer presented in this prospectus does not extend to you. The information contained in this prospectus speaks only as of the date of this prospectus unless the information specifically indicates that another date applies. Therefore, you should not assume that the information contained in this prospectus or applicable prospectus supplement is accurate on any date subsequent to the date set forth on the front of the document or that any information we have incorporated by reference is correct on any date subsequent to the date of the document incorporated by reference, even though this prospectus and any applicable prospectus supplement is delivered or securities are sold on a later date.

We may sell securities to underwriters who will sell the securities to the public on terms fixed at the time of sale. In addition, the securities may be sold by us directly or through dealers or agents designated from time to time, which may be our affiliates. If we, directly or through dealers or agents, solicit offers to purchase the securities, we reserve the sole right to accept and, together with the applicable dealers or agents, to reject, in whole or in part, any of those offers. An applicable prospectus supplement will contain the names of the underwriters, dealers or agents, if any, together with the terms of offering, the compensation of those persons and the net proceeds to us. Any underwriters, dealers or agents participating in the offering may be deemed underwriters within the meaning of the Securities Act of 1933, as amended (the **Securities Act**).

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International Financial Reporting Standards (IFRS) replaced Canadian generally accepted accounting principles (GAAP) for publicly accountable enterprises beginning in 2011. For the Bank, IFRS became effective for interim and annual periods commencing November 1, 2011 (adoption date), and include the preparation and reporting of one year of comparative figures, including an opening balance sheet as of November 1, 2010 (transition date). For additional information regarding the Bank's adoption of IFRS, see the sections entitled First-time adoption of IFRS and Explanation of significant adjustments from Canadian GAAP to IFRS in our Annual Report on Form 40-F for the fiscal year ended October 31, 2012.

Additionally, the Bank publishes its consolidated financial statements in Canadian dollars. In this prospectus and any prospectus supplement, currency amounts are stated in Canadian dollars, unless specified otherwise. References to \$, Cdn\$ and dollars are to Canadian dollars, and references to U.S.\$ are to U.S. dollars.

The tables below set forth the high and low daily noon buying rates, the average yearly rate and the rate at period end between Canadian dollars and U.S. dollars (in U.S. dollars per Canadian dollar) for the five-year period ended October 31, 2012 and the high and low daily noon buying rates for the month of November 2012 and the period December 1, 2012 through December 14, 2012. On December 14, 2012, the noon buying rate was U.S.\$1.00 = \$1.01. Our reference to the noon buying rate is the inverse of the rate in The City of New York for cable transfers in foreign currencies as announced by the U.S. Federal Reserve Bank of New York for customs purposes on a specified date.

| Year Ended October 31, | High | Low | Average Rate⁽¹⁾ | At Period End |
|-------------------------------|-------------|------------|-----------------------------------|----------------------|
| 2008 | 1.0908 | 0.7727 | 0.9720 | 0.8225 |
| 2009 | 0.9719 | 0.7695 | 0.8605 | 0.9288 |
| 2010 | 1.0040 | 0.9280 | 0.9604 | 0.9816 |
| 2011 | 1.0584 | 0.9430 | 1.0159 | 1.0068 |
| 2012 | 1.0299 | 0.9536 | 0.9969 | 1.0006 |

| Month of 2012 | High | Low |
|--------------------------------|-------------|------------|
| November | 1.0074 | 0.9971 |
| December (through December 14) | 1.0157 | 1.0072 |

(1) The average of the noon buying rates on the last business day of each full month during the relevant period.

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The Bank's public communications often include oral or written forward-looking statements. Statements of this type are included in this document, and may be included in other filings with Canadian securities regulators or the SEC, or in other communications. All such statements are made pursuant to the "safe harbor" provisions of the United States Private Securities Litigation Reform Act of 1995 and any applicable Canadian securities legislation. Forward-looking statements may include comments with respect to the Bank's objectives, strategies to achieve those objectives, expected financial results (including those in the area of risk management), and the outlook for the Bank's businesses and for the Canadian, United States and global economies. Such statements are typically identified by words or phrases such as "believe," "expect," "anticipate," "intent," "estimate," "plan," "may increase," "may fluctuate," and similar expressions of future or conditional verbs, such as "will," "should," and "could."

By their very nature, forward-looking statements involve numerous assumptions, inherent risks and uncertainties, both general and specific, and the risk that predictions and other forward-looking statements will not prove to be accurate. Do not unduly rely on forward-looking statements, as a number of important factors, many of which are beyond the Bank's control, could cause actual results to differ materially from the estimates and intentions expressed in such forward-looking statements. These factors include, but are not limited to: the economic and financial conditions in Canada and globally; fluctuations in interest rates and currency values; liquidity; significant market volatility and interruptions; the failure of third parties to comply with their obligations to the Bank and its affiliates; the effect of changes in monetary policy; legislative and regulatory developments in Canada and elsewhere, including changes in tax laws; the effect of changes to the Bank's credit ratings; amendments to, and interpretations of, risk-based capital guidelines and reporting instructions and liquidity regulatory guidance; operational and reputational risks; the risk that the Bank's risk management models may not take into account all relevant factors; the accuracy and completeness of information the Bank receives on customers and counterparties; the timely development and introduction of new products and services in receptive markets; the Bank's ability to expand existing distribution channels and to develop and realize revenues from new distribution channels; the Bank's ability to complete and integrate acquisitions and its other growth strategies; changes in accounting policies and methods the Bank uses to report its financial condition and financial performance, including uncertainties associated with critical accounting assumptions and estimates; the effect of applying future accounting changes; global capital markets activity; the Bank's ability to attract and retain key executives; reliance on third parties to provide components of the Bank's business infrastructure; unexpected changes in consumer spending and saving habits; technological developments; fraud by internal or external parties, including the use of new technologies in unprecedented ways to defraud the Bank or its customers; consolidation in the Canadian financial services sector; competition, both from new entrants and established competitors; judicial and regulatory proceedings; acts of God, such as earthquakes and hurricanes; the possible impact of international conflicts and other developments, including terrorist acts and war on terrorism; the effects of disease or illness on local, national or international economies; disruptions to public infrastructure, including transportation, communication, power and water; and the Bank's anticipation of and success in managing the risks implied by the foregoing. A substantial amount of the Bank's business involves making loans or otherwise committing resources to specific companies, industries or countries. Unforeseen events affecting such borrowers, industries or countries could have a material adverse effect on the Bank's financial results, businesses, financial condition or liquidity. These and other factors may cause the Bank's actual performance to differ materially from that contemplated by forward-looking statements. For more information, see the discussion in the Bank's Annual Report on Form 40-F for the fiscal year ended October 31, 2012, which is incorporated by reference herein and which outlines in detail certain key factors that may affect the Bank's future results.

The preceding list of important factors is not exhaustive. When relying on forward-looking statements to make decisions with respect to the Bank and its securities, investors and others should carefully consider the preceding factors, other uncertainties and potential events. The Bank does not undertake to update any forward-looking statements, whether written or oral, that may be made from time to time by or on its behalf.

WHERE YOU CAN FIND MORE INFORMATION

In addition to the continuous disclosure obligations under the securities laws of the provinces and territories of Canada, the Bank is subject to the informational reporting requirements of the U.S. Securities Exchange Act of 1934, as amended (the "Exchange Act"), and in accordance therewith files reports and other information with the SEC. Under a multijurisdictional disclosure system adopted by the United States and Canada, such reports and other information may be prepared in accordance with the disclosure requirements of the provincial and territorial securities regulatory authorities of Canada, which requirements are different from those of the United States. As a foreign private issuer, the Bank is exempt from the rules under the Exchange Act prescribing the furnishing and content of proxy statements, and the Bank's officers and directors are exempt from the reporting and short swing profit recovery provisions contained in Section 16 of the Exchange Act. The Bank's reports and other information filed with or furnished to the SEC since November 2000 are available, and reports and other information filed or furnished in the future with or to the SEC will be available, from the SEC's Electronic Document Gathering and Retrieval System (<http://www.sec.gov>), which is commonly known by the acronym "EDGAR," as well as from commercial document retrieval services. Any document the Bank files with or furnishes to the SEC may be inspected and, by paying a fee, copied at the public reference facilities maintained by the SEC at 100 F Street, N.E., Washington, D.C. 20549. Prospective investors may call the SEC at 1-800-SEC-0330 for further information regarding the public reference facilities. The Bank's common shares are listed on the New York Stock Exchange and reports and other information concerning the

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Bank may be inspected at the offices of the New York Stock Exchange, 20 Broad Street, New York, New York 10005.

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The Bank has filed with the SEC, under the Securities Act, a registration statement on Form F-3 with respect to the securities and of which this prospectus forms a part. This prospectus does not contain all of the information that is set forth in the registration statement, certain parts of which are omitted in accordance with the rules and regulations of the SEC. Statements made in this prospectus as to the contents of any contract, agreement or other document referred to are not necessarily complete, and in each instance, reference is made to an exhibit, if applicable, for a more complete description of the matter, each such statement being qualified in its entirety by such reference. For further information with respect to the Bank and the securities, reference is made to the registration statement and the exhibits thereto, which are publicly available as described in the preceding paragraph.

INCORPORATION OF CERTAIN INFORMATION BY REFERENCE

The SEC allows us to incorporate by reference into this prospectus the information in documents we file with it. This means that we can disclose important information to you by referring you to those documents. The information incorporated by reference is considered to be a part of this prospectus and should be read with the same care. When we update the information contained in documents that have been incorporated by reference by making future filings with the SEC the information incorporated by reference in this prospectus is considered to be automatically updated and superseded. The modifying or superseding statement need not state that it has modified or superseded a prior statement or include any other information set forth in the document that it modifies or supersedes. In other words, in the case of a conflict or inconsistency between information contained in this prospectus and information incorporated by reference into this prospectus, you should rely on the information contained in the document that was filed later. The making of a modifying or superseding statement shall not be deemed an admission for any purposes that the modified or superseded statement, when made, constituted a misrepresentation, an untrue statement of a material fact or an omission to state a material fact that is required to be stated or that is necessary to make a statement not misleading in light of the circumstances in which it was made. Any statement so modified or superseded shall not be deemed, except as so modified or superseded to constitute a part of this prospectus.

We incorporate by reference the documents listed below and all documents which we subsequently file with the SEC (other than, in each case, documents or information deemed to have been furnished and not filed in accordance with the SEC rules) pursuant to Section 13(a), 13(c), 14, or 15(d) Exchange Act until the termination of the offering of the securities under this prospectus:

Registration Statement on Form 40-F filed on May 3, 2002;

Report on Form 6-K filed on April 21, 2011; and

Annual Report on Form 40-F for the fiscal year ended October 31, 2012.

All subsequent annual reports we file on Form 40-F pursuant to the Exchange Act, prior to the termination of the applicable offering, shall be deemed to be incorporated by reference into this prospectus for purposes of said offering.

We may also incorporate any other Form 6-K that we submit to the SEC on or after the date of this prospectus and prior to the termination of this offering if the Form 6-K filing specifically states that it is incorporated by reference into the registration statement of which this prospectus forms a part.

You may request a copy of these filings, other than an exhibit to a filing unless that exhibit is specifically incorporated by reference into that filing, at no cost, by writing to or telephoning us at the following address:

The Bank of Nova Scotia

Scotia Plaza

44 King Street West

Toronto, Ontario

Canada M5H 1H1

Attention: Secretary

Telephone: (416) 866-3672

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RISK FACTORS

Investment in these securities is subject to various risks including those risks inherent in conducting the business of a diversified financial institution. Before deciding whether to invest in any securities, you should consider carefully the risks set out herein and incorporated by reference in this prospectus (including subsequently filed documents incorporated by reference) and, if applicable, those described in the applicable prospectus supplements relating to a specific offering of securities. You should consider the categories of risks identified and discussed in the Bank's Annual Report on Form 40-F for the fiscal year ended October 31, 2012, which is incorporated herein by reference, including credit risk, market risk, liquidity risk, operational risk, reputational risk and environmental risk, those summarized under "Caution Regarding Forward-Looking Statements" above, as well as the following.

Foreign Accounts Tax Compliance Act Withholding

Sections 1471 through 1474 of the United States Internal Revenue Code of 1986, as amended, or similar law implementing an intergovernmental approach thereto (" FATCA ") may affect payments on the securities. See " United States Taxation Foreign Accounts Tax Compliance Act Withholding " for a discussion of the effects of FATCA on the ownership of the securities.

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THE BANK OF NOVA SCOTIA

The Bank is a Canadian chartered bank under the Bank Act (Canada) (the Bank Act). The Bank Act is the charter of the Bank and governs its operations.

The Bank is a leading multinational financial services provider and Canada's most international bank. Through its team of more than 81,000 employees, the Bank and its affiliates offer a broad range of products and services, including personal, commercial, corporate and investment banking to over 19 million customers in more than 55 countries.

A list of the principal subsidiaries directly or indirectly owned or controlled by the Bank as at October 31, 2012 is incorporated by reference from the Bank's Annual Report on Form 40-F for the fiscal year ended October 31, 2012.

Certain Matters Relating to the Bank's Board of Directors

Under the Bank Act, the Bank's board of directors must have at least seven members and the Bank's board of directors may establish by by-law a minimum and maximum number of directors. Under the Bank's by-laws, the minimum number of directors is the minimum required by the Bank Act and the maximum number of directors is 35. The Bank's by-laws also provide that the number of directors to be elected at any annual meeting of shareholders of the Bank will be fixed by the board of directors before the meeting. The Bank currently has 13 directors. The Bank Act requires that no more than two-thirds of the directors may be affiliated with the Bank, and no more than 15% of the directors may be employees of the Bank or a subsidiary of the Bank, except that up to four employees may be directors if they constitute not more than 50% of the directors. Under the Bank Act, a majority of the directors of the Bank must be resident Canadians and, except in limited circumstances, directors may not transact business at a meeting of directors or a committee of directors at which a majority of the directors present are not resident Canadians. Subject to the Bank Act a quorum for the transaction of business at any meeting of the board of directors consists of 5 directors. The Bank Act also requires the directors of a bank to appoint from their members a chief executive officer who must ordinarily be resident in Canada.

Under the Bank Act, any director or the entire board of directors may be removed, with or without cause, with the approval of a majority of the votes cast at a special meeting of shareholders. A vacancy created by such removal may be filled at the meeting or by a quorum of the directors. Directors who were elected on or before April 1, 2011 (existing directors) must retire at the earlier of 10 years from April 1, 2011 or age 70, provided that if an existing director has not served a 10 year term at the time of achieving age 70, their term will be extended for additional years in order to complete a minimum 10 year term. For directors elected after April 1, 2011, retirement is the earlier of age 70 or a 15 year term, provided that if a director has not served a 10 year term at the time of achieving age 70, their term will be extended for additional years in order to complete a minimum 10 year term.

Conflicts of Interest

The Bank Act contains detailed provisions with regard to a director's power to vote on a material contract or material transaction in which the director is interested. These provisions include procedures for: disclosure of the conflict of interest and the timing for such disclosure; the presence of directors at board meetings where the contract or transaction giving rise to the conflict of interest is being considered, and voting with respect to the contract or transaction giving rise to the conflict of interest; and other provisions for dealing with such conflicts of interest. The Bank Act also contains detailed provisions regarding transactions with persons who are related parties of the Bank, including directors of the Bank. See **Borrowing Powers**.

Compensation

The by-laws of the Bank have provisions with regard to remuneration of directors. The board of directors may, from time to time, by resolution determine their remuneration that may be paid, but such remuneration may not exceed in each year an aggregate cap set out in the by-laws, and individually may be in such amounts as the board may determine by resolution. The directors may also be paid their reasonable out-of-pocket expenses incurred in attending meetings of the board, shareholders or committees of the board.

Directors are required to hold common shares and/or directors' deferred stock units (DDSU) with a value of not less than \$450,000. The redemption value of a DDSU is equal to the market value of a common share at the time of redemption. The value of DDSUs is tied to the future value of the common shares. However, DDSUs do not entitle the holder to voting or other shareholder rights.

Borrowing Powers

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The directors of the Bank may, without authorization of the shareholders, authorize the Bank to borrow money. The Bank Act, however, prohibits the Bank from entering into transactions with persons who are deemed to be related parties of the Bank, subject to certain exceptions. Related party transactions may include loans made on the credit of the Bank.

Table of Contents**CONSOLIDATED CAPITALIZATION OF THE BANK**

The following table sets forth the consolidated capitalization of the Bank at October 31, 2012:

| | As at October 31, 2012 (In millions of Canadian dollars) |
|----------------------------------------------------------------|-----------------------------------------------------------------------------|
| Subordinated Debentures | 10,143 |
| Capital Instruments | 1,358 |
| Equity | |
| Common Equity | |
| Common Shares | 13,139 |
| Retained Earnings | 21,978 |
| Accumulated Other Comprehensive Loss | (31) |
| Other Reserves | 166 |
| Total Common Equity | 35,252 |
| Preferred Shares | 4,384 |
| Total Equity Attributable to Equity Holders of the Bank | 39,636 |
| Non-controlling Interests | |
| Non-controlling Interests in Subsidiaries | 966 |
| Capital Instrument Equity Holders | 777 |
| Total Non-controlling Interests | 1,743 |
| Total Equity | 41,379 |
| Total Capitalization | 52,880 |

Table of Contents**CONSOLIDATED EARNINGS RATIOS**

The following table provides the Bank's consolidated ratios of earnings to fixed charges, calculated in accordance with Canadian GAAP for each of years in the three year period ended October 31, 2010 and in accordance with IFRS for each of the years in the two year period ended October 31, 2012.

| | Years Ended October 31, | | | | |
|------------------------------------------------------------------------------------------|--------------------------------|---------------------------|---------------------------|---------------------------|---------------------------|
| | 2012⁽¹⁾ | 2011⁽¹⁾ | 2010⁽²⁾ | 2009⁽²⁾ | 2008⁽²⁾ |
| Consolidated Ratios of Earnings to Fixed Charges | | | | | |
| Excluding interest on deposits | 6.85 | 5.73 | 4.70 | 3.00 | 2.45 |
| Including interest on deposits | 2.05 | 1.91 | 1.70 | 1.44 | 1.26 |
| Consolidated Ratios of Earnings to Combined Fixed Charges and Preferred Dividends | | | | | |
| Excluding interest on deposits | 5.66 | 4.76 | 3.99 | 2.72 | 2.33 |
| Including interest on deposits | 1.97 | 1.84 | 1.64 | 1.41 | 1.25 |

(1) Calculated in accordance with IFRS.

(2) Calculated in accordance with Canadian GAAP.

For purposes of computing these ratios:

earnings represent income from continuing operations plus income taxes and fixed charges (excluding capitalized interest);

fixed charges, excluding interest on deposits, represent interest (including capitalized interest), estimated interest within rent, and amortization of debt issuance costs; and

fixed charges, including interest on deposits, represent all interest.

Table of Contents**COMPARATIVE PER SHARE MARKET PRICE**

The Bank's common shares are listed on the Toronto Stock Exchange (the "TSX") and the New York Stock Exchange (the "NYSE") under the trading symbol "BNS".

The table below sets forth, for the periods indicated, the per share high and low closing sales prices for the Bank's common shares as reported on the NYSE and the TSX. TSX closing prices of the Bank's common shares are presented in Canadian dollars, and the NYSE closing prices of the Bank's common shares are presented in U.S. dollars.

| | BNS shares TSX (in C\$) | | BNS shares NYSE (in U.S.\$) | |
|-------------------------------------------------------------------------------------|----------------------------|-------|--------------------------------|-------|
| | High | Low | High | Low |
| Annual information for the past fiscal years | | | | |
| 2008 | 53.50 | 35.25 | 57.15 | 27.77 |
| 2009 | 49.19 | 23.99 | 46.13 | 19.24 |
| 2010 | 55.75 | 44.12 | 54.85 | 41.34 |
| 2011 | 61.28 | 49.01 | 62.33 | 46.02 |
| 2012 | 57.05 | 47.93 | 57.32 | 45.90 |
| Quarterly information for the past two fiscal years and subsequent quarters: | | | | |
| 2011, quarter ended | | | | |
| January 31 | 57.71 | 52.11 | 57.90 | 50.90 |
| April 30 | 61.28 | 56.25 | 62.33 | 56.81 |
| July 31 | 59.73 | 53.77 | 62.33 | 56.15 |
| October 31 | 54.96 | 49.01 | 57.64 | 46.02 |
| 2012, quarter ended | | | | |
| January 31 | 54.85 | 47.54 | 54.51 | 45.79 |
| April 30 | 57.17 | 50.60 | 57.57 | 50.72 |
| July 31 | 54.89 | 50.26 | 55.71 | 48.45 |
| October 31 | 54.75 | 51.36 | 55.86 | 51.02 |
| Monthly information for the most recent six months | | | | |
| June 2012 | 53.57 | 50.55 | 52.49 | 48.45 |
| July 2012 | 54.03 | 50.51 | 53.32 | 49.51 |
| August 2012 | 53.65 | 51.25 | 54.45 | 50.86 |
| September 2012 | 55.00 | 51.92 | 56.11 | 51.75 |
| October 2012 | 54.47 | 53.22 | 55.51 | 53.84 |
| November 2012 | 56.00 | 52.80 | 55.74 | 52.72 |

Fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar will affect any comparisons of the Bank's common shares traded on the TSX and the Bank's common shares traded on the NYSE.

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USE OF PROCEEDS

Unless otherwise specified in an applicable prospectus supplement, the net proceeds to the Bank from the sale of securities will be added to the general funds of the Bank and utilized for general banking purposes. The application of the proceeds will depend upon the funding requirements of the Bank at the time.

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DESCRIPTION OF COMMON SHARES AND PREFERRED SHARES

Set forth below is a summary of the material terms of the Bank's share capital and certain provisions of the Bank Act and the Bank's amended and restated by-laws as they relate to the Bank's share capital. The following summary is not complete and is qualified in its entirety by the Bank Act, the Bank's amended and restated by-laws and the actual terms and conditions of such shares.

Capital Stock

The authorized capital of the Bank consists of an unlimited number of common shares, without nominal or par value, and an unlimited number of preferred shares, without nominal or par value, issuable in series, in each case the aggregate consideration for which is also unlimited.

Common Shares

Voting. Holders of the Bank's common shares are entitled to vote at all meetings of the Shareholders of the Bank, except meetings at which only the holders of preferred shares of the Bank are entitled to vote. Holders of common shares are entitled to one vote per share on all matters to be voted on by holders of common shares. Unless otherwise required by the Bank Act, any matter to be voted on by holders of common shares shall be decided by a majority of the votes cast on the matter.

Liquidation Rights. Upon the liquidation, dissolution or winding up of the Bank, whether voluntary or involuntary, the holders of common shares are entitled to receive the remaining property of the Bank available after the payment of all debts and other liabilities and subject to the prior rights of holders of any outstanding preferred shares.

Preemptive, Subscription, Redemption and Conversion Rights. Holders of common shares, as such, have no preemptive, subscription, redemption or conversion rights.

Dividends. Holders of common shares are entitled to receive dividends as and when declared by the board of directors of the Bank, subject to the preference of the holders of the preferred shares of the Bank. The Bank's dividends have historically been declared on a quarterly basis in Canadian dollars. As a matter of practice, at the request of a shareholder to the transfer agent or broker, the Bank will pay dividends to a U.S. holder of common shares, if and when a dividend is declared, in U.S. dollars. The declaration and payment of dividends and the amount of the dividends is subject to the discretion of the board of directors, and will be dependent upon the results of operations, financial condition, cash requirements and future regulatory restrictions on the payment of dividends by the Bank and other factors deemed relevant by the board of directors.

Preferred Shares

This section describes the general terms and provisions of our preferred shares. The applicable prospectus supplement will describe the specific terms of the preferred shares offered through that prospectus supplement, as well as any general terms described in this section that will not apply to those preferred shares.

General. The board of directors is authorized, subject to the provisions of the Bank Act, without shareholder approval, to divide any unissued preferred shares into series and fix the number of shares in each series and the rights, privileges, restrictions and conditions of each such series, and to change the rights, privileges, restrictions and conditions attached to unissued preferred shares of any series.

Priority. The preferred shares, as a class, are entitled to preference over common shares and over any other shares ranking junior to the preferred shares with respect to the payment of dividends and distribution of assets in the event of the liquidation, dissolution or winding-up of the Bank, or any other distribution of the assets among shareholders for the purpose of winding-up the affairs of the Bank. The preferred shares of each series rank on a parity with the preferred shares of every other series with respect to priority in payment of dividends and in the distribution of assets in the event of liquidation, dissolution or winding-up of the Bank, or any other distribution of the assets among shareholders for the purpose of winding-up the affairs of the Bank.

Restriction. Under the terms of the Bank Act, the approval of the holders of the preferred shares is required for the creation of any class of shares ranking prior to or on a parity with the preferred shares.

Voting. Except as required under the Bank Act or in the rights, privileges, restrictions or conditions attached to any series before the issue thereof, the holders of preferred shares are not entitled to receive notice, to attend or to vote at any meeting of the shareholders of the Bank. Any

approval to be given by the holders of preferred shares may be given by a resolution carried by the affirmative vote of not less than 66 2/3% of the votes cast at a meeting of holders of preferred shares at which a majority of the outstanding preferred shares is represented or, if no quorum is present at such meeting, at any adjourned meeting at which no quorum requirements would apply.

Limitations Affecting Holders of Common and Preferred Shares

Restraints on Bank Shares Under the Bank Act

In accordance with the Bank Act, no person or group of associated persons may own more than 10% of any class of shares of the Bank without the approval of the Minister of Finance (Canada) (the Minister). No person may be a major shareholder of a bank if the bank has equity of \$12 billion or more (which would include the Bank). A person is a major shareholder of a bank if: (a) the aggregate number of shares of any class of voting shares beneficially owned by that person and that are beneficially owned by any entities controlled by that person is more than 20% of that class of voting shares; or (b) the aggregate number of shares of any class of non-voting shares beneficially owned by that person and that are beneficially owned by any entities controlled by that person is

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more than 30% of that class of non-voting shares. Ownership of the Bank's shares by Canadian or foreign governments is prohibited under the Bank Act. However, in 2009 certain amendments were made to the Bank Act that would permit the Canadian federal government to acquire shares of a bank, including the Bank, if the Minister and Governor in Council were to conclude that to do so was necessary to promote stability in the financial system. While the government holds any shares of a bank, including the Bank, the Minister may impose certain terms and conditions, including conditions on the payment by the Bank of dividends on any of its shares.

The Minister may only approve the acquisition of up to 30% of the shares of any class of non-voting shares and up to 20% of the shares of a class of voting shares of the Bank, provided, in each case, that the person acquiring those shares does not have direct or indirect influence over the Bank that, if exercised, would result in that person having control in fact of the Bank. No person may have a significant interest in any class of shares of a bank, including the Bank, unless the person first receives the approval of the Minister. In addition, the Bank is not permitted to record any transfer or issue of any shares of the Bank if the transfer or issue would cause the person to have a significant interest in a class of shares, unless the prior approval of the Minister is obtained. No person who has a significant interest in the Bank may exercise any voting rights attached to the shares held by that person, unless the prior approval of the Minister for the acquisition of the significant interest is obtained. For purposes of the Bank Act, a person has a significant interest in a class of shares of a bank where the aggregate of any shares of the class beneficially owned by that person, by entities controlled by that person and by any person associated or acting jointly or in concert with that person exceeds 10% of all of the outstanding shares of that class of shares of such bank. If a person contravenes any of these restrictions, the Minister may, by order, direct that person to dispose of all or any portion of those shares. Holders of securities of the Bank may be required to furnish declarations relating to ownership in a form prescribed by the Bank.

Bank Act and Government Restrictions and Approvals

Under the Bank Act, the Bank cannot redeem or purchase any of its shares, including its common shares, unless the consent of the Office of the Superintendent of Financial Institutions (Canada) (OSFI) has been obtained. In addition, the Bank Act prohibits a payment to purchase or redeem any shares or the declaration and payment of a dividend if there are reasonable grounds for believing that the Bank is, or the payment would cause the Bank to be, in contravention of the capital adequacy and liquidity regulations of the Bank Act or any capital or liquidity directions of OSFI. The Bank is prohibited from declaring dividends on its preferred or common shares when it would be, as a result of paying such a dividend, in contravention of the capital adequacy and liquidity regulations of the Bank Act or any capital or liquidity directions of OSFI.

The government of Canada placed a moratorium on mergers among Canada's largest financial institutions in 2003, including the Bank and its peers, pending a further review of Canada's bank merger policy. The current Minister has previously stated that a review of the government's bank merger policy is not currently a priority, and as a result, it is unlikely that the Minister would grant an approval for a merger between any large Canadian financial institutions at this time.

The restrictions contained in the Bank Act and the Canadian government's policies may deter, delay or prevent a future amalgamation involving the Bank and will prevent the acquisition of control of the Bank, including transactions that could be perceived as advantageous to the Bank's shareholders.

Amendments to the Rights, Privileges, Restrictions and Conditions of the Bank's Share Capital

Under the Bank Act, the rights of holders of the Bank's shares can be changed by the board of directors of the Bank by making, amending or repealing the by-laws of the Bank. The board of directors of the Bank must submit such a by-law, or amendment to or repeal of a by-law, to the shareholders of the Bank in accordance with the procedures of the Bank Act and the Bank's by-laws, and the shareholders must approve the by-law, amendment to or repeal of the by-law by special resolution to be effective. Under the Bank Act, a special resolution is a resolution passed by not less than two-thirds of the votes cast by or on behalf of the shareholders who voted in respect of that resolution or signed by all the shareholders entitled to vote on that resolution. In some circumstances, the Bank Act mandates that holders of shares of a class or a series are entitled to vote separately as a class or series on a proposal to amend the by-laws of the Bank.

Meetings of the Shareholders***Quorum***

The Bank Act permits a bank to establish by by-law the quorum requirement for meetings of shareholders. The Bank's by-laws provide that a quorum at any meeting of shareholders will be any shareholders present in person or represented by proxy of at least 10% of the outstanding shares of the Bank entitled to vote at the meeting.

Annual Meetings; Shareholder Proposals

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The Bank is required to hold an annual meeting of shareholders not later than six months after the end of each financial year on such day and at such time as its directors shall determine.

Proposals by shareholders of a bank may be made by certain registered or beneficial holders of shares that are entitled to vote at an annual meeting of shareholders. To be eligible to submit any shareholder proposal, a shareholder must satisfy certain eligibility criteria set forth in the Bank Act. Under the Bank Act, shareholder proposals may only be submitted at annual meetings of shareholders. A shareholder eligible to submit a proposal and entitled to vote at an annual meeting of shareholders may submit to the Bank notice of any matter that the shareholder proposes to raise at the meeting provided that, among other things, the proposal is submitted to the Bank at least 90 days before the anniversary date of the notice of meeting that was sent to shareholders in respect of the Bank's previous annual meeting of shareholders.

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If the Bank solicits proxies for such annual meeting, it is required to set out in the management proxy a proposal submitted by a shareholder for consideration at such meeting. If so requested by a shareholder who submits a proposal to the Bank, the Bank is required to include in the management proxy circular, or attach thereto, a statement by the shareholder in support of the proposal and the name and address of the shareholder. The proposal and the statement together are not to exceed 500 words. Under the Bank Act, a proposal may include nominations for the election of directors if it is signed by one or more holders of shares representing in the aggregate not less than 5% of the issued and outstanding shares of the Bank or 5% of the issued and outstanding shares of a class of shares of the Bank entitled to vote at the meeting at which the proposal is to be presented.

The Bank is not required to comply with the obligations to include the proposal, or a statement of the shareholder submitting a proposal, in its management proxy circular, if

the proposal is not submitted to the Bank at least 90 days before the anniversary date of the notice of meeting that was sent to shareholders in respect of the previous annual meeting of shareholders;

it clearly appears that the primary purpose of the proposal is to enforce a personal claim or redress a personal grievance against the Bank or its directors, officers or security holders;

it clearly appears that the proposal does not relate in a significant way to the business or affairs of the Bank;

the person submitting the proposal failed within the prescribed period before the Bank receives their proposal to present, in person or by proxy, at a meeting of shareholders a proposal that at their request had been set out in or attached to a management proxy circular;

substantially the same proposal was set out in or attached to a management proxy circular or dissident's proxy circular relating to, and presented to shareholders at, a meeting of shareholders of the Bank held within the prescribed period before the receipt of the proposal and did not receive the prescribed minimum amount of support at the meeting; or

the rights to submit a proposal as described above are being abused to secure publicity.

If the Bank refuses to include a proposal in a management proxy circular, it is obligated to notify the shareholder in writing of such refusal and its reasons for such refusal. The shareholder may apply to a court if such shareholder claims it has been aggrieved by such refusal, and the court may restrain the holding of the meeting at which the proposal is sought to be presented and may make such further order it thinks fit. In addition, if the Bank claims to be aggrieved by the proposal, it may apply to a court for an order permitting the Bank to omit the proposal from the management proxy circular.

Special Meetings

Under the Bank Act, special meetings of shareholders may be called at any time by the board of directors. In addition, subject to certain provisions of the Bank Act, the holders of not less than 5% of the issued and outstanding shares of the Bank that carry the right to vote at a meeting may requisition that the directors call a meeting of shareholders for the purpose stated in the requisition and may call the special meeting if the directors do not do so within 21 days after receiving the request.

Size of Board of Directors

The Bank Act requires that the number of directors on the Bank's board of directors be at least seven. All directors of the Bank are elected annually. The Bank Act also requires that at least a majority of the directors must be, at the time of each director's election or appointment, resident Canadians.

Anti-Takeover Provisions and Ownership Provisions

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Rules and policies of certain Canadian securities regulatory authorities, including Multilateral Instrument 61-101 Protection of Minority Security Holders in Special Transactions, contain requirements in connection with related party transactions. A related party transaction means, among other things, any transaction in which an issuer directly or indirectly engages in the following with a related party: acquires, sells, leases or transfers an asset, acquires the related party, acquires or issues securities, amends the terms of a security if the security is owned by the related party or assumes or becomes subject to a liability or takes certain other actions with respect to debt.

Related party includes directors, senior officers and holders of more than 10% of the voting rights attached to all outstanding voting securities of the issuer or holders of a sufficient number of any securities of the issuer to materially affect control of the issuer.

If a transaction is determined to be a related party transaction, Multilateral Instrument 61-101 requires, subject to certain exceptions, the preparation of a formal valuation relating to certain aspects of the transaction and more detailed disclosure in the proxy material sent to security holders in connection with the related party transaction, including disclosure related to the valuation.

Multilateral Instrument 61-101 also requires, subject to certain exceptions, that an issuer not engage in a related party transaction unless the shareholders of the issuer, other than the related parties, approve the transaction by a simple majority of the votes cast.

In addition, under the Bank Act, a sale of all or substantially all of the Bank's assets to another financial institution or an amalgamation must also be approved by the shareholders by a vote of not less than two-thirds of the votes cast by shareholders who voted in respect of the special resolution, with each share carrying the right to vote whether or not it otherwise carries the right to vote. The holders of each class or series of shares which is affected differently by the sale from the shares of any other class or series are entitled to vote separately as a class or series. The Minister must also approve any such sale or amalgamation involving the Bank.

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These restrictions, in addition to those imposed by the Bank Act relating to the purchase or other acquisition, issue, transfer and voting of shares of the Bank's common shares may deter, delay or prevent a future amalgamation involving the Bank and will prevent the acquisition of control of the Bank, including transactions that could be perceived as advantageous to the Bank's shareholders. See Limitations Affecting Holders of Common and Preferred Shares.

Rights of Inspection

Any person is entitled to a basic list of the Bank's shareholders and may request the Bank to furnish such list within 10 days after receipt by the Bank of an affidavit, swearing that the list will not be used except in accordance with a permitted purpose, and payment of a reasonable fee. Further, shareholders and creditors of the Bank and their personal representatives may examine certain limited records of the Bank during its usual business hours and may take extracts therefrom, free of charge, or have copies made thereof on payment of a reasonable fee.

Transfer Agent and Registrar

The registrar and transfer agent for the Bank's common and preferred shares is Computershare Trust Company of Canada at the following addresses: Computershare Trust Company of Canada, 100 University Avenue, 9th Floor, Toronto, Ontario, M5J 2Y1 and Computershare Trust Company N.A., 250 Royall Street, Canton, Massachusetts, 02021, U.S.A.

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DESCRIPTION OF THE DEBT SECURITIES WE MAY OFFER

References to the Bank, us, we or our in this section mean The Bank of Nova Scotia, and do not include the subsidiaries of The Bank of Nova Scotia. Also, in this section, references to holders mean those who own debt securities registered in their own names, on the books that we or the applicable trustees maintain for this purpose, and not those who own beneficial interests in debt securities registered in street name or in debt securities issued in book-entry form through one or more depositaries. When we refer to you in this prospectus, we mean all purchasers of the debt securities being offered by this prospectus, whether they are the holders or only indirect owners of those debt securities. Owners of beneficial interests in the debt securities should read the section below entitled Legal Ownership and Book-Entry Issuance.

The following description sets forth certain general terms and provisions of the debt securities. We will provide particular terms and provisions of a series of debt securities and a description of how the general terms and provisions described below may apply to that series in a prospectus supplement. Prospective investors should rely on information in the applicable prospectus supplement if it is different from the following information.

Debt Securities May Be Senior or Subordinated

We may issue debt securities which may be senior or subordinated in right of payment. Neither the senior debt securities nor the subordinated debt securities will be secured by any of our property or assets or the property or assets of our subsidiaries. Thus, by owning a debt security, you are one of our unsecured creditors.

The senior debt securities will be issued under our senior debt indenture described below and will be unsubordinated obligations that rank equally with all of our other unsecured and unsubordinated debt, including deposit liabilities, other than certain governmental claims in accordance with applicable law.

The subordinated debt securities will be issued under our subordinated debt indenture described below and will be subordinate in right of payment to all of our senior indebtedness, as defined in the subordinated debt indenture. Neither indenture limits our ability to incur additional indebtedness.

In the event we become insolvent, our governing legislation provides that priorities among payments of our deposit liabilities (including payments in respect of the senior debt securities) and payments of all of our other liabilities (including payments in respect of the subordinated debt securities) are to be determined in accordance with the laws governing priorities and, where applicable, by the terms of the indebtedness and liabilities. In addition, our right to participate in any distribution of the assets of our banking or non-banking subsidiaries, upon a subsidiary's dissolution, winding-up, liquidation or reorganization or otherwise, and thus your ability to benefit indirectly from such distribution, is subject to the prior claims of creditors of that subsidiary, except to the extent that we may be a creditor of that subsidiary and our claims are recognized. There are legal limitations on the extent to which some of our subsidiaries may extend credit, pay dividends or otherwise supply funds to, or engage in transactions with, us or some of our other subsidiaries. Accordingly, the debt securities will be structurally subordinated to all existing and future liabilities of our subsidiaries, and holders of debt securities should look only to our assets for payments on the debt securities.

Neither the senior debt securities nor the subordinated debt securities will constitute deposits insured under the Canada Deposit Insurance Corporation Act (Canada) or by the United States Federal Deposit Insurance Corporation or any other Canadian or United States governmental agency or instrumentality.

When we refer to debt securities or debt security in this section, we mean both the senior debt securities and the subordinated debt securities.

The Senior and Subordinated Debt Indentures

The senior debt securities and the subordinated debt securities are each governed by an indenture the senior debt indenture, in the case of the senior debt securities, and the subordinated debt indenture, in the case of the subordinated debt securities. When we refer to the indentures, we mean both the senior debt indenture and the subordinated debt indenture, and when we refer to the indenture, we mean either the senior debt indenture or the subordinated debt indenture, as applicable. Each indenture is a contract between us, Computershare Trust Company, N.A., as U.S. trustee, and Computershare Trust Company of Canada, as Canadian trustee, which act as trustees. When we refer to the trustees, we mean both the U.S. trustee and the Canadian trustee, and when we refer to the trustee, we mean either the U.S. trustee or the Canadian trustee, as applicable. The indentures are subject to and governed by the U.S. Trust Indenture Act of 1939, as amended, and applicable Canadian trust indenture legislation. The indentures are substantially identical, except for the provisions relating to:

the events of default, which are more limited in the subordinated debt indenture; and

subordination, which are included only in the subordinated debt indenture.

Reference to the indenture or the trustees, with respect to any debt securities, means the indenture under which those debt securities are issued and the trustees under that indenture.

The trustees have two main roles:

The trustees can enforce the rights of holders against us if we default on our obligations under the terms of the indenture or the debt securities. There are some limitations on the extent to which the trustees act on behalf of holders, described below under Events of Default Remedies If an Event of Default Occurs.

The trustees perform administrative duties for us, such as sending interest payments and notices to holders and transferring a holder's debt securities to a new buyer if a holder sells.

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The indentures and their associated documents contain the full legal text of the matters described in this section. The indentures and the debt securities will be governed by New York law, except that the subordination provisions in the subordinated debt indenture and certain provisions relating to the status of the senior debt securities, which will be governed by the laws of the Province of Ontario and the laws of Canada applicable therein. A copy of each of the senior debt indenture and the subordinated debt indenture is an exhibit to the registration statement of which this prospectus forms a part. See [Available Information](#) above for information on how to obtain a copy.

General

We may issue as many distinct series of debt securities under either indenture as we wish. The provisions of the senior debt indenture and the subordinated debt indenture allow us not only to issue debt securities with terms different from those previously issued under the applicable indenture, but also to re-open a previous issue of a series of debt securities and issue additional debt securities of that series. We may issue debt securities in amounts that exceed the total amount specified on the cover of your applicable prospectus supplement at any time without your consent and without notifying you. In addition, we may issue additional debt securities of any series at any time without your consent and without notifying you. We may also issue other securities at any time without your consent and without notifying you. The indentures do not limit our ability to incur other indebtedness or to issue other securities, and we are not subject to financial or similar restrictions under the indentures.

This section summarizes the material terms of the debt securities that are common to all series, subject to any modifications contained in an applicable prospectus supplement. Most of the specific terms of your series will be described in the applicable prospectus supplements accompanying this prospectus. As you read this section, please remember that the specific terms of your debt security as described in the applicable prospectus supplements will supplement and, if applicable, may modify or replace the general terms described in this section. If there are any differences between the information in the applicable prospectus supplements and this prospectus, the information in the most recent applicable prospectus supplement will control. Accordingly, the statements we make in this section may not apply to your debt securities. Because this section is a summary, it does not describe every aspect of the debt securities. This summary is subject to and qualified in its entirety by reference to all the provisions of the indentures and the applicable series of debt securities, including definitions of certain terms used in the indentures and the applicable series of debt securities. In this summary, we describe the meaning of only some of the more important terms. You must look to the indentures or the applicable series of debt securities for the most complete description of what we describe in summary form in this prospectus.

We may issue the debt securities as original issue discount securities, which will be offered and sold at a substantial discount below their stated principal amount. An applicable prospectus supplement relating to the original issue discount securities will describe U.S. federal income tax consequences and other special considerations applicable to them. An applicable prospectus supplement relating to specific debt securities will also describe any special considerations and any material tax considerations applicable to such debt securities.

When we refer to a series of debt securities, we mean a series issued under the indenture pursuant to which the debt securities will be issued. Each series is a single distinct series under the indenture pursuant to which they will be issued and we may issue debt securities of each series in such amounts, at such times and on such terms as we wish. The debt securities of each series will differ from one another, and from any other series, in their terms, but all debt securities of a series together will constitute a single series for all purposes under the indenture pursuant to which they will be issued.

We may issue debt securities up to an aggregate principal amount as we may authorize from time to time. The applicable prospectus supplements will describe the terms of any debt securities being offered, including:

the title of the series of debt securities;

whether it is a series of senior debt securities or a series of subordinated debt securities;

any limit on the aggregate principal amount of the series of debt securities;

the person to whom interest on a debt security is payable, if other than the holder on the regular record date;

the date or dates on which the series of debt securities will mature;

the rate or rates (which may be fixed or variable) per annum, at which the series of debt securities will bear interest, if any, and the date or dates from which that interest, if any, will accrue;

the dates on which such interest, if any, will be payable and the regular record dates for such interest payment dates;

the place or places where the principal of, premium, if any, and interest on the debt securities is payable;

any mandatory or optional sinking funds or similar provisions or provisions for redemption at our option or the option of the holder;

if applicable, the date after which, the price at which, the periods within which and the terms and conditions upon which the debt securities may, pursuant to any optional or mandatory redemption provisions, be redeemed and other detailed terms and provisions of those optional or mandatory redemption provisions, if any;

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if applicable, the terms and conditions upon which the debt securities may be repayable prior to final maturity at the option of the holder thereof (which option may be conditional);

the portion of the principal amount of the debt securities, if other than the entire principal amount thereof, payable upon acceleration of maturity thereof;

if the debt securities may be converted into or exercised or exchanged for other of our securities, the terms on which conversion, exercise or exchange may occur, including whether conversion, exercise or exchange is mandatory, at the option of the holder or at our option, the period during which conversion, exercise or exchange may occur, the initial conversion, exercise or exchange price or rate and the circumstances or manner in which the amount of our securities issuable upon conversion, exercise or exchange may be adjusted;

if other than denominations of U.S.\$2,000 and integral multiples of U.S.\$1,000 in excess thereof, the denominations in which the series of debt securities will be issuable;

the currency of payment of principal, premium, if any, and interest on the series of debt securities;

if the currency of payment for principal, premium, if any, and interest on the series of debt securities is subject to our election or that of a holder, the currency or currencies in which payment can be made and the period within which, and the terms and conditions upon which, the election can be made;

the applicability of the provisions described under **Defeasance** below;

any event of default under the series of debt securities if different from those described under **Events of Default** below;

if the series of debt securities will be issuable only in the form of a global debt security, the depositary or its nominee with respect to the series of debt securities and the circumstances under which the global debt security may be registered for transfer or exchange in the name of a person other than the depositary or the nominee; and

any other special feature of the series of debt securities.

Market-Making Transactions

One or more of our subsidiaries may purchase and resell debt securities in market-making transactions after their initial issuance. We may also, subject to applicable law and any required regulatory approval, purchase debt securities in the open market or in private transactions to be held by us or cancelled.

Covenants

Except as described in this sub-section or as otherwise provided in an applicable prospectus supplement with respect to any series of debt securities, we are not restricted by the indentures from incurring, assuming or becoming liable for any type of debt or other obligations, from paying dividends or making distributions on our capital stock or purchasing or redeeming our capital stock. The indentures do not require the maintenance of any financial ratios or specified levels of net worth or liquidity, nor do they contain any covenants or other provisions that would limit our or our subsidiaries' right to incur additional indebtedness, enter into any sale and leaseback transaction or grant liens on our or our subsidiaries' assets. The indentures do not contain any provisions that would require us to repurchase or redeem or otherwise modify the terms of any of the debt securities upon a change in control or other events that may adversely affect the creditworthiness of the debt securities, for

example, a highly leveraged transaction, except as otherwise specified in this prospectus or any applicable prospectus supplement.

Mergers and Similar Events

Each of the indentures provide that we are permitted to merge, amalgamate, consolidate or otherwise combine with another entity, or to sell or lease substantially all of our assets to another entity, as long as the following conditions are met:

When we merge, amalgamate, consolidate or otherwise are combined with another entity, or sell or lease substantially all of our assets, the surviving, resulting or acquiring entity is a duly organized entity and is legally responsible for and assumes, either by agreement, operation of law or otherwise, our obligations under such indenture and the debt securities issued thereunder.

The merger, amalgamation, consolidation, other combination, or sale or lease of assets, must not result in an event of default under such indenture. A default for this purpose would include any event that would be an event of default if the requirements for giving us default notice or our default having to exist for a specified period of time were disregarded.

If the conditions described above are satisfied, we will not need to obtain the consent of the holders of the debt securities in order to merge, amalgamate, consolidate or otherwise combine with another entity or to sell or lease substantially all of our assets.

We will not need to satisfy the conditions described above if we enter into other types of transactions, including:

any transaction in which we acquire the stock or assets of another entity but in which we do not merge, amalgamate, consolidate or otherwise combine;

any transaction that involves a change of control but in which we do not merge, amalgamate, consolidate or otherwise combine; and

any transaction in which we sell less than substantially all of our assets.

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It is possible that this type of transaction may result in a reduction in our credit rating, may reduce our operating results or may impair our financial condition. Holders of debt securities, however, will have no approval right with respect to any transaction of this type.

Modification and Waiver of the Debt Securities

There are four types of changes we can make to the indenture and the debt securities issued under that indenture.

Changes Requiring Consent of All Holders. First, there are changes that cannot be made to the indenture or the debt securities without the consent of each holder of a series of debt securities affected in any material respect by the change under a particular indenture. Following is a list of those types of changes:

change the stated maturity of the principal or reduce the interest on a debt security;

reduce any amounts due on a debt security;

reduce the amount of principal payable upon acceleration of the maturity of a debt security (including the amount payable on an original issue discount security) following a default;

change the currency of payment on a debt security;

change the place of payment for a debt security;

impair a holder's right to sue for payment;

impair a holder's right to require repurchase on the original terms of those debt securities that provide a right of repurchase;

reduce the percentage of holders of debt securities whose consent is needed to modify or amend the indenture;

reduce the percentage of holders of debt securities whose consent is needed to waive compliance with certain provisions of the indenture or to waive certain defaults; or

modify any other aspect of the provisions dealing with modification and waiver of the indenture.

Changes Requiring a Majority Consent. The second type of change to the indenture and the debt securities is the kind that requires the consent of holders of debt securities owning not less than a majority of the principal amount of the particular series affected. Most changes fall into this category, except for clarifying changes and certain other changes that would not adversely affect in any material respect holders of the debt securities. We may also obtain a waiver of a past default from the holders of debt securities owning a majority of the principal amount of the particular series affected. However, we cannot obtain a waiver of a payment default or any other aspect of the indenture or the debt securities listed in the first category described above under *Changes Requiring Consent of All Holders* unless we obtain the individual consent of each holder to the waiver.

Changes Not Requiring Consent. The third type of change to the indenture and the debt securities does not require the consent by holders of debt securities. This type is limited to the issuance of new series of debt securities under the indenture, clarifications and certain other changes that

would not adversely affect in any material respect the interests of the holders of the debt securities of any series.

We may also make changes or obtain waivers that do not adversely affect in any material respect a particular debt security, even if they affect other debt securities. In those cases, we do not need to obtain the consent of the holder of the unaffected debt security; we need only obtain any required approvals from the holders of the affected debt securities.

Modification of Subordination Provisions. The fourth type of change to the indenture and the debt securities is the kind that requires the consent of the holders of a majority of the principal amount of all affected series of subordinated debt securities, voting together as one class. We may not modify the subordination provisions of the subordinated debt indenture in a manner that would adversely affect in any material respect the outstanding subordinated debt securities of any one or more series without the consent of the holders of a majority of the principal amount of all affected series of subordinated debt securities, voting together as one class.

Further Details Concerning Voting. When seeking consent, we will use the following rules to decide how much principal amount to attribute to a debt security:

For original issue discount securities, we will use the principal amount that would be due and payable on the voting date if the maturity of the debt securities were accelerated to that date because of a default.

For debt securities whose principal amount is not known, we will use a special rule for that debt security described in the applicable prospectus supplement.

For debt securities denominated in one or more non-U.S. currencies or currency units, we will use the U.S. dollar equivalent. Debt securities will not be considered outstanding, and therefore not eligible to vote or take other action under the applicable indenture, if we have given a notice of redemption and deposited or set aside in trust for the holders money for the payment or redemption of those debt securities. Debt securities will also not be considered outstanding, and therefore not eligible to vote or take other action under the applicable indenture, if they have been fully defeased as described below under **Defeasance** **Full Defeasance** or if we or one of our affiliates is the beneficial owner of the debt securities.

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We will generally be entitled to set any day as a record date for the purpose of determining the holders of outstanding debt securities that are entitled to vote or take other action under the applicable indenture. In certain limited circumstances, the trustees will be entitled to set a record date for action by holders. If the trustees or we set a record date for a vote or other action to be taken by holders of a particular series, that vote or action may be taken only by persons who are holders of outstanding debt securities of that series on the record date. We or the trustees, as applicable, may shorten or lengthen this period from time to time. This period, however, may not extend beyond the 180th day after the record date for the action.

Book-entry and other indirect holders should consult their banks, brokers or other financial institutions for information on how approval may be granted or denied if we seek to change the indenture or the debt securities or request a waiver.

Special Provisions Related to the Subordinated Debt Securities

The subordinated debt securities issued under the subordinated debt indenture will be our direct unsecured obligations constituting subordinated indebtedness for the purpose of the Bank Act and will therefore rank subordinate to our deposits. Holders of subordinated debt securities should recognize that contractual provisions in the subordinated debt indenture may prohibit us from making payments on these debt securities.

If we become insolvent or are wound-up, the subordinated debt securities issued and outstanding under the subordinated debt indenture will rank equally with, but not prior to, all other subordinated indebtedness and subordinate in right of payment to the prior payment in full of all other indebtedness of the Bank then outstanding, other than liabilities which, by their terms, rank in right of payment equally with or subordinate to the subordinated indebtedness, and in accordance with the terms of such liabilities or such other indebtedness under certain circumstances.

For these purposes, indebtedness at any time means:

1. the deposit liabilities of the Bank at such time; and
2. all other liabilities and obligations of the Bank which in accordance with the accounting rules established for Canadian chartered banks issued under the authority of the Superintendent of Financial Institutions (Canada) or with generally accepted accounting principles (the primary source of which is the Handbook of the Canadian Institute of Chartered Accountants Part V pre-changeover accounting standards; IFRS replaced current Canadian GAAP for the Bank commencing November 1, 2011 which is Part I of the Handbook of the Canadian Institute of Chartered Accountants), as the case may be, would be included in determining the total liabilities of the Bank, other than liabilities for paid-up capital, contributed surplus, retained earnings and general reserves of the Bank.

Subordinated indebtedness at any time means:

1. the liability of the Bank in respect of the principal of and premium, if any, and interest on its outstanding subordinated indebtedness outlined above;
2. any indebtedness which ranks equally with and not prior to the outstanding subordinated indebtedness, in right of payment in the event of the insolvency or winding up of the Bank and which, pursuant to the terms of the instrument evidencing or creating the same, is expressed to be subordinate in right of payment to all indebtedness to which the outstanding subordinated indebtedness is subordinate in right of payment to at least the same extent as the outstanding subordinated indebtedness is subordinated thereto pursuant to the terms of the instrument evidencing or creating the same;
3. any indebtedness which ranks subordinate to and not equally with or prior to the outstanding subordinated indebtedness, in right of payment in the event of the insolvency or winding-up of the Bank and which, pursuant to the terms of the instrument evidencing or creating the same, is expressed to be subordinate in right of payment to all indebtedness to which the outstanding subordinated indebtedness is subordinate in right of payment to at least the same extent as the outstanding subordinated indebtedness is subordinate pursuant to the terms of the instrument evidencing or creating the same; and

4. the subordinated debt securities, which will rank equally to the Bank's outstanding subordinated indebtedness. The subordination provisions of the subordinated debt indenture are governed by the laws of the Province of Ontario and the federal laws of Canada applicable therein.

Conversion or Exchange of Debt Securities

If and to the extent mentioned in the applicable prospectus supplements, any debt securities may be optionally or mandatorily convertible or exchangeable for other securities of the Bank, into the cash value therefor or into any combination of the above. The specific terms on which any debt securities may be so converted or exchanged will be described in the applicable prospectus supplements. These terms may include provisions for conversion or exchange, either mandatory, at the holder's option or at our option, in which case the amount or number of securities the holders of the debt securities would receive would be calculated at the time and manner described in the applicable prospectus supplements.

Defeasance

The following discussion of full defeasance and covenant defeasance will be applicable to each series of debt securities that is denominated in U.S. dollars and has a fixed rate of interest and will apply to other series of debt securities if we so specify in the applicable prospectus supplements.

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Full Defeasance. If there is a change in U.S. federal income tax law, as described below, we can legally release ourselves from any payment or other obligations on the debt securities of a series, called full defeasance, if we put in place the following other arrangements for holders to be repaid:

We must deposit in trust for the benefit of all holders of the debt securities of that series a combination of money and notes or bonds of (i) the U.S. government or (ii) a U.S. government agency or U.S. government-sponsored entity, the obligations of which, in each case, are backed by the full faith and credit of the U.S. government, that will generate enough cash to make interest, principal and any other payments on the debt securities of that series on their various due dates.

There must be a change in current U.S. federal income tax law or a ruling by the United States Internal Revenue Service that lets us make the above deposit without causing the holders to be taxed on the debt securities of that series any differently than if we did not make the deposit and just repaid the debt securities of that series ourselves. (Under current U.S. federal income tax law, the deposit and our legal release from the obligations pursuant to the debt securities would be treated as though we took back your debt securities and gave you your share of the cash and notes or bonds deposited in trust. In that event, you could recognize gain or loss on the debt securities you give back to us.)

We must deliver to the trustees a legal opinion of our counsel confirming the tax-law change described above and that the holders of the debt securities of that series will not recognize income, gain or loss for U.S. federal income tax purposes as a result of such deposit, defeasance and discharge and will be subject to U.S. federal income tax on the same amounts and in the same manner and at the same times as would be the case if such deposit, defeasance and discharge had not occurred.

In the case of the subordinated debt securities, the following requirement must also be met:

No event or condition may exist that, under the provisions described under Special Provisions Related to the subordinated debt securities above, would prevent us from making payments of principal, premium or interest on those subordinated debt securities on the date of the deposit referred to above or during the 90 days after that date.

If we ever did accomplish full defeasance, as described above, you would have to rely solely on the trust deposit for repayment on the debt securities. You could not look to us for repayment in the event of any shortfall.

Covenant Defeasance. Even without a change in current U.S. federal income tax law, we can make the same type of deposit as described above, and we will be released from the restrictive covenants under the debt securities of a series that may be described in the applicable prospectus supplements. This is called covenant defeasance. In that event, you would lose the protection of these covenants but would gain the protection of having money and U.S. government, U.S. government agency or U.S. government-sponsored entity notes or bonds set aside in trust to repay the debt securities. In order to achieve covenant defeasance, we must do the following:

Deposit in trust for the benefit of all holders of the debt securities of that series a combination of money and notes or bonds of (i) the U.S. government or (ii) a U.S. government agency or U.S. government-sponsored entity, the obligations of which, in each case, are backed by the full faith and credit of the U.S. government, that will generate enough cash to make interest, principal and any other payments on the debt securities of that series on their various due dates.

Deliver to the trustees a legal opinion of our counsel confirming that the holders of the debt securities of that series will not recognize income, gain or loss for U.S. federal income tax purposes as a result of such deposit and covenant defeasance and will be subject to U.S. federal income tax on the same amounts and in the same manner and at the same times as would be the case if such deposit and covenant defeasance had not occurred.

If we accomplish covenant defeasance, certain provisions of the indentures and the debt securities would no longer apply:

Covenants applicable to the series of debt securities and described in the applicable prospectus supplements.

Any events of default relating to breach of those covenants.

If we accomplish covenant defeasance, you can still look to us for repayment of the debt securities if there were a shortfall in the trust deposit. In fact, if one of the remaining events of default occurs (such as a bankruptcy) and the debt securities become immediately due and payable, there may be such a shortfall.

Events of Default

You will have special rights if an event of default occurs and is not cured, as described later in this subsection.

What is an Event of Default?

Under the senior debt indenture, the term event of default means in respect of any series of debt securities any of the following:

We do not pay the principal of or any premium on a debt security of that series within five days of its due date.

We do not pay interest on a debt security of that series for more than 30 days after its due date.

We file for bankruptcy or certain other events of bankruptcy, insolvency or reorganization occur.

Any other event of default described in an applicable prospectus supplement occurs.

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Under the subordinated debt indenture, the term "event of default" in respect of any series of debt securities means any of the following:

We file for bankruptcy or certain other events of bankruptcy, insolvency or reorganization occur.

Any other event of default described in an applicable prospectus supplement occurs.

Remedies If an Event of Default Occurs. If an event of default occurs, the trustees will have special duties. In that situation, the trustees will be obligated to use those of their rights and powers under the applicable indenture, and to use the same degree of care and skill in doing so, that a prudent person would use in that situation in conducting his or her own affairs. If an event of default has occurred and has not been cured, the trustees or the holders of at least 25% in principal amount of the debt securities of the affected series may declare the entire principal amount of (or, in the case of original issue discount securities, the portion of the principal amount that is specified in the terms of the affected debt security) and interest on all of the debt securities of that series to be due and immediately payable. This is called a declaration of acceleration of maturity. The declaration of acceleration of maturity is not, however, an automatic right upon the occurrence of an event of default, and for such acceleration to be effective, the trustees must take the aforementioned action or the holders must direct the trustees to act as described in this section below. Furthermore, a declaration of acceleration of maturity may be cancelled, but only before a judgment or decree based on the acceleration has been obtained, by the holders of at least a majority in principal amount of the debt securities of the affected series. If you are the holder of a subordinated debt security, the principal amount of the subordinated debt security will not be paid and may not be required to be paid at any time prior to the relevant maturity date, except in the event of our insolvency or winding-up. If any provisions of applicable Canadian banking law prohibit the payment of any amounts due under the debt securities before a specified time, then the Bank's ability to make such payment could be adversely affected.

You should read carefully the applicable prospectus supplements relating to any series of debt securities which are original issue discount securities for the particular provisions relating to acceleration of the maturity of a portion of the principal amount of original issue discount securities upon the occurrence of an event of default and its continuation.

Except in cases of default in which the trustees have the special duties described above, the trustees are not required to take any action under the indenture at the request of any holders unless the holders offer the trustees reasonable protection from expenses and liability called an indemnity reasonably satisfactory to the trustees. If such an indemnity is provided, the holders of a majority in principal amount of the outstanding debt securities of the relevant series may direct the time, method and place of conducting any lawsuit or other formal legal action seeking any remedy available to the trustees. These majority holders may also direct the trustees in performing any other action under the applicable indenture with respect to the debt securities of that series.

Before you bypass the trustees and bring your own lawsuit or other formal legal action or take other steps to enforce your rights or protect your interests relating to the debt securities the following must occur:

the holder of the debt security must give the trustees written notice that an event of default has occurred and remains uncured;

the holders of not less than 25% in principal amount of all outstanding debt securities of the relevant series must make a written request that the trustees take action because of such event of default;

such holder or holders must offer reasonable indemnity to the trustees against the cost and other liabilities of taking that action;

the trustees must have not taken action for 90 days after receipt of the above notice and offer of indemnity; and

the trustees have not received any direction from a majority in principal amount of all outstanding debt securities that is inconsistent with such written request during such 90-day period.

However, you are entitled at any time to bring a lawsuit for the payment of money due on your debt security on or after its due date.

BOOK-ENTRY AND OTHER INDIRECT HOLDERS SHOULD CONSULT THEIR BANKS, BROKERS OR OTHER FINANCIAL INSTITUTIONS OR INFORMATION ON HOW TO GIVE NOTICE OR DIRECTION TO OR MAKE A REQUEST OF THE TRUSTEES AND TO MAKE OR CANCEL A DECLARATION OF ACCELERATION

We will give to the trustees every year a written statement of certain of our officers certifying that to their knowledge we are in compliance with the applicable indenture and the debt securities issued under it, or else specifying any default.

Form, Exchange and Transfer

Unless we specify otherwise in an applicable prospectus supplement, the debt securities will be issued:

only in fully-registered form;

without interest coupons; and

in denominations of U.S.\$2,000 and integral multiples of U.S.\$1,000 in excess thereof.

If a debt security is issued as a registered global debt security, only the depositary such as DTC, Euroclear and Clearstream, each as defined below under Legal Ownership and Book-Entry Issuance will be entitled to transfer and exchange the debt security as described in this subsection because the depositary will be the sole registered holder of the debt security and is referred to

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below as the holder. Those who own beneficial interests in a global debt security do so through participants in the depositary's securities clearance system, and the rights of these indirect owners will be governed by the applicable procedures of the depositary and its participants. We describe book-entry procedures below under Legal Ownership and Book-Entry Issuance.

Holders of debt securities issued in fully-registered form may have their debt securities broken into more debt securities of smaller authorized denominations or combined into fewer debt securities of larger authorized denominations, as long as the total principal amount is not changed. This is called an exchange.

Holders may exchange or register the transfer of debt securities at the office of the applicable trustee. Debt securities may be transferred by endorsement. Holders may also replace lost, stolen or mutilated debt securities at that office. The trustees act as our agents for registering debt securities in the names of holders and registering the transfer of debt securities. We may change this appointment to another entity or perform it ourselves. The entity performing the role of maintaining the list of registered holders is called the security registrar. It will also record transfers. The applicable trustee may require an indemnity before replacing any debt securities.

Holders will not be required to pay a service charge to register the transfer or exchange of debt securities, but holders may be required to pay for any tax or other governmental charge associated with the exchange or transfer. The registration of a transfer or exchange will only be made if the security registrar is satisfied with your proof of ownership.

If we designate additional agents, they will be named in the applicable prospectus supplements. We may cancel the designation of any particular agent. We may also approve a change in the office through which any agent acts.

If the debt securities are redeemable and we redeem less than all of the debt securities of a particular series, we may block the registration of transfer or exchange of debt securities during the period beginning 15 days before the day we mail the notice of redemption and ending on the day of that mailing, in order to freeze the list of holders entitled to receive the mailing. We may also refuse to register transfers or exchanges of debt securities selected for redemption, except that we will continue to permit registration of transfers and exchanges of the unredeemed portion of any debt security being partially redeemed.

The Trustees

Computershare Trust Company, N.A. and Computershare Trust Company of Canada serve as the trustees for our senior debt securities.

Computershare Trust Company, N.A. and Computershare Trust Company of Canada also serve as the trustees for the subordinated debt securities.

The trustees make no representation or warranty, whether express or implied, with respect to the Bank or the debt securities and other matters described in this prospectus. The trustees have not prepared or reviewed any of the information included in this prospectus, except the trustees have consented to the use of their names. Such approval does not constitute a representation or approval by the trustees of the accuracy or sufficiency of any information contained in this prospectus.

Payment and Paying Agents

We will pay interest to the person listed in the trustees' records at the close of business on a particular day in advance of each due date for interest, even if that person no longer owns the debt security on the interest due date. That particular day, usually about two weeks in advance of the interest due date, is called the regular record date and will be stated in an applicable prospectus supplement. Holders buying and selling debt securities must work out between them how to compensate for the fact that we will pay all the interest for an interest period to the one who is the registered holder on the regular record date. The most common manner is to adjust the sale price of the debt securities to prorate interest fairly between buyer and seller. This prorated interest amount is called accrued interest.

We will pay interest, principal and any other money due on the debt securities at the corporate trust office of Computershare Trust Company, N.A. or such other office as may be agreed upon. Holders must make arrangements to have their payments picked up at or wired from that office or such other office as may be agreed upon. We may also choose to pay interest by mailing checks.

BOOK-ENTRY AND OTHER INDIRECT HOLDERS SHOULD CONSULT THEIR BANKS, BROKERS OR OTHER FINANCIAL INSTITUTIONS FOR INFORMATION ON HOW THEY WILL RECEIVE PAYMENTS

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We may also arrange for additional payment offices and may cancel or change these offices, including our use of the trustees' corporate trust offices. These offices are called paying agents. We may also choose to act as our own paying agent or choose one of our subsidiaries to do so. We must notify holders of changes in the paying agents for any particular series of debt securities.

Notices

We and the trustees will send notices regarding the debt securities only to registered holders, using their addresses as listed in the trustees' records. With respect to who is a registered holder for this purpose, see Legal Ownership and Book-Entry Issuance.

Regardless of who acts as paying agent, all money paid by us to a paying agent that remains unclaimed at the end of two years after the amount is due to holders will be repaid to us. After that two-year period, holders may look to us for payment and not to the trustees or any other paying agent.

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LEGAL OWNERSHIP AND BOOK-ENTRY ISSUANCE

In this section, we describe special considerations that will apply to registered debt securities issued in global i.e., book-entry, form. First we describe the difference between registered ownership and indirect ownership of registered debt securities. Then we describe special provisions that apply to global debt securities.

Who is the Legal Owner of a Registered Security?

Each debt security will be represented either by a certificate issued in definitive form to a particular investor or by one or more global debt securities representing debt securities. We refer to those who have debt securities registered in their own names, on the books that we or the trustees maintain for this purpose, as the registered holders of those debt securities. Subject to limited exceptions, we and the trustees are entitled to treat the registered holder of a debt security as the person exclusively entitled to vote, to receive notices, to receive any interest or other payment in respect of the debt security and to exercise all the rights and power as an owner of the debt security. We refer to those who own beneficial interests in debt securities that are not registered in their own names as indirect owners of those debt securities. As we discuss below, indirect owners are not registered holders, and investors in debt securities issued in book-entry form or in street name will be indirect owners.

Book-Entry Owners. Unless otherwise noted in an applicable prospectus supplement, we will issue each debt security in book-entry form only. This means debt securities will be represented by one or more global debt securities registered in the name of a financial institution that holds them as depository on behalf of other financial institutions that participate in the depository's book-entry system. These participating institutions, in turn, hold beneficial interests in the debt securities on behalf of themselves or their customers.

Under each indenture (and the Bank Act in the case of subordinated indebtedness), subject to limited exceptions and applicable law, only the person in whose name a debt security is registered is recognized as the holder of that debt security. Consequently, for debt securities issued in global form, we will recognize only the depository as the holder of the debt securities and we will make all payments on the debt securities, including deliveries of any property other than cash, to the depository. The depository passes along the payments it receives to its participants, which in turn pass the payments along to their customers who are the beneficial owners. The depository and its participants do so under agreements they have made with one another or with their customers; they are not obligated to do so under the terms of the debt securities.

As a result, investors will not own debt securities directly. Instead, they will own beneficial interests in a global debt security, through a bank, broker or other financial institution that participates in the depository's book-entry system or holds an interest through a participant. As long as the debt securities are issued in global form, investors will be indirect owners, and not registered holders, of the debt securities.

Street Name Owners. We may issue debt securities initially in non-global form or we may terminate an existing global debt security, as described below under *Holder's Option to Obtain a Non-Global Security; Special Situations When a Global Security Will Be Terminated*. In these cases, investors may choose to hold their debt securities in their own names or in street name. Debt securities held by an investor in street name would be registered in the name of a bank, broker or other financial institution that the investor chooses, and the investor would hold only a beneficial interest in those debt securities through an account he or she maintains at that institution.

For debt securities held in street name, we will, subject to limited exceptions and applicable law, recognize only the intermediary banks, brokers and other financial institutions in whose names the debt securities are registered as the holders of those debt securities, and we will make all payments on those debt securities, including deliveries of any property other than cash, to them. These institutions pass along the payments they receive to their customers who are the beneficial owners, but only because they agree to do so in their customer agreements or because they are legally required to do so. Investors who hold debt securities in street name will be indirect owners, not registered holders, of those debt securities.

Registered Holders. Subject to limited exceptions, our obligations, as well as the obligations of the trustees under any indenture and the obligations, if any, of any other third parties employed by us, run only to the registered holders of the debt securities. We do not have obligations to investors who hold beneficial interests in global debt securities, in street name or by any other indirect means. This will be the case whether an investor chooses to be an indirect owner of a debt security or has no choice because we are issuing the debt securities only in global form.

For example, once we make a payment or give a notice to the registered holder, we have no further responsibility for that payment or notice even if that holder is required, under agreements with depository participants or customers or by law, to pass it along to the indirect owners but does not do so. Similarly, if we want to obtain the approval of the holders for any purpose—for example, to amend the indenture for a series of debt securities or to relieve us of the consequences of a default or of our obligation to comply with a particular provision of an indenture—we would seek the approval only from the registered holders, and not the indirect owners, of the relevant debt securities. Whether and how the registered holders contact the indirect owners is up to the registered holders.

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When we refer to "you" in this prospectus, we mean all purchasers of the debt securities being offered by this prospectus and the applicable prospectus supplements, whether they are the registered holders or only indirect owners of those debt securities. When we refer to "your debt securities" in this prospectus, we mean the debt securities in which you will hold a direct or indirect interest.

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Special Considerations for Indirect Owners. If you hold debt securities through a bank, broker or other financial institution, either in book-entry form or in street name, you should check with your own institution to find out:

how it handles securities payments and notices;

whether it imposes fees or charges;

how it would handle a request for the holders' consent, if ever required;

how it would exercise rights under the debt securities if there were a default or other event triggering the need for holders to act to protect their interests; and

if the debt securities are in book-entry form, how the depository's rules and procedures will affect these matters.

What is a Global Security?

Unless otherwise noted in the applicable prospectus supplement, we will issue each debt security in book-entry form only. Each debt security issued in book-entry form will be represented by a global debt security that we deposit with and register in the name of one or more financial institutions or clearing systems, or their nominees, which we select. A financial institution or clearing system that we select for any debt security for this purpose is called the depository for that debt security. A debt security will usually have only one depository but it may have more. Each series of debt securities will have one or more of the following as the depositories:

The Depository Trust Company, New York, New York, which is known as DTC ;

Euroclear Bank S.A./N.V., as operator of the Euroclear System, which is known as Euroclear ;

Clearstream Banking, société anonyme, which is known as Clearstream ; or

any other clearing system or financial institution named in the applicable prospectus supplements.

The depositories named above may also be participants in one another's systems. Thus, for example, if DTC is the depository for a global debt security, investors may hold beneficial interests in that debt security through Euroclear or Clearstream, as DTC participants. The depository or depositories for your debt securities will be named in the applicable prospectus supplements; if none is named, the depository will be DTC.

A global debt security may represent one or any other number of individual debt securities. Generally, all debt securities represented by the same global debt security will have the same terms. We may, however, issue a global debt security that represents multiple debt securities of the same kind, such as debt securities that have different terms and are issued at different times. We call this kind of global debt security a master global debt security. The applicable prospectus supplements will not indicate whether your debt securities are represented by a master global debt security.

A global debt security may not be transferred to or registered in the name of anyone other than the depository or its nominee, unless special termination situations arise. We describe those situations below under Holder's Option to Obtain a Non-Global Security; Special Situations When a Global Security Will Be Terminated. As a result of these arrangements, the depository, or its nominee, will be the sole registered owner and holder of all debt securities represented by a global debt security, and investors will be permitted to own only indirect interests in a global debt

security. Indirect interests must be held by means of an account with a broker, bank or other financial institution that in turn has an account with the depository or with another institution that does. Thus, an investor whose debt security is represented by a global debt security will not be a holder of the debt security, but only an indirect owner of an interest in the global debt security.

If an applicable prospectus supplement for a particular debt security indicates that the debt security will be issued in global form only, then the debt security will be represented by a global debt security at all times unless and until the global debt security is terminated. We describe the situations in which this can occur below under *Holder's Option to Obtain a Non-Global Security; Special Situations When a Global Security Will Be Terminated*. If termination occurs, we may issue the debt securities through another book-entry clearing system or decide that the debt securities may no longer be held through any book-entry clearing system.

Special Considerations for Global Securities. As an indirect owner, an investor's rights relating to a global debt security will be governed by the account rules of the depository and those of the investor's bank, broker, financial institution or other intermediary through which it holds its interest (such as Euroclear or Clearstream, if DTC is the depository), as well as general laws relating to securities transfers. We do not recognize this type of investor or any intermediary as a holder of debt securities and instead deal only with the depository that holds the global debt security.

If debt securities are issued only in the form of a global debt security, an investor should be aware of the following:

an investor cannot cause the debt securities to be registered in his or her own name, and cannot obtain non-global certificates for his or her interest in the debt securities, except in the special situations we describe below;

an investor will be an indirect holder and must look to his or her own bank, broker or other financial institution for payments on the debt securities and protection of his or her legal rights relating to the debt securities, as we describe above under *Who is the Legal Owner of a Registered Security?* ;

an investor may not be able to sell interests in the debt securities to some insurance companies and other institutions that are required by law to own their debt securities in non-book-entry form;

an investor may not be able to pledge his or her interest in a global debt security in circumstances in which certificates representing the debt securities must be delivered to the lender or other beneficiary of the pledge in order for the pledge to be effective;

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the depositary's policies will govern payments, deliveries, transfers, exchanges, notices and other matters relating to an investor's interest in a global debt security, and those policies may change from time to time. We and the trustees will have no responsibility for any aspect of the depositary's policies, actions or records of ownership interests in a global debt security. We and the trustees also do not supervise the depositary in any way;

the depositary may require that those who purchase and sell interests in a global debt security within its book-entry system use immediately available funds and your bank, broker or other financial institution may require you to do so as well; and

financial institutions that participate in the depositary's book-entry system and through which an investor holds its interest in the global debt securities, directly or indirectly, may also have their own policies affecting payments, deliveries, transfers, exchanges, notices and other matters relating to the debt securities, and those policies may change from time to time. For example, if you hold an interest in a global debt security through Euroclear or Clearstream, when DTC is the depositary, Euroclear or Clearstream, as applicable, may require those who purchase and sell interests in that debt security through them to use immediately available funds and comply with other policies and procedures, including deadlines for giving instructions as to transactions that are to be effected on a particular day. There may be more than one financial intermediary in the chain of ownership for an investor. We and the trustees do not monitor and are not responsible for the policies or actions or records of ownership interests of any of those intermediaries.

Holder's Option to Obtain a Non-Global Security; Special Situations When a Global Security Will Be Terminated. If we issue any series of debt securities in book-entry form but we choose to give the beneficial owners of that series the right to obtain non-global debt securities, any beneficial owner entitled to obtain non-global debt securities may do so by following the applicable procedures of the depositary, any transfer agent or registrar for that series and that owner's bank, broker or other financial institution through which that owner holds its beneficial interest in the debt securities. If you are entitled to request a non-global certificate and wish to do so, you will need to allow sufficient lead time to enable us or our agent to prepare the requested certificate.

In addition, in a few special situations described below, a global debt security will be terminated and interests in it will be exchanged for certificates in non-global form representing the debt securities it represented. After that exchange, the choice of whether to hold the debt securities directly or in street name will be up to the investor. Investors must consult their own banks, brokers or other financial institutions, to find out how to have their interests in a global debt security transferred on termination to their own names, so that they will be holders. We have described the rights of holders and street name investors above under "Who is the Legal Owner of a Registered Security?".

The special situations for termination of a global debt security are as follows:

if the depositary notifies us that it is unwilling, unable or no longer qualified to continue as depositary for that global debt security and we do not appoint another institution to act as depositary within 60 days;

if we notify the trustees that we wish to terminate that global debt security; or

if an event of default has occurred with regard to these debt securities and has not been cured or waived.

If a global debt security is terminated, only the depositary, and neither we nor the trustees for any debt securities, is responsible for deciding the names of the institutions in whose names the debt securities represented by the global debt security will be registered and, therefore, who will be the registered holders of those debt securities.

Considerations Relating to DTC

DTC has informed us that it is a limited-purpose trust company organized under the New York Banking Law, a banking organization within the meaning of the New York Banking Law, a member of the Federal Reserve System, a clearing corporation within the meaning of the New York Uniform Commercial Code, and a clearing agency registered pursuant to the provisions of Section 17A of the Exchange Act. DTC holds securities that DTC participants deposit with DTC. DTC also facilitates the settlement among DTC participants of securities transactions, such as transfers and pledges, in deposited securities through electronic computerized book-entry changes in DTC participants' accounts, thereby eliminating the need for physical movement of certificates. DTC participants include securities brokers and dealers, banks, trust companies and

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clearing corporations, and may include other organizations. DTC is owned by a number of its direct participants and by the New York Stock Exchange, Inc. and the Financial Industry Regulatory Authority, Inc. Indirect access to the DTC system also is available to others such as banks, brokers, dealers and trust companies that clear through or maintain a custodial relationship with a participant, either directly or indirectly. The rules applicable to DTC and DTC participants are on file with the SEC.

Purchases of debt securities within the DTC system must be made by or through DTC participants, who will receive a credit for the debt securities on DTC's records. Transfers of ownership interests in the debt securities are accomplished by entries made on the books of participants acting on behalf of beneficial owners.

Redemption notices will be sent to DTC's nominee, Cede & Co., as the registered holder of the debt securities. If less than all of the debt securities are being redeemed, DTC will determine the amount of the interest of each direct participant to be redeemed in accordance with its then-current procedures.

In instances in which a vote is required, neither DTC nor Cede & Co. will itself consent or vote with respect to the debt securities. Under its usual procedures, DTC would mail an omnibus proxy to the relevant trustee as soon as possible after the record date. The omnibus proxy assigns Cede & Co.'s consenting or voting rights to those direct participants to whose accounts such debt securities are credited on the record date (identified in a listing attached to the omnibus proxy).

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Distribution payments on the debt securities will be made by the relevant trustee to DTC. DTC's usual practice is to credit direct participants accounts on the relevant payment date in accordance with their respective holdings shown on DTC's records unless DTC has reason to believe that it will not receive payments on such payment date. Payments by participants to beneficial owners will be governed by standing instructions and customary practices and will be the responsibility of such participants and not of DTC, the relevant trustee or us, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of distributions to DTC is the responsibility of the relevant trustee, and disbursements of such payments to the beneficial owners are the responsibility of direct and indirect participants.

The information in this section concerning DTC and DTC's book-entry system has been obtained from sources that we believe to be accurate, but we assume no responsibility for the accuracy thereof. We do not have any responsibility for the performance by DTC or its participants of their respective obligations as described herein or under the rules and procedures governing their respective operations.

Considerations Relating to Clearstream and Euroclear

Clearstream and Euroclear are securities clearance systems in Europe. Clearstream and Euroclear have respectively informed us that Clearstream and Euroclear each hold securities for their customers and facilitate the clearance and settlement of securities transactions by electronic book-entry transfer between their respective account holders. Clearstream and Euroclear provide various services including safekeeping, administration, clearance and settlement of internationally traded securities and securities lending and borrowing. Clearstream and Euroclear also deal with domestic securities markets in several countries through established depository and custodial relationships. Clearstream and Euroclear have established an electronic bridge between their two systems across which their respective participants may settle trades with each other. Clearstream and Euroclear customers are world-wide financial institutions including underwriters, securities brokers and dealers, banks, trust companies and clearing corporations. Indirect access to Clearstream and Euroclear is available to other institutions that clear through or maintain a custodial relationship with an account holder of either system.

Euroclear and Clearstream may be depositaries for a global debt security. In addition, if DTC is the depository for a global debt security, Euroclear and Clearstream may hold interests in the global debt security as participants in DTC.

As long as any global debt security is held by Euroclear or Clearstream, as depository, you may hold an interest in the global debt security only through an organization that participates, directly or indirectly, in Euroclear or Clearstream. If Euroclear or Clearstream is the depository for a global debt security and there is no depository in the United States, you will not be able to hold interests in that global debt security through any securities clearance system in the United States.

Payments, deliveries, transfers, exchanges, notices and other matters relating to the debt securities made through Euroclear or Clearstream must comply with the rules and procedures of those systems. Those systems could change their rules and procedures at any time. We have no control over those systems or their participants and we take no responsibility for their activities. Transactions between participants in Euroclear or Clearstream, on one hand, and participants in DTC, on the other hand, when DTC is the depository, would also be subject to DTC's rules and procedures.

Special Timing Considerations Relating to Transactions in Euroclear and Clearstream. Investors will be able to make and receive through Euroclear and Clearstream payments, deliveries, transfers, exchanges, notices and other transactions involving any debt securities held through those systems only on days when those systems are open for business. Those systems may not be open for business on days when banks, brokers and other financial institutions are open for business in the United States.

In addition, because of time-zone differences, U.S. investors who hold their interests in the debt securities through these systems and wish to transfer their interests, or to receive or make a payment or delivery or exercise any other right with respect to their interests, on a particular day may find that the transaction will not be effected until the next business day in Luxembourg or Brussels, as applicable. Thus, investors who wish to exercise rights that expire on a particular day may need to act before the expiration date. In addition, investors who hold their interests through both DTC and Euroclear or Clearstream may need to make special arrangements to finance any purchases or sales of their interests between the U.S. and European clearing systems, and those transactions may settle later than would be the case for transactions within one clearing system.

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UNITED STATES TAXATION

This section describes the material United States federal income tax consequences to a United States holder (as defined below) of owning the securities we are offering. It is the opinion of Allen & Overy LLP, counsel to the Bank. It applies to you only if you acquire your securities at their original issuance, and you hold your securities as capital assets for United States federal income tax purposes. This section does not apply to you if you are a member of a class of holders subject to special rules, such as:

a dealer in securities or currencies,

a trader in securities that elects to use a mark-to-market method of accounting for your securities holdings,

a bank,

a life insurance company,

a tax-exempt organization,

a person that actually or constructively owns 10% or more of our voting stock,

a person that holds securities as part of a straddle or a hedging or conversion transaction, or

a person whose functional currency for tax purposes is not the U.S. dollar.

This section is based on the Internal Revenue Code of 1986, as amended (the *Code*), its legislative history, existing and proposed regulations under the Code, published rulings and court decisions, as well as the income tax treaty between the United States and Canada (the *Treaty*), all as currently in effect. These laws are subject to change, possibly on a retroactive basis.

If a partnership holds the securities, the United States federal income tax treatment of a partner will generally depend on the status of the partner and the tax treatment of the partnership. A partner in a partnership holding the securities should consult its tax advisor with regard to the United States federal income tax treatment of an investment in the securities. This summary does not address tax consequences applicable to holders of equity interests in a holder of the securities, U.S. federal estate, gift or alternative minimum tax considerations, or non-U.S., state or local tax considerations.

Please consult your own tax advisor concerning the consequences of owning these securities in your particular circumstances under the Code and the laws of any other taxing jurisdiction.

You are a United States holder if you are a beneficial owner of a security and you are:

a citizen or individual resident of the United States,

a domestic corporation,

an estate whose income is subject to United States federal income tax regardless of its source, or

a trust if a United States court can exercise primary supervision over the trust's administration and one or more United States persons are authorized to control all substantial decisions of the trust.

Tax consequences to holders of our shares

This subsection discusses tax consequences relevant to the purchase, ownership and disposition of our shares. Additional United States federal income tax consequences relevant to certain preferred shares are not described in this prospectus and will be discussed in an applicable prospectus supplement.

Taxation of Dividends

The gross amount of any dividend we pay out of our current or accumulated earnings and profits (as determined for United States federal income tax purposes) is subject to United States federal income taxation. If you are a noncorporate United States holder, dividends paid to you in taxable years beginning before January 1, 2013 that constitute qualified dividend income will be taxable to you at a maximum tax rate of 15% provided that (i) the Bank is a qualified foreign corporation and (ii) you hold the shares for more than 60 days during the 121 day period beginning 60 days before the ex-dividend date (or, in the case of preferred stock, if the dividend is attributable to a period or periods aggregating over 366 days, provided that you hold the shares for more than 90 days during the 181 day period beginning 90 days before the ex-dividend date) and meet other holding period requirements. The Bank generally will be a qualified foreign corporation if (1) it is either (a) eligible for the benefits of the Treaty, or (b) if the stock with respect to which such dividend is paid is readily tradable on an established securities market in the United States, and (2) it is not a PFIC (as defined below) in the taxable year of the distribution or the immediately preceding taxable year. The Bank expects to be eligible for the benefits of the Treaty. In addition, as discussed below under PFIC Rules, the Bank does not believe it should be treated as a PFIC for the current year or any future years.

The dividend is taxable to you when you receive the dividend, actually or constructively. The dividend will not be eligible for the dividends-received deduction generally allowed to United States corporations in respect of dividends received from other United States corporations. The amount of the dividend distribution that you must include in your income as a United States holder will be the U.S. dollar value of the Canadian payments made, determined at the spot Canadian dollar/U.S. dollar rate on the date the dividend distribution is includible in your income, regardless of whether the payment is in fact converted into U.S. dollars. Generally, any gain or loss resulting from currency exchange fluctuations during the period from the date you include the dividend

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payment in income to the date you convert the payment into U.S. dollars will be treated as ordinary income or loss and will not be eligible for the special tax rate applicable to qualified dividend income. The gain or loss generally will be income or loss from sources within the United States for foreign tax credit limitation purposes. Distributions in excess of current and accumulated earnings and profits (as determined for United States federal income tax purposes) will be treated as a non-taxable return of capital to the extent of your basis in the shares and thereafter as capital gain. We do not expect to maintain calculations of earnings and profits for U.S. federal income tax purposes. Therefore, a United States holder should expect that such distribution will generally be treated as a dividend.

For foreign tax credit limitation purposes, dividends will be income from sources outside the United States and will, depending on your circumstances, be either passive or general income for foreign tax credit limitation purposes. The rules relating to the determination of the U.S. foreign tax credit, or deduction in lieu of the U.S. foreign tax credit, are complex and you should consult your tax advisors with respect to these rules.

Sale or Exchange of Shares

If you are a United States holder and you sell or otherwise dispose of your shares, you will recognize capital gain or loss for United States federal income tax purposes equal to the difference between the U.S. dollar value of the amount that you realize and your tax basis, determined in U.S. dollars, in your shares. Capital gain of a noncorporate United States holder is generally taxed at preferential rates where the property is held for more than one year. The deductibility of capital losses is subject to limitations. The gain or loss will generally be income or loss from sources within the United States for foreign tax credit limitation purposes.

PFIC Rules

We believe that our shares should not be treated as stock of a Passive Foreign Investment Company (a PFIC) for United States federal income tax purposes, but this conclusion is a factual determination that is made annually and thus may be subject to change. Any subsequent determinations that we make with respect to our PFIC status will be discussed in an applicable prospectus supplement.

In general, if you are a United States holder, we will be a PFIC with respect to you if for any taxable year in which you held our shares:

at least 75% of our gross income for the taxable year is passive income, or

at least 50% of the value, determined on the basis of a quarterly average, of our assets is attributable to assets that produce or are held for the production of passive income.

Passive income generally includes dividends, interest, royalties, rents (other than certain rents and royalties derived in the active conduct of a trade or business), annuities and gains from assets that produce passive income. If a foreign corporation owns at least 25% by value of the stock of another corporation, the foreign corporation is treated for purposes of the PFIC tests as owning its proportionate share of the assets of the other corporation, and as receiving directly its proportionate share of the other corporation's income. For this purpose, income derived in the active conduct of our banking business should not be treated as passive income.

Tax consequences to holders of our debt securities

This subsection deals only with debt securities that are due to mature 30 years or less from the date on which they are issued and whose terms are described in this prospectus. The United States federal income tax consequences of owning debt securities that are due to mature more than 30 years from their date of issue and debt securities whose terms are not described in this prospectus will be discussed in an applicable prospectus supplement.

Payments of Interest

Except as described below in the case of interest on a discount debt security that is not qualified stated interest, each as defined below under

Original Issue Discount General, you will be taxed on any interest on your debt security, whether payable in U.S. dollars or a foreign currency, including a composite currency or basket of currencies other than U.S. dollars, as ordinary income at the time you receive the interest or when it accrues, depending on your method of accounting for tax purposes.

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Interest that we pay on the debt securities and original issue discount, if any, accrued with respect to the debt securities (as described below under **Original Issue Discount**) is income from sources outside the United States subject to the rules regarding the foreign tax credit allowable to a United States holder. Under the foreign tax credit rules, interest and original issue discount and additional amounts will, depending on your circumstances, be either **passive** or **general** income for purposes of computing the foreign tax credit.

Cash Basis Taxpayers. If you are a taxpayer that uses the cash receipts and disbursements method of accounting for tax purposes and you receive an interest payment that is denominated in, or determined by reference to, a foreign currency, you must recognize income equal to the U.S. dollar value of the interest payment, based on the exchange rate in effect on the date of receipt, regardless of whether you actually convert the payment into U.S. dollars.

Accrual Basis Taxpayers. If you are a taxpayer that uses an accrual method of accounting for tax purposes, you may determine the amount of income that you recognize with respect to an interest payment denominated in, or determined by reference to, a foreign currency by using one of two methods. Under the first method, you will determine the amount of income accrued based on the average exchange rate in effect during the interest accrual period or, with respect to an accrual period that spans two taxable years, that part of the period within the taxable year.

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If you elect the second method, you would determine the amount of income accrued on the basis of the exchange rate in effect on the last day of the accrual period, or, in the case of an accrual period that spans two taxable years, the exchange rate in effect on the last day of the part of the period within the taxable year. Additionally, under this second method, if you receive a payment of interest within five business days of the last day of your accrual period or taxable year, you may instead translate the interest accrued into U.S. dollars at the exchange rate in effect on the day that you actually receive the interest payment. If you elect the second method it will apply to all debt instruments that you hold at the beginning of the first taxable year to which the election applies and to all debt instruments that you subsequently acquire. You may not revoke this election without the consent of the Internal Revenue Service.

When you actually receive an interest payment, including a payment attributable to accrued but unpaid interest upon the sale or retirement of your debt security, denominated in, or determined by reference to, a foreign currency for which you accrued an amount of income, you will recognize ordinary income or loss measured by the difference, if any, between the exchange rate that you used to accrue interest income and the exchange rate in effect on the date of receipt, regardless of whether you actually convert the payment into U.S. dollars.

Original Issue Discount

General. If you own a debt security, other than a short-term debt security with a term of one year or less, it will be treated as a discount debt security issued at an original issue discount if the amount by which the debt security's stated redemption price at maturity exceeds its issue price is more than a de minimis amount. Generally, a debt security's issue price will be the first price at which a substantial amount of debt securities included in the issue of which the debt security is a part is sold to persons other than bond houses, brokers, or similar persons or organizations acting in the capacity of underwriters, placement agents, or wholesalers. A debt security's stated redemption price at maturity is the total of all payments provided by the debt security that are not payments of qualified stated interest. Generally, an interest payment on a debt security is qualified stated interest if it is one of a series of stated interest payments on a debt security that are unconditionally payable at least annually at a single fixed rate, with certain exceptions for lower rates paid during some periods, applied to the outstanding principal amount of the debt security. There are special rules for variable rate debt securities that are discussed under [Variable Rate Debt Securities](#).

In general, your debt security is not a discount debt security if the amount by which its stated redemption price at maturity exceeds its issue price is less than the de minimis amount of 1/4 of 1% of its stated redemption price at maturity multiplied by the number of complete years to its maturity. Your debt security will have de minimis original issue discount if the amount of the excess is less than the de minimis amount. If your debt security has de minimis original issue discount, you must include the de minimis amount in income as stated principal payments are made on the debt security, unless you make the election described below under [Election to Treat All Interest as Original Issue Discount](#). You can determine the includible amount with respect to each such payment by multiplying the total amount of your debt security's de minimis original issue discount by a fraction equal to:

the amount of the principal payment made
divided by:

the stated principal amount of the debt security.

Generally, if your discount debt security matures more than one year from its date of issue, you must include original issue discount, or OID, in income before you receive cash attributable to that income. The amount of OID that you must include in income is calculated using a constant-yield method, and generally you will include increasingly greater amounts of OID in income over the life of your debt security. More specifically, you can calculate the amount of OID that you must include in income by adding the daily portions of OID with respect to your discount debt security for each day during the taxable year or portion of the taxable year that you hold your discount debt security. You can determine the daily portion by allocating to each day in any accrual period a pro rata portion of the OID allocable to that accrual period. You may select an accrual period of any length with respect to your discount debt security and you may vary the length of each accrual period over the term of your discount debt security. However, no accrual period may be longer than one year and each scheduled payment of interest or principal on the discount debt security must occur on either the first or final day of an accrual period.

You can determine the amount of OID allocable to an accrual period by:

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multiplying your discount debt security's adjusted issue price at the beginning of the accrual period by your debt security's yield to maturity, and then

subtracting from this figure the sum of the payments of qualified stated interest on your debt security allocable to the accrual period. You must determine the discount debt security's yield to maturity on the basis of compounding at the close of each accrual period and adjusting for the length of each accrual period. Further, you determine your discount debt security's adjusted issue price at the beginning of any accrual period by:

adding your discount debt security's issue price and any accrued OID for each prior accrual period, and then

subtracting any payments previously made on your discount debt security that were not qualified stated interest payments. If an interval between payments of qualified stated interest on your discount debt security contains more than one accrual period, then, when you determine the amount of OID allocable to an accrual period, you must allocate the amount of qualified stated interest payable at the end of the interval, including any qualified stated interest that is payable on the first day of the accrual period immediately following the interval, pro rata to each accrual period in the interval based on their relative lengths. In addition, you

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must increase the adjusted issue price at the beginning of each accrual period in the interval by the amount of any qualified stated interest that has accrued prior to the first day of the accrual period but that is not payable until the end of the interval. You may compute the amount of OID allocable to an initial short accrual period by using any reasonable method if all other accrual periods, other than a final short accrual period, are of equal length.

The amount of OID allocable to the final accrual period is equal to the difference between:

the amount payable at the maturity of your debt security, other than any payment of qualified stated interest, and

your debt security's adjusted issue price as of the beginning of the final accrual period.

Acquisition Premium. If you purchase your debt security for an amount that is less than or equal to the sum of all amounts, other than qualified stated interest, payable on your debt security after the purchase date but is greater than the amount of your debt security's adjusted issue price, as determined above under General, the excess is acquisition premium. If you do not make the election described below under Election to Treat All Interest as Original Issue Discount, then you must reduce the daily portions of OID by a fraction equal to:

the excess of your adjusted basis in the debt security immediately after purchase over the adjusted issue price of the debt security divided by:

the excess of the sum of all amounts payable, other than qualified stated interest, on the debt security after the purchase date over the debt security's adjusted issue price.

Pre-Issuance Accrued Interest. An election may be made to decrease the issue price of your debt security by the amount of pre-issuance accrued interest if:

a portion of the initial purchase price of your debt security is attributable to pre-issuance accrued interest,

the first stated interest payment on your debt security is to be made within one year of your debt security's issue date, and

the payment will equal or exceed the amount of pre-issuance accrued interest.

If this election is made, a portion of the first stated interest payment will be treated as a return of the excluded pre-issuance accrued interest and not as an amount payable on your debt security.

Debt Securities Subject to Contingencies Including Optional Redemption. Your debt security is subject to a contingency if it provides for an alternative payment schedule or schedules applicable upon the occurrence of a contingency or contingencies, other than a remote or incidental contingency, whether such contingency relates to payments of interest or of principal. In such a case, you must determine the yield and maturity of your debt security by assuming that the payments will be made according to the payment schedule most likely to occur if:

the timing and amounts of the payments that comprise each payment schedule are known as of the issue date, and

one of such schedules is significantly more likely than not to occur.

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If there is no single payment schedule that is significantly more likely than not to occur, other than because of a mandatory sinking fund, you must include income on your debt security in accordance with the general rules that govern contingent payment obligations. These rules will be discussed in an applicable prospectus supplement.

Notwithstanding the general rules for determining yield and maturity, if your debt security is subject to contingencies, and either you or we have an unconditional option or options that, if exercised, would require payments to be made on the debt security under an alternative payment schedule or schedules, then:

in the case of an option or options that we may exercise, we will be deemed to exercise or not exercise an option or combination of options in the manner that minimizes the yield on your debt security, and

in the case of an option or options that you may exercise, you will be deemed to exercise or not exercise an option or combination of options in the manner that maximizes the yield on your debt security.

If both you and we hold options described in the preceding sentence, those rules will apply to each option in the order in which they may be exercised. You may determine the yield on your debt security for the purposes of those calculations by using any date on which your debt security may be redeemed or repurchased as the maturity date and the amount payable on the date that you chose in accordance with the terms of your debt security as the principal amount payable at maturity.

If a contingency, including the exercise of an option, actually occurs or does not occur contrary to an assumption made according to the above rules then, except to the extent that a portion of your debt security is repaid as a result of this change in circumstances and solely to determine the amount and accrual of OID, you must redetermine the yield and maturity of your debt security by treating your debt security as having been retired and reissued on the date of the change in circumstances for an amount equal to your debt security's adjusted issue price on that date.

Election to Treat All Interest as Original Issue Discount. You may elect to include in gross income all interest that accrues on your debt security using the constant-yield method described above under General, with the modifications described below. For purposes of this election, interest will include stated interest, OID, de minimis original issue discount, market discount, de minimis market discount and unstated interest, as adjusted by any amortizable bond premium, described below under Debt Securities Purchased at a Premium, or acquisition premium.

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If you make this election for your debt security, then, when you apply the constant-yield method:

the issue price of your debt security will equal your cost,

the issue date of your debt security will be the date you acquired it, and

no payments on your debt security will be treated as payments of qualified stated interest.

Generally, this election will apply only to the debt security for which you make it; however, if the debt security has amortizable bond premium, you will be deemed to have made an election to apply amortizable bond premium against interest for all debt instruments with amortizable bond premium, other than debt instruments the interest on which is excludible from gross income, that you hold as of the beginning of the taxable year to which the election applies or any taxable year thereafter. Additionally, if you make this election for a market discount debt security, you will be treated as having made the election discussed below under **Debt Securities Purchased with Market Discount** to include market discount in income currently over the life of all debt instruments having market discount that you acquire on or after the first day of the first taxable year to which the election applies. You may not revoke any election to apply the constant-yield method to all interest on a debt security or the deemed elections with respect to amortizable bond premium or market discount debt securities without the consent of the Internal Revenue Service.

Variable Rate Debt Securities. Your debt security will be a variable rate debt security if:

your debt security's issue price does not exceed the total noncontingent principal payments by more than the lesser of:

1. 0.015 multiplied by the product of the total noncontingent principal payments and the number of complete years to maturity from the issue date, or
2. 15% of the total noncontingent principal payments; and

your debt security provides for stated interest, compounded or paid at least annually, only at:

1. one or more qualified floating rates,
2. a single fixed rate and one or more qualified floating rates,
3. a single objective rate, or
4. a single fixed rate and a single objective rate that is a qualified inverse floating rate; and

your debt security satisfies certain other conditions.

Your debt security will have a variable rate that is a qualified floating rate if:

variations in the value of the rate can reasonably be expected to measure contemporaneous variations in the cost of newly borrowed funds in the currency in which your debt security is denominated; or

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the rate is equal to such a rate multiplied by either:

5. a fixed multiple that is greater than 0.65 but not more than 1.35, or
6. a fixed multiple greater than 0.65 but not more than 1.35, increased or decreased by a fixed rate; and

the value of the rate on any date during the term of your debt security is set no earlier than three months prior to the first day on which that value is in effect and no later than one year following that first day.

If your debt security provides for two or more qualified floating rates that are within 0.25 percentage points of each other on the issue date or can reasonably be expected to have approximately the same values throughout the term of the debt security, the qualified floating rates together constitute a single qualified floating rate.

Your debt security will not have a qualified floating rate, however, if the rate is subject to certain restrictions (including caps, floors, governors, or other similar restrictions) unless such restrictions are fixed throughout the term of the debt security or are not reasonably expected to significantly affect the yield on the debt security.

Your debt security will have a variable rate that is a single objective rate if:

the rate is not a qualified floating rate,

the rate is determined using a single, fixed formula that is based on objective financial or economic information that is not within the control of or unique to the circumstances of the issuer or a related party, and

the value of the rate on any date during the term of your debt security is set no earlier than three months prior to the first day on which that value is in effect and no later than one year following that first day.

Your debt security will not have a variable rate that is an objective rate, however, if it is reasonably expected that the average value of the rate during the first half of your debt security's term will be either significantly less than or significantly greater than the average value of the rate during the final half of your debt security's term.

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An objective rate as described above is a qualified inverse floating rate if:

the rate is equal to a fixed rate minus a qualified floating rate, and

the variations in the rate can reasonably be expected to inversely reflect contemporaneous variations in the cost of newly borrowed funds.

Your debt security will also have a single qualified floating rate or an objective rate if interest on your debt security is stated at a fixed rate for an initial period of one year or less followed by either a qualified floating rate or an objective rate for a subsequent period, and either:

the fixed rate and the qualified floating rate or objective rate have values on the issue date of the debt security that do not differ by more than 0.25 percentage points, or

the value of the qualified floating rate or objective rate is intended to approximate the fixed rate.

In general, if your variable rate debt security provides for stated interest at a single qualified floating rate or objective rate, or one of those rates after a single fixed rate for an initial period, all stated interest on your debt security is qualified stated interest. In this case, the amount of OID, if any, is determined by using, in the case of a qualified floating rate or qualified inverse floating rate, the value as of the issue date of the qualified floating rate or qualified inverse floating rate, or, for any other objective rate, a fixed rate that reflects the yield reasonably expected for your debt security.

If your variable rate debt security does not provide for stated interest at a single qualified floating rate or a single objective rate, and also does not provide for interest payable at a fixed rate other than a single fixed rate for an initial period, you generally must determine the interest and OID accruals on your debt security by:

determining a fixed rate substitute for each variable rate provided under your variable rate debt security,

constructing the equivalent fixed rate debt instrument, using the fixed rate substitute described above,

determining the amount of qualified stated interest and OID with respect to the equivalent fixed rate debt instrument, and

adjusting for actual variable rates during the applicable accrual period.

When you determine the fixed rate substitute for each variable rate provided under the variable rate debt security, you generally will use the value of each variable rate as of the issue date or, for an objective rate that is not a qualified inverse floating rate, a rate that reflects the reasonably expected yield on your debt security.

If your variable rate debt security provides for stated interest either at one or more qualified floating rates or at a qualified inverse floating rate, and also provides for stated interest at a single fixed rate other than at a single fixed rate for an initial period, you generally must determine interest and OID accruals by using the method described in the previous paragraph. However, your variable rate debt security will be treated, for purposes of the first three steps of the determination, as if your debt security had provided for a qualified floating rate, or a qualified inverse floating rate, rather than the fixed rate. The qualified floating rate, or qualified inverse floating rate, that replaces the fixed rate must be such that the fair market value of your variable rate debt security as of the issue date approximates the fair market value of an otherwise identical debt instrument that provides for the qualified floating rate, or qualified inverse floating rate, rather than the fixed rate.

Short-Term Debt Securities. In general, if you are an individual or other cash basis United States holder of a short-term debt security, you are not required to accrue OID, as specially defined below for the purposes of this paragraph, for United States federal income tax purposes unless you elect to do so (although it is possible that you may be required to include any stated interest in income as you receive it). If you are an accrual basis taxpayer, a taxpayer in a special class, including, but not limited to, a regulated investment company, common trust fund, or a certain type of pass-through entity, or a cash basis taxpayer who so elects, you will be required to accrue OID on short-term debt securities on either a straight-line basis or under the constant-yield method, based on daily compounding. If you are not required and do not elect to include OID in income currently, any gain you realize on the sale or retirement of your short-term debt security will be ordinary income to the extent of the accrued OID, which will be determined on a straight-line basis unless you make an election to accrue the OID under the constant-yield method, through the date of sale or retirement. However, if you are not required and do not elect to accrue OID on your short-term debt securities, you will be required to defer deductions for interest on borrowings allocable to your short-term debt securities in an amount not exceeding the deferred income until the deferred income is realized.

When you determine the amount of OID subject to these rules, you must include all interest payments on your short-term debt security, including stated interest, in your short-term debt security's stated redemption price at maturity.

Foreign Currency Discount Debt Securities. If your discount debt security is denominated in, or determined by reference to, a foreign currency, you must determine OID for any accrual period on your discount debt security in the foreign currency and then translate the amount of OID into U.S. dollars in the same manner as stated interest accrued by an accrual basis United States holder, as described under Tax consequences to holders of our debt securities Payments of Interest. You may recognize ordinary income or loss when you receive an amount attributable to OID in connection with a payment of interest or the sale or retirement of your debt security.

Debt Securities Purchased at a Premium

If you purchase your debt security for an amount in excess of its principal amount, you may elect to treat the excess as amortizable bond premium. If you make this election, you will reduce the amount required to be included in your income each year

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with respect to interest on your debt security by the amount of amortizable bond premium allocable to that year, based on your debt security's yield to maturity. If your debt security is denominated in, or determined by reference to, a foreign currency, you will compute your amortizable bond premium in units of the foreign currency and your amortizable bond premium will reduce your interest income in units of the foreign currency. Gain or loss recognized that is attributable to changes in exchange rates between the time your amortized bond premium offsets interest income and the time of the acquisition of your debt security is generally taxable as ordinary income or loss. If you make an election to amortize bond premium, it will apply to all debt instruments, other than debt instruments the interest on which is excludible from gross income, that you hold at the beginning of the first taxable year to which the election applies or that you thereafter acquire, and you may not revoke it without the consent of the Internal Revenue Service. See also Original Issue Discount Election to Treat All Interest as Original Issue Discount.

Debt Securities Purchased with Market Discount

You will be treated as if you purchased your debt security, other than a short-term debt security, at a market discount, and your debt security will be a market discount debt security if:

In the case of an initial purchaser, you purchase your debt security for less than its issue price as determined above under Original Issue Discount General, and

the difference between the debt security's stated redemption price at maturity or, in the case of a discount debt security, the debt security's revised issue price, and the price you paid for your debt security is equal to or greater than 1/4 of 1% of your debt security's stated redemption price at maturity or revised issue price, respectively, multiplied by the number of complete years to the debt security's maturity. To determine the revised issue price of a discount debt security for these purposes, you generally add any OID that has accrued on the notes prior to your acquisition of the notes to its issue price.

If your debt security's stated redemption price at maturity or, in the case of a discount debt security, its revised issue price, exceeds the price you paid for the debt security by less than 1/4 of 1% multiplied by the number of complete years to the debt security's maturity, the excess constitutes de minimis market discount, and the rules discussed below are not applicable to you.

You must treat any gain you recognize on the maturity or disposition of your market discount debt security as ordinary income to the extent of the accrued market discount on your debt security. Alternatively, you may elect to include market discount in income currently over the life of your debt security. If you make this election, it will apply to all debt instruments with market discount that you acquire on or after the first day of the first taxable year to which the election applies. You may not revoke this election without the consent of the Internal Revenue Service. If you own a market discount debt security and do not make this election, you will generally be required to defer deductions for interest on borrowings allocable to your debt security in an amount not exceeding the accrued market discount on your debt security until the maturity or disposition of your debt security.

You will accrue market discount on your market discount debt security on a straight-line basis unless you elect to accrue market discount using a constant-yield method. If you make this election, it will apply only to the debt security with respect to which it is made and you may not revoke it.

Purchase, Sale and Retirement of the Debt Securities

Your tax basis in your debt security will generally be the U.S. dollar cost, as defined below, of your debt security, adjusted by:

adding any OID or market discount previously included in income with respect to your debt security, and then

subtracting any payments on your debt security that are not qualified stated interest payments and any amortizable bond premium applied to reduce interest on your debt security.

If you purchase your debt security with foreign currency, the U.S. dollar cost of your debt security will generally be the U.S. dollar value of the purchase price on the date of purchase. However, if you are a cash basis taxpayer, or an accrual basis taxpayer if you so elect, and your debt security is traded on an established securities market, as defined in the applicable Treasury regulations, the U.S. dollar cost of your debt security

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will be the U.S. dollar value of the purchase price on the settlement date of your purchase.

You will generally recognize gain or loss on the sale or retirement of your debt security equal to the difference between the amount you realize on the sale or retirement and your tax basis in your debt security. If your debt security is sold or retired for an amount in foreign currency, the amount you realize will be the U.S. dollar value of such amount on the date the debt security is disposed of or retired, except that in the case of a debt security that is traded on an established securities market, as defined in the applicable Treasury regulations, a cash basis taxpayer, or an accrual basis taxpayer that so elects, will determine the amount realized based on the U.S. dollar value of the foreign currency on the settlement date of the sale.

You will recognize capital gain or loss when you sell or retire your debt security, except to the extent:

described above under Original Issue Discount Short-Term Debt Securities or Debt Securities Purchased with Market Discount,

attributable to accrued but unpaid interest,

the rules governing contingent payment obligations apply, or

attributable to changes in exchange rates as described below.

Capital gain of a noncorporate United States holder is generally taxed at preferential rates where the property is held for more than one year.

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You must treat any portion of the gain or loss that you recognize on the sale or retirement of a debt security as United States source ordinary income or loss to the extent attributable to changes in exchange rates. However, you take exchange gain or loss into account only to the extent of the total gain or loss you realize on the transaction.

Exchange of Amounts in Other Than U.S. Dollars

If you receive foreign currency as interest on your debt security or on the sale or retirement of your debt security, your tax basis in the foreign currency will equal its U.S. dollar value when the interest is received or at the time of the sale or retirement. If you purchase foreign currency, you generally will have a tax basis equal to the U.S. dollar value of the foreign currency on the date of your purchase. If you sell or dispose of a foreign currency, including if you use it to purchase debt securities or exchange it for U.S. dollars, any gain or loss recognized generally will be ordinary income or loss.

Indexed Debt Securities, Exchangeable Debt Securities and Contingent Payment Debt Securities

An applicable prospectus supplement will discuss any special United States federal income tax rules with respect to debt securities the payments on which are determined by reference to any index, debt securities that are exchangeable at our option or the option of the holder into debt securities of an issuer other than the Bank or into other property and debt securities that are subject to the rules governing contingent payment obligations which are not subject to the rules governing variable rate debt securities.

Treasury Regulations Requiring Disclosure of Reportable Transactions

Treasury regulations require United States taxpayers to report certain transactions that give rise to a loss in excess of certain thresholds (a *Reportable Transaction*). Under these regulations, if the debt securities are denominated in a foreign currency, a United States holder that recognizes a loss with respect to the debt securities that is characterized as an ordinary loss due to changes in currency exchange rates (under any of the rules discussed above) would be required to report the loss on Internal Revenue Service Form 8886 (Reportable Transaction Statement) if the loss exceeds the thresholds set forth in the regulations. For individuals and trusts, this loss threshold is \$50,000 in any single taxable year. For other types of taxpayers and other types of losses, the thresholds are higher. You should consult with your tax advisor regarding any tax filing and reporting obligations that may apply in connection with acquiring, owning and disposing of debt securities.

Other Considerations

Information with Respect to Foreign Financial Assets

Individuals that own specified foreign financial assets with an aggregate value in excess of \$50,000 will generally be required to file an information report with respect to such assets with their tax returns. Specified foreign financial assets include any financial accounts maintained by foreign financial institutions, as well as any of the following, but only if they are not held in accounts maintained by financial institutions: (i) stock or securities issued by non-United States persons, (ii) financial instruments and contracts held for investment that have non-United States issuers or counterparties, and (iii) interests in foreign entities. The securities may be subject to these rules. United States holders that are individuals are urged to consult their tax advisors regarding the application of this legislation to their ownership of the securities.

Backup Withholding and Information Reporting

If you are a noncorporate United States holder, information reporting requirements, on Internal Revenue Service Form 1099, generally will apply to:

dividend payments or payments of principal and interest on a security or other taxable distributions made to you within the United States, including payments made by wire transfer from outside the United States to an account you maintain in the United States, and

the payment of the proceeds from the sale of a security effected at a United States office of a broker.

Additionally, backup withholding will apply to such payments if you are a noncorporate United States holder that:

fails to provide an accurate taxpayer identification number,

is notified by the Internal Revenue Service that you have failed to report all interest and dividends required to be shown on your federal income tax returns, or

in certain circumstances, fails to comply with applicable certification requirements.

Payment of the proceeds from the sale of a security effected at a foreign office of a broker generally will not be subject to information reporting or backup withholding. However, a sale of a security that is effected at a foreign office of a broker will generally be subject to information reporting and backup withholding if:

the proceeds are transferred to an account maintained by you in the United States,

the payment of proceeds or the confirmation of the sale is mailed to you at a United States address, or

the sale has some other specified connection with the United States as provided in U.S. Treasury regulations.

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In addition, a sale of a security effected at a foreign office of a broker will generally be subject to information reporting if the broker is:

a United States person,

a controlled foreign corporation for United States tax purposes,

a foreign person 50% or more of whose gross income is effectively connected with the conduct of a United States trade or business for a specified three-year period, or

a foreign partnership, if at any time during its tax year:

one or more of its partners are U.S. persons, as defined in U.S. Treasury regulations, who in the aggregate hold more than 50% of the income or capital interest in the partnership, or

such foreign partnership is engaged in the conduct of a United States trade or business.

Backup withholding will apply if the sale is subject to information reporting and the broker has actual knowledge that you are a United States person.

You generally may obtain a refund of any amounts withheld under the backup withholding rules that exceed your income tax liability by filing a refund claim with the United States Internal Revenue Service.

Foreign Accounts Tax Compliance Act Withholding

Pursuant to Sections 1471 through 1474 of the Code or similar law implementing an intergovernmental approach thereto (FATCA), the Bank and other financial institutions through which payments on the securities are made may be required to withhold U.S. tax at a rate of 30% on all, or a portion of, payments made after December 31, 2016, in respect of (i) any securities treated as debt for U.S. federal tax purposes that are issued or materially modified more than six months after the relevant regulations are finalized and (ii) any securities treated as equity or that do not have a fixed term for U.S. federal tax purposes, whenever issued if (a) the Bank is a foreign financial institution (FFI) (as defined in FATCA) that, in order to avoid withholding on payments to it, enters into and complies with an agreement with the Internal Revenue Service to provide certain information about its account holders (so that the Issuer would be a Participating FFI) and (b)(x) any FFI to or through which payment on such securities is made is not a Participating FFI or otherwise exempt from FATCA withholding or (y) a holder does not provide information sufficient for the Bank to determine whether the holder is a U.S. person or should otherwise be treated as holding a United States account of the Bank.

The application of FATCA to interest, principal or other amounts paid with respect to your securities is not clear. If an amount in respect of U.S. withholding tax were to be deducted or withheld from interest, principal or other payments on the securities, neither the Bank nor any paying agent, nor any other person would, pursuant to the conditions of the securities, be required to pay additional amounts as a result of the deduction or withholding of such tax. As a result, you may, if FATCA is implemented as currently proposed by the Internal Revenue Service, receive less interest or principal than expected.

FATCA is particularly complex and its application is uncertain at this time. The above description is based in part on proposed regulations and official guidance that is subject to change. You should consult your own tax advisor for more information.

10,198

—

July 30, 2013

2,187,344

—

22,344

2,165,000

September 19, 2013

30,000

—

—

30,000

October 28, 2013

40,000

—

—

40,000

November 18, 2013

15,000

—

—

15,000

March 14, 2014

—

554,000

—

554,000

March 26, 2014

—

35,000

—

35,000

Total

2,366,700

589,000

111,700

2,844,000

During the three months ended March 31, 2014, the related restrictions lapsed on restricted common stock awards of 1,000 shares.

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Note 4 — Net Loss per Common Share

Basic net loss per common share is computed by dividing net loss by the weighted-average number of common shares outstanding during the period including a warrant for shares issuable for little or no cash consideration which is considered a common share equivalent. Diluted net loss per common share is computed by dividing net loss by the weighted-average number of common shares outstanding during the period, including the potential dilution that could occur if all of the Company's outstanding stock awards that are in-the-money were exercised, using the treasury stock method.

A reconciliation of the weighted-average number of common shares and equivalents outstanding used in the calculation of basic and diluted net loss per common share is shown in the table below for the periods indicated:

| (in thousands) | Three Months Ended March 31, | |
|---------------------------|---------------------------------|--------|
| | 2014 | 2013 |
| Basic | 45,685 | 47,397 |
| Dilutive effect of awards | — | — |
| Diluted | 45,685 | 47,397 |
| Antidilutive securities: | | |
| Options | 2,844 | 3,160 |
| Warrants | — | 282 |
| Restricted stock | 1 | 3 |

During the first quarter of 2014, the Company repurchased 167,961 shares of its outstanding common stock for \$0.3 million. After these transactions, the Company has \$0.3 million remaining under its previously disclosed share repurchase authorization.

Note 5 — Fair Value Measurements

Fair value is defined as the price that would be received to sell an asset, or paid to transfer a liability (exit price), in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques are based on observable or unobservable inputs. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. These two types of inputs have created the following fair value hierarchy:

- Level 1 — Quoted prices for identical instruments in active markets.
 - Level 2 — Quoted prices for similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; and model-derived valuations in which significant value drivers are observable.
 - Level 3 — Valuations derived from valuation techniques in which significant value drivers are unobservable.
- Applicable guidance requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value.

As of March 31, 2014, financial instruments include \$41.2 million of cash and cash equivalents, restricted assets of \$6.5 million, collateral investments of \$4.1 million, and \$172.5 million of senior secured notes. As of December 31, 2013, financial instruments include \$68.0 million of cash and cash equivalents, restricted assets of \$6.8 million, collateral investments of \$2.0 million, and \$174.5 million of senior secured notes. The fair market values of cash equivalents and restricted assets are equal to their carrying value, as these investments are recorded based on quoted market prices and/or other market data for the same or comparable instruments and transactions as of the end of the reporting period.

As of March 31, 2014, the fair value of the senior secured notes was \$175.4 million based on quoted market prices in active markets for these debt instruments when traded as assets.

Assets and liabilities measured at fair value on a recurring basis are as follows:

| (in thousands) | Fair Value at Reporting Date Using Quoted Prices | | | |
|--------------------------------|--------------------------------------------------|----------------------------|-----------------------------|-------------------------------|
| | in Active Markets Significant for | | | |
| Description | As of | Identical Assets (Level 1) | Other | Significant |
| | | | Observable Inputs (Level 2) | Unobservable Inputs (Level 3) |
| | March 31, 2014 | | | |
| Restricted Assets: | | | | |
| Money Market | \$6,509 | \$6,509 | \$ — | \$ — |
| Collateral Investments: | | | | |
| Money Market | 904 | 904 | — | — |
| Certificate of Deposit | 3,199 | 3,199 | — | — |

| (in thousands) | Fair Value at Reporting Date Using Quoted Prices | | | |
|--------------------------------|--------------------------------------------------|----------------------------|-----------------------------|-------------------------------|
| | in Active Markets Significant for | | | |
| Description | As of | Identical Assets (Level 1) | Other | Significant |
| | | | Observable Inputs (Level 2) | Unobservable Inputs (Level 3) |
| | December 31, 2013 | | | |
| Restricted Assets: | | | | |
| Money Market | \$ 6,835 | \$6,835 | \$ — | \$ — |
| Collateral Investments: | | | | |
| Money Market | 903 | 903 | — | — |

| | | | | |
|------------------------|-------|-------|---|---|
| Certificate of Deposit | 1,068 | 1,068 | — | — |
|------------------------|-------|-------|---|---|

| | Total Gains (Losses) for the |
|-------------------------|---------------------------------------|
| | Three Months Ended March |
| (in thousands) | 31, 2014 |
| Description | 2013 |
| Restricted Assets: | |
| Money Market | \$— \$— |
| Collateral Investments: | |
| Money Market | — — |
| Certificate of Deposit | — — |
| Warrant | — 22 |
| Assets held for sale: | |
| Recovered Properties | — — |
| CVRs | — (55) |

The warrant was valued using the Black-Scholes pricing model. Due to the low exercise price of the warrant, the model assumptions do not significantly impact the valuation.

Contingent Value Rights

As part of the 2009 merger with Voyager Learning Company (“VLCY”), each former VLCY shareholder received a CVR to receive cash in an amount equal to the aggregate amount of specified tax refunds received after the closing of the mergers and various other amounts deposited in escrow on or after the closing date, reduced by any payments to be made under the escrow agreement entered into in connection with the mergers, with respect to agreed contingencies, a potential working capital adjustment and allowed expenses, divided by the total number of shares of VLCY common stock outstanding immediately prior to the effective time of the mergers.

The CVR payment dates were in September 2010, June 2011, and June 2013, with \$1.1 million, \$2.0 million, and \$7.7 million, respectively, distributed to the escrow agent at those times for distribution to holders of the CVRs. The final payment comprised \$5.8 million related to a Michigan state tax matter and \$1.9 million related to a potential tax indemnity obligation. Restricted cash in an escrow account for the benefit of the CVRs was \$3.0 million for the potential tax indemnity obligation. As the potential tax indemnity obligation was not triggered, the remaining \$1.1 million in the escrow account reverted back to the general cash of the Company in the second quarter of 2013.

Assets and liabilities measured at fair value on a non-recurring basis are listed below at their carrying values as of each reporting date:

| (in thousands) | Value at Reporting Date Using | | | |
|-----------------------------------------------------|-------------------------------|------------------|--------------|-----------|
| | Quoted Prices | | | |
| | in Active | | | |
| | Markets Significant for | | | |
| | Other | Significant | | |
| | Identical | Observable | Unobservable | |
| | As of | Assets | Inputs | |
| Description | March 31, 2014 | Inputs (Level 1) | (Level 2) | (Level 3) |
| Goodwill | \$47,842 | \$— | — | \$ 47,842 |
| Property, equipment and software | 20,196 | — | — | 20,196 |
| Pre-publication costs, net | 14,115 | — | — | 14,115 |
| Acquired curriculum and technology intangibles, net | 7,811 | — | — | 7,811 |
| Acquired publishing rights, net | 4,219 | — | — | 4,219 |
| Other intangible assets, net | 5,870 | — | — | 5,870 |

| (in thousands) | Value at Reporting Date Using | | | |
|----------------|-------------------------------|------------------|-----------|-----------|
| Description | Quoted Prices | | | |
| | in Active | | | |
| | Markets Significant for | | | |
| | Other | Significant | | |
| | Observable | Unobservable | | |
| | As of | Assets | Inputs | |
| Description | December 31, 2013 | Inputs (Level 1) | (Level 2) | (Level 3) |

| | | Identical | | |
|-----------------------------------------------------|-----------|-----------|---|-----------|
| | | Assets | | |
| | | (Level 1) | | |
| Goodwill | \$ 47,842 | \$— | — | \$ 47,842 |
| Property, equipment and software | 20,315 | — | — | 20,315 |
| Pre-publication costs, net | 13,401 | — | — | 13,401 |
| Acquired curriculum and technology intangibles, net | 8,719 | — | — | 8,719 |
| Acquired publishing rights, net | 4,705 | — | — | 4,705 |
| Other intangible assets, net | 6,251 | — | — | 6,251 |

| (in thousands) | Description | Total Gains (Losses) for the Three Months Ended March 31, | |
|----------------|-----------------------------------------------------|-----------------------------------------------------------|------|
| | | 2014 | 2013 |
| | Goodwill | \$ — | \$ — |
| | Property, equipment and software | — | — |
| | Pre-publication costs, net | — | — |
| | Acquired curriculum and technology intangibles, net | — | — |
| | Acquired publishing rights, net | — | — |
| | Other intangible assets, net | — | — |

Note 6 — Other Current Assets

Other current assets at March 31, 2014 and December 31, 2013 consisted of the following:

| | As of | |
|----------------------|----------------|-----------------|
| | March | December |
| | 31, | 31, |
| (in thousands) | 2014 | 2013 |
| Deferred costs | \$4,081 | \$ 4,968 |
| Prepaid expenses | 2,387 | 1,369 |
| Deferred taxes | 536 | 536 |
| Other current assets | 171 | — |
| Total | \$7,175 | \$ 6,873 |

Note 7 — Other Assets

Other assets at March 31, 2014 and December 31, 2013 consisted of the following:

| | As of | |
|--------------------------|-----------------|-----------------|
| | March | December |
| | 31, | 31, |
| (in thousands) | 2014 | 2013 |
| Collateral investments | \$4,103 | \$ 1,971 |
| Deferred financing costs | 3,929 | 4,541 |
| Other | 2,094 | 1,776 |
| Total | \$10,126 | \$ 8,288 |

The deferred financing costs represent costs incurred in connection with the issuance of the 9.75% senior secured notes as described in Note 13 to the Condensed Consolidated Financial Statements.

During the first quarter of 2014, the Company purchased an additional \$2.1 million certificate of deposit to serve as collateral for the outstanding letters of credit. The letters of credit had previously been collateralized by the ABL Facility that was terminated on March 26, 2014 as described in Note 13 to the Condensed Consolidated Financial Statements.

Note 8 — Accrued Expenses

Accrued expenses at March 31, 2014 and December 31, 2013 consisted of the following:

| | As of March 31, | December 31, |
|----------------------------------------------|-----------------------|------------------|
| (in thousands) | 2014 | 2013 |
| Salaries, bonuses and benefits | \$5,576 | \$ 9,687 |
| Accrued interest | 2,108 | 6,471 |
| Pension and post-retirement medical benefits | 1,172 | 1,214 |
| Accrued royalties | 976 | 1,649 |
| Headsprout acquisition accrual | — | 3,600 |
| Other | 2,487 | 2,658 |
| Total | \$12,319 | \$ 25,279 |

Accrued interest primarily relates to the 9.75% senior secured notes. The notes require semi-annual interest payments in arrears on each February 15 and August 15 over the life of the notes.

In December 2013, LAZEL, Inc., a wholly owned subsidiary of the Company, completed the acquisition of certain assets of Headsprout for \$4.0 million. Of the total purchase price, \$3.6 million was paid in January 2014 and the remaining \$0.4 million will be paid 18 months after the closing date subject to the holdback provisions of the purchase agreement. The remaining accrual of \$0.4 million is included in Other Liabilities as disclosed in Note 9 below.

Note 9 — Other Liabilities

Other liabilities at March 31, 2014 and December 31, 2013 consisted of the following:

| | As of | |
|-----------------------------------------------------------------|----------|-----------|
| | March | December |
| | 31, | 31, |
| (in thousands) | 2014 | 2013 |
| Pension and post-retirement medical benefits, long-term portion | \$10,059 | \$ 10,241 |
| Deferred rent | 1,161 | 1,201 |
| Long-term income tax payable | 914 | 902 |
| Long-term deferred tax liability | 570 | 570 |
| Long-term deferred compensation | 472 | 491 |
| Headsprout acquisition accrual | 400 | 400 |
| Other | 150 | 149 |
| Total | \$13,726 | \$ 13,954 |

Note 10 — Pension Plan

The net pension costs of the Company's defined benefit pension plan were primarily comprised of interest costs and totaled \$0.1 million for the three month periods ended March 31, 2014 and 2013. The net pension costs for the three months ended March 31, 2014 and 2013 also included immaterial accumulated net loss amortization.

Note 11 — Uncertain Tax Positions

The Company recognizes the financial statement impacts of a tax return position when it is more likely than not, based on technical merits, that the position will ultimately be sustained. For tax positions that meet this recognition threshold, the Company applies judgment, taking into account applicable tax laws, experience managing tax audits and relevant GAAP, to determine the amount of tax benefits to recognize in its financial statements. For each position, the difference between the benefit realized on the Company's tax return and the benefit reflected in its financial statements is recorded on the Condensed Consolidated Balance Sheet as an unrecognized tax benefit ("UTB"). The Company updates its UTBs at each financial statement date to reflect the impacts of audit settlements and other resolution of audit issues, expiration of statutes of limitation, developments in tax law and ongoing discussions with tax authorities. The balance of UTBs was \$6.4 million at March 31, 2014 and December 31, 2013.

The Company files income tax returns in the U.S. federal jurisdiction and various state jurisdictions. All U.S. tax years prior to 2008 related to the VLCY acquired entities have been audited by the Internal Revenue Service. Cambium and

its subsidiaries have been examined by the Internal Revenue Service through the end of 2006. The Company has been audited by the various state tax authorities through 2007.

Note 12 — Commitments and Contingencies

The Company is involved in various legal proceedings incidental to its business. Management believes that the outcome of these proceedings will not have a material adverse effect upon the Company's consolidated operations or financial condition and the Company has recognized appropriate liabilities as necessary based on facts and circumstances known to management. The Company expenses legal costs related to legal contingencies as incurred.

From time to time, the Company may enter into firm purchase commitments for printed materials included in inventory which the Company expects to use in the ordinary course of business. These commitments are typically for terms less than one year and require the Company to buy minimum quantities of materials with specific delivery dates at a fixed price over the term. These open purchase commitments totaled \$0.3 million as of March 31, 2014.

The Company has letters of credit outstanding as of March 31, 2014 in the amount of \$2.5 million to support the build-to-suit lease, credit collections, performance bonds for certain contracts and workers' compensation activity. The Company maintains certificates of deposit as collateral for the letters of credit. The Company also maintains a \$0.9 million money market fund investment as collateral for a travel card program. The certificates of deposit and money market fund investment are recorded in Other Assets.

Note 13 — Long-Term Debt

Long-term debt consists of the following at March 31, 2014 and December 31, 2013:

| | March 31, | December 31, |
|---------------------------------------------------------------------------------|--------------|-----------------|
| (in thousands) | 2014 | 2013 |
| 9.75% senior secured notes due February 15, 2017, interest payable semiannually | \$ 173,000 | \$ 175,000 |
| Less: Unamortized discount | (464) | (509) |
| Total long-term debt | \$ 172,536 | \$ 174,491 |

In February 2011, the Company closed an offering of \$175 million aggregate principal amount of 9.75% senior secured notes due 2017 (the “Notes”). Deferred financing costs are capitalized in Other Assets in the Condensed Consolidated Balance Sheets, net of accumulated amortization, and are to be amortized over the term of the related debt using the effective interest method. Unamortized capitalized deferred financing costs at March 31, 2014 and December 31, 2013 were \$3.9 million and \$4.5 million, respectively, related to the Notes and an asset-based revolving credit facility which was terminated in the first quarter of 2014.

Interest on the Notes accrues at a rate of 9.75% per annum from the date of original issuance and is payable semi-annually in arrears on each February 15 and August 15 to the holders of record of the Notes on the immediately preceding February 1 and August 1. No principal repayments are due until the maturity date of the Notes.

The Notes are secured by (i) a first priority lien on substantially all of the Company’s assets including capital stock of the guarantors (which are certain of the Company’s subsidiaries), and (ii) a second-priority lien, prior to the termination of the ABL Facility (as defined and described below), on substantially all of the inventory and accounts receivable and related assets of the ABL Credit Parties, in each case, subject to certain permitted liens. The Notes also contain customary covenants, including limitations on the Company’s ability to incur debt, and events of default as defined by the agreement. The Company may, at its option, redeem the Notes prior to their maturity based on the terms included in the agreement.

During the quarter ended March 31, 2014, the Company repurchased \$2.0 million aggregate principal amount of Notes for approximately \$2.0 million, plus accrued and unpaid interest. A Loss on Extinguishment of Debt of \$0.1 million was recorded in connection with the repurchase primarily related to the write-off of unamortized deferred financing costs. In April 2014, the Company repurchased an additional \$5.0 million aggregate principal amount of Notes for \$5.1 million, plus accrued and unpaid interest.

ABL Facility. In February 2011, the Company’s wholly owned subsidiary, Cambium Learning, Inc. (together with its wholly owned subsidiaries, the “ABL Credit Parties”), entered into a credit facility (the “ABL Facility”) pursuant to a Loan and Security Agreement (the “ABL Loan Agreement”), by and among the ABL Credit Parties, Harris N.A., individually and as Agent (the “Agent”) for any ABL Lender (as hereinafter defined) which is or becomes a party to said ABL Loan Agreement, certain other lenders party thereto (together with Harris N.A. in its capacity as a lender, the “ABL Lenders”), Barclays Bank PLC, individually and as Collateral Agent, and BMO Capital Markets and Barclays Capital, as Joint Lead Arrangers and Joint Book Runners. The ABL Facility consisted of a four-year \$40.0 million revolving credit facility, which included a \$5.0 million subfacility for swing line loans and a \$5.0 million subfacility for letters of credit.

The ABL Facility was, subject to certain exceptions, secured by a first-priority lien on the ABL Credit Parties' inventory and accounts receivable and related assets and a second-priority lien (junior to the lien securing the ABL Credit Parties' obligations with respect to the Notes) on substantially all of the ABL Credit Parties' other assets.

The ABL Credit Parties were required to pay, quarterly in arrears, an unused line fee equal to the product of (x) either 0.375% or 0.50% (depending upon the ABL Credit Parties' fixed charge coverage ratio at the time) and (y) the average daily unused amount of the revolver. The ABL Facility contained a financial covenant that generally required the ABL Credit Parties to maintain, on a consolidated basis, either (i) excess availability of at least the greater of \$8 million and 15% of the revolver commitment or (ii) a fixed charge coverage ratio of 1.1 to 1.0.

During the first quarter of 2014, the Company's excess availability and fixed charge coverage ratios fell below the required thresholds, which put the Company in a Trigger Period as defined under the ABL Facility agreement. On March 26, 2014, the Company terminated the ABL Facility. As the Company did not have any funds outstanding under the facility and does not anticipate any borrowing needs in the near term, the Company does not expect this to have any impact on its liquidity. A Loss on Extinguishment of Debt of \$0.2 million was recorded in connection with the termination related to the write-off of unamortized deferred financing costs.

Note 14 — Segment Reporting

The Company operates in four reportable segments with separate management teams and infrastructures that offer various products and services:

Voyager Sopris Learning:

Voyager Sopris Learning (“VSL”) is committed to partnering with school districts to overcome obstacles that students, teachers, and school leaders face every day. The suite of instructional and service solutions that VSL provides are not only research based, but also evidence based—proven to increase student achievement and educator effectiveness. VSL solutions have been fully tested in the classroom, ensuring that they are easy to implement and teacher friendly. They are innovative, both in overall instructional approach and in the strategic use of technology in blended and 100% online solutions, and they are supported by an unparalleled commitment to build local capacity for sustained success. With a comprehensive suite of instructional resources, VSL provides assessments, professional development and school-improvement services, literacy and math instructional tools—both comprehensive intervention and supplemental—and resources to build a positive school climate. VSL’s products include the work of world-renowned researchers and education leaders.

Learning A-Z:

Learning A-Z is a preK-6 educational resource company specializing in online delivery of leveled readers and other supplementary curriculum. Founded in 2002 to help teachers differentiate instruction and meet the unique needs of all students, Learning A-Z’s resources are currently used in over two thirds of the elementary schools in the United States and in 177 countries worldwide. In addition to general classroom use, Learning A-Z serves a wide range of student need, including English Language Learners, Response to Intervention, Special Education, and more. Learning A-Z’s value proposition focuses on three key things:

- Saving teachers time, giving them all the resources they need, all online, all accessible at the click of a mouse
- Saving teachers money, delivering thousands of resources for a fraction of the cost of print and other online providers
- Supporting student achievement through differentiated instruction, ensuring the right high-quality resources for every PreK-6 student

Winner of more than 15 industry awards in 2013 alone, Learning A-Z’s subscription-based websites provide online supplemental books, lessons, assessments, and other instructional resources for individual classrooms, schools, and districts. These solutions include: Reading A-Z, Raz-Kids, Science A-Z, Writing A-Z, Vocabulary A-Z, Headsprout Early Reading and Headsprout Comprehension.

ExploreLearning:

ExploreLearning develops online solutions to improve student learning in math and science. ExploreLearning currently has two products: Gizmos, the world’s largest library of interactive, online simulations for math and science in grades 3-12; and Reflex, a powerful solution available for math fact fluency development. Gizmos and Reflex bring research-proven instructional strategies to classrooms around the world.

Kurzweil/IntelliTools:

The Kurzweil/IntelliTools reporting segment includes the Kurzweil Educational Systems and IntelliTools product lines.

Kurzweil Educational Systems is recognized as the leading developer of literacy software for people with learning differences such as dyslexia, attention deficit disorder, and those who are English Language Learners as well as those who are blind or visually impaired. Kurzweil provides complete reading, study skills, writing, and test taking support for students. For over 30 years the company has been driven by the vision to serve the needs of struggling learners to enable them to reach their full potential. We offer products that bring the power and pleasure of reading and learning to the lives of users, striving to enhance learning and expand literacy. Kurzweil Educational Systems is committed to providing research-based solutions that help educators raise the achievement levels of preK–12 students as well as adult learning communities.

IntelliTools offers hardware products that target students with physical, visual and cognitive disabilities that make using a standard keyboard and mouse difficult. IntelliTools also offers software products that target elementary and middle school special education students struggling with reading and math.

On April 17, 2014, the Company completed a sale of the IntelliTools product line.

Other:

This consists of unallocated shared services, such as accounting, legal, human resources and corporate related items. Depreciation and amortization expense, interest income and expense, other income and expense, and income taxes are also included in Other, as the Company and its chief operating decision maker evaluate the performance of operating segments excluding these captions.

The following table represents the revenues, operating expenses, income (loss) from operations, and capital expenditures which are used by the Company's chief operating decision maker to measure the segment's operating performance. The Company does not track assets directly by segment and the chief operating decision maker does not use assets to measure a segment's operating performance, and therefore this information is not presented.

| (in thousands) | Voyager | | | Kurzweil/ | | | Consolidated |
|--------------------------------|-----------|-----------|-----------------|--------------|-------------|--|--------------|
| | Sopris | Learning | | IntelliTools | Other | | |
| Quarter ended March 31, 2014 | Learning | A-Z | ExploreLearning | IntelliTools | Other | | |
| Net revenues | \$ 14,311 | \$ 10,181 | \$ 4,474 | \$ 2,114 | \$ — | | \$ 31,080 |
| Cost of revenues | 7,409 | 422 | 740 | 440 | — | | 9,011 |
| Amortization | — | — | — | — | 4,080 | | 4,080 |
| Total cost of revenues | 7,409 | 422 | 740 | 440 | 4,080 | | 13,091 |
| Other operating expenses | 6,583 | 4,404 | 2,704 | 1,216 | 3,798 | | 18,705 |
| Depreciation and amortization | — | — | — | — | 1,064 | | 1,064 |
| Net interest expense | — | — | — | — | 4,738 | | 4,738 |
| Loss on extinguishment of debt | — | — | — | — | 213 | | 213 |
| Other income, net | — | — | — | — | (215) | | (215) |
| Income tax expense | — | — | — | — | 71 | | 71 |
| Segment net income (loss) | \$ 319 | \$ 5,355 | \$ 1,030 | \$ 458 | \$ (13,749) | | \$ (6,587) |
| Capital expenditures | \$ 1,480 | \$ 1,444 | \$ 341 | \$ 135 | \$ 586 | | \$ 3,986 |

| (in thousands) | Voyager | | | Kurzweil/ | | | Consolidated |
|------------------------------|-----------|----------|-----------------|--------------|-------|--|--------------|
| | Sopris | Learning | | IntelliTools | Other | | |
| Quarter ended March 31, 2013 | Learning | A-Z | ExploreLearning | IntelliTools | Other | | |
| Net revenues | \$ 17,463 | \$ 7,620 | \$ 3,751 | \$ 2,595 | \$ — | | \$ 31,429 |

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| | | | | | | |
|-------------------------------|----------|----------|----------|--------|-------------|------------|
| Cost of revenues | 10,054 | 253 | 487 | 597 | 12 | 11,403 |
| Amortization | — | — | — | — | 3,707 | 3,707 |
| Total cost of revenues | 10,054 | 253 | 487 | 597 | 3,719 | 15,110 |
| Other operating expenses | 7,836 | 3,077 | 2,137 | 1,130 | 5,576 | 19,756 |
| Depreciation and amortization | — | — | — | — | 1,216 | 1,216 |
| Net interest expense | — | — | — | — | 4,576 | 4,576 |
| Other income, net | — | — | — | — | (219) | (219) |
| Income tax expense | — | — | — | — | 68 | 68 |
| Segment net income (loss) | \$ (427) | \$ 4,290 | \$ 1,127 | \$ 868 | \$ (14,986) | \$ (9,078) |
| Capital expenditures | \$ 1,690 | \$ 1,077 | \$ 322 | \$ 72 | \$ 631 | \$ 3,792 |

The capital expenditures disclosed for each segment represent development expenses, primarily developed curriculum and capitalized software. The capital expenditures disclosed for Other represent general capital expenditures that benefit the entire Company such as back-office systems, computer equipment or office furniture.

Note 15 — Related Parties

As previously disclosed, the Company is party to a consulting fee agreement with VSS entitling VSS to the following fees: (i) a fee equal to 1% of the gross proceeds of any debt or equity financing by the Company, and (ii) a fee equal to 1% of the enterprise value of any entities acquired or disposed of by the Company. During the first quarter of 2014, the Company accrued forty thousand dollars under this agreement as a result of the Headsprout acquisition.

Note 16 — Subsequent Events

On April 17, 2014, the Company completed a sale of the IntelliTools product line for \$0.8 million. Any recognized gain or loss on the transaction is not expected to be significant.

In April 2014, the Company repurchased an additional \$5.0 million aggregate principal amount of Notes for \$5.1 million, plus accrued and unpaid interest.

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations.

This section should be read in conjunction with the audited Consolidated Financial Statements of Cambium Learning Group, Inc. and its subsidiaries (the “Company,” “we,” “us,” or “our”) and the notes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2013.

Cautionary Note Regarding Forward-looking Statements.

This report contains forward-looking statements within the meaning of the federal securities laws that involve risks and uncertainties, and which are based on beliefs, expectations, estimates, projections, forecasts, plans, anticipations, targets, outlooks, initiatives, visions, objectives, strategies, opportunities, drivers and intents of our management. Such statements are made in reliance upon the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact included in this report, including statements regarding our future financial position, economic performance and results of operations, as well as our business strategy, objectives of management for future operations, and the information set forth under “Management’s Discussion and Analysis of Financial Condition and Results of Operations,” are forward-looking statements.

Statements that are not historical facts, including statements about our beliefs and expectations, are forward-looking statements. Forward-looking statements can be identified by, among other things, the use of forward-looking language, such as “believes,” “expects,” “estimates,” “projects,” “forecasts,” “plans,” “anticipates,” “targets,” “outlooks,” “initiates,” “visions,” “objectives,” “strategies,” “opportunities,” “drivers,” “intends,” “scheduled to,” “seeks,” “may,” “will,” or “should,” or other variations of those terms or comparable language, or by discussions of strategy, plans, targets, models or intentions. Forward-looking statements speak only as of the date they are made, and except for our ongoing obligations under the federal securities laws, we undertake no obligation to publicly update any forward-looking statements, whether as a result of new information, future events, or otherwise, or to update the reasons actual results could differ materially from those anticipated in these forward-looking statements. Accordingly, you are cautioned that any such forward-looking statements are not guarantees of future performance and are subject to certain risks, uncertainties and assumptions that are difficult to predict. Although we believe that the expectations reflected in such forward-looking statements are reasonable as of the date made, expectations may prove to have been materially different from the results expressed or implied by such forward-looking statements, as it is impossible for us to anticipate all factors that could affect our actual results. These risks and uncertainties include, but are not limited to, those described in “Risk Factors” in Part II, Item 1A and elsewhere in this report and in our Annual Report on Form 10-K for the year ended December 31, 2013, and those described from time to time in our future reports filed with the SEC. Unless otherwise required by law, we also disclaim any obligation to update our view of any such risks or uncertainties or to announce publicly the results of any revisions to the forward-looking statements made in this report.

Our Company

We are a leading educational solutions and services company that is committed to helping all students reach their full potential by providing evidence-based solutions and expert professional services to empower educators and raise the achievement levels of all students. Our brands include: Voyager Sopris Learning (www.voyagersopris.com), Learning A–Z (www.learninga-z.com), ExploreLearning® (www.explorelearning.com www.reflexmath.com) and Kurzweil Educational Systems® (www.kurzweilededu.com). Together, these business units provide best-in-class intervention and supplemental instructional materials; gold-standard professional development and school-improvement services; breakthrough technology solutions for online learning and professional support; valid and reliable assessments; and proven materials to support a positive and safe school environment.

Our products have continued to receive awards and accolades from industry publications including the Best Educational Software (BESSIE) awards from the ComputED Gazette, the CODiE awards from the Software and Information Industry Association and the Education Software Review Awards (EDDIES) by The ComputED Gazette.

The following products were recently named finalists for the 2014 CODiE awards:

- Learning A-Z – ReadingA-Z.com
- Learning A-Z – Raz-Kids.com
- Learning A-Z – ScienceA-Z.com
- ExploreLearning – Gizmos
- ExploreLearning – Reflex

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Overview

Order volume is an internal metric that is a leading indicator of revenues. For the first three months of 2014, company-wide order volumes declined 7% compared to the same period of 2013, and order volume changes by segment were as follows:

- Voyager Sopris Learning decreased 18%
- Learning A-Z increased 24%
- ExploreLearning decreased 7%
- Kurzweil/IntelliTools decreased 31%

Learning A-Z continued its trend of double-digit growth rates. Offsetting this growth, Voyager Sopris Learning and Kurzweil/IntelliTools continued to show order volume declination as reductions in legacy products are currently outpacing gains from newer online and technology-enabled solutions. The decline in order volume in ExploreLearning was primarily due to timing as a large multi-year order was received in the first quarter of 2013. ExploreLearning order volume growth for the trailing twelve months ended March 31, 2014 compared to the trailing twelve months ended March 31, 2013 was 21%.

School district funding continues to undergo significant change and uncertainty, and most of our public school district customers are largely dependent on federal, state and local funding to purchase our products. Additionally, the digitalization of education content and delivery is driving a substantial shift in the education market. The demand for these products has developed rapidly over the past several years and has led to changes in the way that providers develop, produce, market and distribute products.

The education market is also changing in response to the adoption of the Common Core State Standards by a majority of the states. Common Core State Standards define the knowledge and skills students should have within their K-12 education careers so that they will graduate high school able to succeed in entry-level, credit-bearing academic college courses and in workforce training programs. These standards are the product of a state-led effort to establish a single set of clear educational standards for grades K-12. Most of the states that have adopted the Common Core State Standards also belong to one of two multistate testing consortia that are developing common state assessments in English language arts and mathematics, aligned to the new standards. These assessments, which will be designed to replace existing statewide tests, are expected to be administered beginning in the 2014-15 school year. Schools in these states may need to augment or replace instructional materials to align to the Common Core State Standards and to prepare students for the new state assessments.

Overall, GAAP net revenues for the first three months of 2014 decreased by 1.1% to \$31.1 million compared with \$31.4 million in the first three months of 2013. GAAP net revenues by segment for the first three months of 2014, and the percentage change from the first three months of 2013, were as follows:

- Voyager Sopris Learning: \$14.3 million, decreased 18%
- Learning A-Z: \$10.2 million, increased 34%
- ExploreLearning: \$4.5 million, increased 19%
- Kurzweil/IntelliTools: \$2.1 million, decreased 19%

To facilitate expected growth in our Learning A-Z and ExploreLearning segments, we have made investments in 2013 and continuing into 2014 in our sales force and product development efforts, which are expected to increase costs as a percentage of net revenues for the full year 2014. These cost increases were partially offset by the impact of right-sizing efforts completed by VSL in 2013.

Segment Results of Operations

Our brands comprise four reportable segments with separate management teams and infrastructures that offer various products and services: Voyager Sopris Learning, Learning A-Z, ExploreLearning and Kurzweil/IntelliTools.

Voyager Sopris Learning

Voyager Sopris Learning (“VSL”) is committed to partnering with school districts to overcome obstacles that students, teachers, and school leaders face every day. The suite of instructional and service solutions we provide is not only research based, but also evidence based—proven to increase student achievement and educator effectiveness. Our solutions have been fully tested in the classroom, ensuring that they are easy to implement and teacher friendly. They are innovative, both in overall instructional approach and in the strategic use of technology in blended and 100% online solutions, and they are supported by an unparalleled commitment to

build local capacity for sustained success. With a comprehensive suite of instructional resources, we provide assessments, professional development and school-improvement services, literacy and math instructional tools—both comprehensive intervention and supplemental—and resources to build a positive school climate.

Results of Operations

Order volumes in the VSL segment declined 18% in the three months ended March 31, 2014 from the same period in 2013. School district funding continues to undergo significant change and uncertainty, and the current environment had made growth challenging for VSL. We believe that VSL order volume declines are also attributable to slow execution of the unit's product development strategies as well as some confusion in the marketplace due to the debates around the movement to Common Core State Standards.

GAAP net revenues for Voyager Sopris Learning were down \$3.2 million, or 18.0%, for the three months ended March 31, 2014 from the same period in 2013 as a result of the order volume declines. VSL costs benefitted from right-sizing efforts completed in 2013.

We expect sales of purely print-based products to continue to decline. Therefore, to stabilize order volumes and enable growth in future years, the Company will focus its development efforts on technology solutions, especially those opportunities that help school districts implement the new Common Core State Standards or other State-based curriculum or assessment standards. We believe that the efficacy of our products and the transition of our existing content to technology-based learning solutions will eventually offset the weakness in our legacy print-based offerings and return the segment to growth. However, these products take a significant amount of time to develop and gain customer acceptance. In the Company's Form 10-K for the year ended December 31, 2013, management disclosed an expectation that overall VSL order volumes would continue to decline in 2014, but at a lower percentage than the 12% decline experienced in 2013. The first quarter 2014 order volume declines of 18% were disappointing and do create some risk to the achievement of this expectation. However, the first quarter is seasonally the least important quarter, and greater visibility is expected as we ramp up to the 2014-2015 school year.

Learning A-Z

Learning A-Z is a preK-6 educational resource company specializing in online delivery of leveled readers and other supplementary curriculum. Founded in 2002 to help teachers differentiate instruction and meet the unique needs of all students, Learning A-Z's resources are currently used in over two thirds of the elementary schools in the United States and in 177 countries worldwide. In addition to general classroom use, Learning A-Z serves a wide range of student need, including English Language Learners, Response to Intervention, Special Education, and more. Learning A-Z's value proposition focuses on three key things:

- Saving teachers time, giving them all the resources they need, all online, all accessible at the click of a mouse
- Saving teachers money, delivering thousands of resources for a fraction of the cost of print and other online providers
- Supporting student achievement through differentiated instruction, ensuring the right high-quality resources for every PreK-6 student

Winner of more than 15 industry awards in 2013 alone, Learning A-Z's subscription-based websites provide online supplemental books, lessons, assessments, and other instructional resources for individual classrooms, schools, and districts. These solutions include: Reading A-Z, Raz-Kids, Science A-Z, Writing A-Z, Vocabulary A-Z, Headsprout Early Reading and Headsprout Comprehension.

Results of Operations

For the three months ended March 31, 2014, Learning A-Z order volume exceeded the same period in 2013 by 24%. GAAP net revenues for Learning A-Z were higher by \$2.6 million, or 33.6%, for the three months ended March 31, 2014 from the same period in 2013, which was consistent with its order volume trends. Learning A-Z revenues are recognized pro rata over their subscription periods, which are generally for one year but can be for longer periods.

Learning A-Z has realized double-digit order volume growth for several years and we believe this unit will continue to deliver strong growth. We believe that the value proposition offered by the Learning A-Z products will continue to be compelling due to quality content and award-winning technology. To facilitate this expected growth, we are making significant investments in our sales force and product development efforts. Learning A-Z products are aligned with the Common Core State Standards and this will continue to be a focus in future development. Costs as a percentage of net revenues are higher in 2014 than experienced in 2013 as a result of these investments.

ExploreLearning

ExploreLearning develops online solutions to improve student learning in math and science. ExploreLearning currently has two products: Gizmos, the world's largest library of interactive, online simulations for math and science in grades 3-12; and Reflex, a powerful solution available for math fact fluency development. Gizmos and Reflex bring research-proven instructional strategies to classrooms around the world.

Results of Operations

Order volumes in the ExploreLearning segment declined 7% in the three months ended March 31, 2014 from the same period in 2013. The decline in order volume in ExploreLearning was primarily due to timing as a large multi-year order was received in the first quarter of 2013. GAAP net revenues for ExploreLearning were higher by \$0.7 million, or 19.3%, for the three months ended March 31, 2014 from the same period in 2013. Although order volumes declined relative to the first quarter of 2013, revenues increased due to the recognition of prior period sales which are recorded pro rata over their subscription periods, which are generally for one year but can be for longer periods.

We believe that the value proposition offered by the ExploreLearning products will continue to be compelling due to quality content and award-winning technology and we expect strong growth in the coming years. ExploreLearning's 2013 order volumes included several large multi-year deals. Therefore, we believe that order volume growth from 2013 to 2014, while still strong, will be a lower percentage growth than the 27% growth experienced from 2012 to 2013. To ensure that ExploreLearning is well positioned for expected future growth, we are making significant investments in 2014 in this segment for the enhancement of existing products, the development of new products, and the expansion of the sales force. Costs as a percentage of net revenues were higher in the first quarter of 2014 compared to the same period in 2013 as a result of these investments.

Kurzweil/IntelliTools

Kurzweil Educational Systems is recognized as the leading developer of literacy software for people with learning differences such as dyslexia, attention deficit disorder, and those who are English Language Learners as well as those who are blind or visually impaired. Kurzweil provides complete reading, study skills, writing, and test taking support for students. For over 30 years the Company has been driven by the vision to serve the needs of struggling learners to enable them to reach their full potential. We offer products that bring the power and pleasure of reading and learning to the lives of users, striving to enhance learning and expand literacy. Kurzweil Educational Systems is committed to providing research-based solutions that help educators raise the achievement levels of preK-12 students as well as adult learning communities.

In March 2014, Alex Saltonstall, President of Kurzweil/IntelliTools, resigned from the Company. John Campbell, Chief Executive Officer of the Company, is currently performing management oversight for this segment.

In April 2014, the Company completed the sale of its IntelliTools product line for \$0.8 million. Net revenues associated with the IntelliTools product line for the year ended December 31, 2013 were \$1.0 million.

Results of Operations

Order volumes in the Kurzweil/IntelliTools segment declined 31% in the three months ended March 31, 2014 from the same period in 2013. Declines are attributable to the segment's transition to a subscription model rather than its historical perpetual model. Additionally, management believes that customers are increasingly meeting their special education and text-to-speech needs with free and low-priced, but less comprehensive, solutions. GAAP net revenues for Kurzweil/IntelliTools declined by \$0.5 million, or 18.5%, for the three months ended March 31, 2014 from the

same period in 2013. The decline in net revenues was less significant than the decline in order volume as we recognized revenues for prior period service and technology sales that were delivered in the first quarter of 2014.

Going forward, the Company plans to continue to invest in improving the firefly offering which brings many of the capabilities of the Kurzweil 3000 product to the web. This subscription solution has shown strong year over year growth and high renewal rates and will continue to be the focus of the business unit. We believe that the strength of the firefly solution and potentially the development of other subscription-based products will eventually return the segment to growth, but we expect Kurzweil/IntelliTools order volumes to continue to decline in 2014. In the Company's Form 10-K for the year ended December 31, 2013, management disclosed an expectation that Kurzweil/IntelliTools order volumes would continue to decline in 2014, but at a lower percentage than the 13% decline experienced in 2013. The first quarter 2014 order volume declines of 31% and the sale of the IntelliTools product line could make achievement of this expectation difficult, but future quarters will provide greater visibility. In addition to expected

order volume declines, the transition to subscription-based products where revenues are recognized pro rata over the subscription life will likely result in a decline in GAAP net revenues greater than the decline in order volumes. We expect any decline in order volumes or GAAP net revenues to reduce segment earnings.

Shared Services and Other

Shared services and other include accounting, legal, human resources and corporate related items, as well as depreciation and amortization expense, interest income and expense, other income and expense, and income taxes. The Company does not allocate any of these costs to its segments, and our chief operating decision maker evaluates the performance of operating segments excluding these items.

First Quarter of Fiscal 2014 Compared to the First Quarter of Fiscal 2013

| (in thousands) | Three Months Ended | | | | Year Over Year Change | | Favorable/(Unfavorable) | | |
|---------------------------------------------------------------|--------------------|---------------|----------------|---------------|-----------------------|-----------|-------------------------|---|--|
| | March 31, 2014 | | March 31, 2013 | | \$ | % | | % | |
| | Amount | % of Revenues | Amount | % of Revenues | | | | | |
| Net revenues: | | | | | | | | | |
| Voyager Sopris Learning | \$14,311 | 46.0 % | \$17,463 | 55.6 % | \$ (3,152) | (18.0)% | | | |
| Learning A-Z | 10,181 | 32.8 % | 7,620 | 24.2 % | 2,561 | 33.6 % | | | |
| ExploreLearning | 4,474 | 14.4 % | 3,751 | 11.9 % | 723 | 19.3 % | | | |
| Kurzweil/IntelliTools | 2,114 | 6.8 % | 2,595 | 8.3 % | (481) | (18.5)% | | | |
| Total net revenues | 31,080 | 100.0 % | 31,429 | 100.0 % | (349) | (1.1)% | | | |
| Cost of revenues: | | | | | | | | | |
| Voyager Sopris Learning | 7,409 | 23.8 % | 10,054 | 32.0 % | 2,645 | 26.3 % | | | |
| Learning A-Z | 422 | 1.4 % | 253 | 0.8 % | (169) | (66.8)% | | | |
| ExploreLearning | 740 | 2.4 % | 487 | 1.5 % | (253) | (52.0)% | | | |
| Kurzweil/IntelliTools | 440 | 1.4 % | 597 | 1.9 % | 157 | 26.3 % | | | |
| Shared Services | — | 0.0 % | 12 | 0.0 % | 12 | 100.0 % | | | |
| Amortization expense | 4,080 | 13.1 % | 3,707 | 11.8 % | (373) | (10.1)% | | | |
| Total cost of revenues | 13,091 | 42.1 % | 15,110 | 48.1 % | 2,019 | 13.4 % | | | |
| Research and development expense | 2,747 | 8.8 % | 2,331 | 7.4 % | (416) | (17.8)% | | | |
| Sales and marketing expense | 10,582 | 34.0 % | 10,333 | 32.9 % | (249) | (2.4)% | | | |
| General and administrative expense | 5,180 | 16.7 % | 6,793 | 21.6 % | 1,613 | 23.7 % | | | |
| Shipping and handling costs | 196 | 0.6 % | 299 | 1.0 % | 103 | 34.4 % | | | |
| Depreciation and amortization expense | 1,064 | 3.4 % | 1,216 | 3.9 % | 152 | 12.5 % | | | |
| Loss before interest, other income (expense) and income taxes | (1,780) | (5.7)% | (4,653) | (14.8)% | 2,873 | 61.7 % | | | |
| Net interest expense | (4,738) | (15.2)% | (4,576) | (14.6)% | (162) | (3.5)% | | | |
| Loss on extinguishment of debt | (213) | (0.7)% | - | 0.0 % | (213) | (100.0)% | | | |
| Other income (expense), net | 215 | 0.7 % | 219 | 0.7 % | (4) | (1.8)% | | | |
| Income tax expense | (71) | (0.2)% | (68) | (0.2)% | (3) | (4.4)% | | | |
| Net loss | \$(6,587) | (21.2)% | \$(9,078) | (28.9)% | \$ 2,491 | 27.4 % | | | |

Net Revenues.

Our total net revenues decreased \$0.3 million, or 1.1%, to \$31.1 million in the first quarter of 2014 compared to the same period in 2013. Although our overall order volume decreased 7% from the first quarter of 2013, the decline in net revenues was less significant as we recognized revenues for prior period service and technology sales that were delivered in the first quarter of 2014.

Cost of Revenues.

Cost of revenues includes expenses to print, purchase, handle and warehouse our products, as well as order processing and royalty costs, and to provide services and support to customers. Cost of revenues, excluding amortization, decreased \$2.4 million, or 21.0%, to \$9.0 million in the first quarter of 2014 compared to the same period in 2013. This decline was primarily due to lower order volumes in our Voyager Sopris Learning segment.

Amortization Expense.

Amortization expense included in cost of revenues includes amortization for acquired pre-publication costs and technology, acquired publishing rights, and developed pre-publication and technology. Amortization for the first quarter of 2014 increased \$0.4 million compared to the first quarter of 2013, or 10.1%, primarily due to continued investments in developed pre-publication and technology which increased the amount of assets being amortized. This increase was partially offset by a reduction in acquired intangible asset amortization as a majority of these assets are amortized using accelerated methodologies.

Research and Development Expense.

Research and development expenditures include costs to research, evaluate and develop educational products, net of capitalization. Research and development expense for the first quarter of 2014 increased \$0.4 million, or 17.8%, to \$2.7 million compared to the first quarter of 2013 as we continue to invest in our product offerings.

Sales and Marketing Expense.

Sales and marketing expenditures include all costs to maintain our various sales channels, including the salaries and commissions paid to our sales force, and costs related to our advertising and marketing efforts. Sales and marketing expense for the first quarter of 2014 increased \$0.2 million, or 2.4%, compared to the first quarter of 2013 primarily due to increased investments in the Learning A-Z and ExploreLearning sales forces. These investments were slightly offset by cost savings in the Voyager Sopris Learning segment.

General and Administrative Expense.

General and administrative expenses for the first quarter of 2014 decreased \$1.6 million, or 23.7%, from the first quarter of 2013 to \$5.2 million. This decline was primarily due to the severance charges recorded in the first quarter of 2013 of \$1.5 million.

Shipping and Handling Costs.

Shipping and handling costs recognized in the first quarter of 2014 decreased \$0.1 million, or 34.4%, from the first quarter of 2013 to \$0.2 million primarily due to a reduction in order volume in our Voyager Sopris Learning segment.

Net Interest Expense.

Net interest expense increased by \$0.2 million, or 3.5%, to \$4.7 million in the first quarter of 2014 compared to the same period in 2013 due to a reduction in interest income on state tax receivables.

Loss on Extinguishment of Debt.

The charges incurred in the first quarter of 2014 represent the write-off of deferred financing costs and issuance discounts for the terminated ABL facility and the portion of the senior secured notes that were repurchased during the quarter.

Income Tax Provision.

During the first quarter of 2014 and 2013, we recorded state income tax expense of \$0.1 million. We continue to maintain a valuation allowance against our deferred tax assets, which eliminated the deferred tax benefit generated.

Liquidity and Capital Resources

Because sales seasonality affects operating cash flow, we normally incur a net cash deficit from all of our activities through the early part of the third quarter of the year. We typically fund these seasonal deficits through the drawdown of cash. The cash balance as of March 31, 2014 was \$41.2 million. The primary sources of liquidity are our current cash balances and our annual cash flow from operations and the primary liquidity requirements relate to interest on our long-term debt, pre-publication costs, capital investments and working capital. We believe that based on current and anticipated levels of operating performance and cash flow from operations, we will be able to make required interest payments on our debt and fund our working capital and capital expenditure requirements for the next 12 months.

Long-term debt

During the quarter ended March 31, 2014, we repurchased \$2.0 million aggregate principal amount of our 9.75% senior secured notes (“Notes”) for approximately \$2.0 million, plus accrued and unpaid interest. A Loss on Extinguishment of Debt of \$0.1 million was recorded in connection with the repurchase primarily related to the write-off of unamortized deferred financing costs. In April 2014, we repurchased an additional \$5.0 million aggregate principal amount of Notes for \$5.1 million, plus accrued and unpaid interest.

On March 26, 2014, we terminated our four-year \$40.0 million revolving credit facility. As we did not have any funds outstanding under the facility and do not anticipate any borrowing needs in the near term, we do not expect this to have any impact on our liquidity. A Loss on Extinguishment of Debt of \$0.2 million was recorded in connection with the termination related to the write-off of unamortized deferred financing costs.

Cash flows

Cash from operations is seasonal, with more cash generated in the second half of the year than in the first half of the year. Cash is historically generated during the second half of the year because the buying cycle of school districts generally starts at the beginning of each new school year in the fall. Cash used in our operating, investing and financing activities is summarized below:

| | For the Three Months Ended March 31, | |
|----------------------|--------------------------------------------|------------|
| (in thousands) | 2014 | 2013 |
| Operating activities | \$(16,649) | \$(16,240) |
| Investing activities | (7,586) | (3,792) |
| Financing activities | (2,519) | (723) |

Operating activities. Cash used in operations was \$16.6 million and \$16.2 million for the three month periods ended March 31, 2014 and 2013, respectively. Cash from operations was impacted by a lower net loss in 2014 versus 2013, the timing of accounts receivable collections, and the movement of \$2.1 million of cash to certificates of deposit to collateralize certain letters of credit after the termination of the ABL facility.

Investing activities. Cash used in investing activities was \$7.6 million in the first three months of 2014 compared to \$3.8 million in the first three months of 2013. The increase in investing cash outflows is primarily due to the payment of a purchase price accrual of \$3.6 million related to the 2013 Headsprout acquisition and an increase in capital expenditures of \$0.2 million.

Financing activities. Cash used in financing activities was \$2.5 million in the first three months of 2014 and \$0.7 million in the first three months of 2013. The increase in financing cash outflows was primarily due to the \$2.0 million repurchase of Notes completed in the first quarter of 2014. The remaining cash flows in each period represent principal payments under capital lease obligations and share repurchases.

Outlook. The following future cash outflows have been made or are expected:

In April 2014, we repurchased an additional \$5.0 million aggregate principal amount of Notes for \$5.1 million plus accrued and unpaid interest.

We have \$0.3 million remaining under the existing share repurchase authorization.

Full year capital expenditures are expected to range between \$18 million and \$20 million.

Non-GAAP Measures

The net loss as reported on a GAAP basis includes material non-operational and non-cash items. We believe that earnings (loss) from operations before interest, income taxes, and depreciation and amortization, or EBITDA, and Adjusted EBITDA, which further excludes non-operational and non-cash items, provide useful information for investors to assess the results of the ongoing business of the Company. In 2014, management began using a new non-GAAP metric, which it refers to as Cash Income, to set and measure progress towards performance targets, which directly affect compensation for employees and executives. Cash Income reduces Adjusted EBITDA for capital expenditures and removes the timing differences for recognition of deferred revenues and related deferred expenses.

EBITDA, Adjusted EBITDA and Cash Income are not prepared in accordance with GAAP and may be different from similarly named, non-GAAP financial measures used by other companies. Non-GAAP financial measures should not be considered a substitute for, or superior to, measures of financial performance prepared in accordance with GAAP. We believe that these non-GAAP measures provide useful information to investors because they reflect the underlying performance of the ongoing operations of the Company and provide investors with a view of the Company's operations from management's perspective. Adjusted EBITDA and Cash Income remove significant purchase accounting, non-operational or certain non-cash items from earnings. We use Adjusted EBITDA and Cash Income to monitor and evaluate the operating performance of the Company and as the basis to set and measure progress towards performance targets, which directly affect compensation for employees and executives. We generally use these non-GAAP measures as measures of operating performance and not as measures of liquidity. Our presentation of EBITDA, Adjusted EBITDA and Cash Income should not be construed as an indication that our future results will be unaffected by unusual, non-operational or non-cash items.

Below are reconciliations between Net Loss and Cash Income (Loss) for the three month periods ended March 31, 2014 and 2013:

Reconciliation Between Net Loss and Cash Income (Loss) for the Three Months Ended March 31, 2014 and 2013

| (\$ in thousands) | Three Months Ended March 31, | |
|-----------------------------------------------------------------------------------------------------------------------|---------------------------------|------------|
| | 2014 | 2013 |
| Net loss | \$(6,587) | \$(9,078) |
| Reconciling items between net loss and EBITDA: | | |
| Depreciation and amortization | 5,144 | 4,923 |
| Net interest expense | 4,738 | 4,576 |
| Income tax expense | 71 | 68 |
| Income (loss) from operations before interest, income taxes, and depreciation and amortization (EBITDA) | 3,366 | 489 |
| Non-operational or non-cash costs included in EBITDA but excluded from Adjusted EBITDA: | | |
| Other income, net | (215) | (219) |
| Loss on extinguishment of debt | 213 | — |

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| | | |
|------------------------------------------------|------------|-----------|
| Merger and acquisition activities (b) | 150 | 158 |
| Stock-based compensation and expense (c) | 112 | 229 |
| Adjustments related to purchase accounting (a) | — | 29 |
| Adjustments to CVR liability (d) | — | 55 |
| Management transition (e) | — | 1,501 |
| Adjusted EBITDA | 3,626 | 2,242 |
| Change in deferred revenues | (10,424) | (7,924) |
| Change in deferred costs | 1,100 | 1,137 |
| Capital expenditures | (3,986) | (3,792) |
| Cash income (loss) | \$(9,684) | \$(8,337) |

Adjusted EBITDA and Cash Income (Loss) by segment were as follows:

| | Three Months Ended | | Three Months Ended | |
|-------------------------|-------------------------|-----------|-------------------------|-----------|
| | March 31, 2014 | | March 31, 2013 | |
| | Adjusted Cash Income | | Adjusted Cash Income | |
| (\$ in thousands) | EBITDA | (Loss) | EBITDA | (Loss) |
| Voyager Sopris Learning | \$351 | \$(4,777) | \$(331) | \$(5,312) |
| Learning A-Z | 5,383 | 1,190 | 4,306 | 1,510 |
| ExploreLearning | 1,042 | (1,878) | 1,144 | (953) |
| Kurzweil/IntelliTools | 461 | (21) | 869 | 796 |
| Shared Services | (3,611) | (4,198) | (3,746) | (4,378) |
| Total | \$3,626 | \$(9,684) | \$2,242 | \$(8,337) |

- (a) Under applicable accounting guidance for business combinations, an acquiring entity is required to recognize all of the assets acquired and liabilities assumed in a transaction at the acquisition date fair value. First quarter 2013 net revenues have been reduced in the historical financial statements due to the write-down of deferred revenue to its estimated fair value as of the merger date. The write-down was determined by estimating the cost to fulfill the related future customer obligations plus a normal profit margin. Partially offsetting this impact, first quarter 2013 cost of revenues were reduced for other purchase accounting adjustments, primarily a write-down of deferred costs to zero at the acquisition date. The adjustment of deferred revenue and deferred costs to fair value is required only at the purchase accounting date; therefore, its impact on net revenues and cost of revenues is non-recurring.
- (b) Costs are related to merger and acquisition activities including due diligence and other non-operational charges such as pension and severance costs for former employees.
- (c) Stock-based compensation and expense is primarily related to our outstanding options and restricted stock awards. The first quarter of 2013 also includes expense related to our outstanding warrants.
- (d) Adjustments to the CVR liability as a result of changes in the likelihood of collecting potential tax receivables and related interest income included in the estimate of the fair value of the CVRs.
- (e) Severance charges recorded in connection with the management transition completed in the first quarter of 2013.
- Off-Balance Sheet Arrangements

The Company has no off-balance sheet arrangements as of March 31, 2014 that have or are reasonably likely to have a current or future material effect on the Company's financial condition, changes in financial conditions, sales or expenses, results of operations, liquidity, capital expenditures or capital resources.

Contractual Obligations

This item is not required for a smaller reporting company.

Critical Accounting Policies

In the ordinary course of business, we make a number of estimates and assumptions relating to the reporting of results of operations and financial position in the preparation of our condensed consolidated financial statements in conformity with GAAP. Actual results could differ significantly from those estimates under different assumptions and conditions. We included in our 2013 Form 10-K a discussion of our critical accounting policies that are particularly important to the portrayal of our financial position and results of operations and that require the use of our

management's most difficult, subjective and complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

We have made no material changes to any of the critical accounting policies discussed in our 2013 Form 10-K through March 31, 2014.

Recently Issued Financial Accounting Standards

In April 2014, new guidance was issued which changes the definition of a discontinued operation to include only those disposals of components of an entity that represent a strategic shift that has (or will have) a major effect on an entity's operations and financial results. This guidance is effective prospectively for reporting periods beginning after December 15, 2014. The Company does not expect the adoption of this standard to have a significant impact on the Company's results of operations or financial position.

Item 3. Quantitative and Qualitative Disclosures About Market Risk.

This item is not required for a smaller reporting company.

Item 4. Controls and Procedures.

Evaluation of Disclosure Controls and Procedures

Management of the Company, with the participation of the Chief Executive Officer and Chief Financial Officer, conducted an evaluation of the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rule 13a-15(e) and Rule 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report. The Company's disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company in the reports it files or submits under the Exchange Act is recorded, processed, summarized and reported on a timely basis and that such information is communicated to management, including the Chief Executive Officer, Chief Financial Officer and its Board of Directors, to allow timely decisions regarding required disclosure.

Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of March 31, 2014.

Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Part II. Other Information

Item 1. Legal Proceedings.

The Company is involved in various legal proceedings incidental to its business. Management believes that the outcome of these proceedings will not have a material adverse effect upon the Company's consolidated operations or financial condition and the Company has recognized appropriate liabilities as necessary based on facts and circumstances known to management.

Item 1A. Risk Factors.

In addition to the other information set forth in this report, you should carefully consider the factors discussed in Part I, "Item 1A. Risk Factors," in the Company's Annual Report on Form 10-K for the year ended December 31, 2013, as such factors could materially affect the Company's business, financial condition, or future results. In the three months ended March 31, 2014, there were no material changes to the risk factors disclosed in the Company's 2013 Annual Report on Form 10-K. The risks described in the Annual Report on Form 10-K are not the only risks the Company faces. Additional risks and uncertainties not currently known to the Company, or that the Company currently deems to be immaterial, also may have a material adverse impact on the Company's business, financial condition, or results of operations.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.

Shares of common stock repurchased by the Company during the quarter ended March 31, 2014 were as follows:

| Period: | Issuer Purchases of Equity Securities | | | (a) Maximum Dollar Value of Shares that May Yet be Purchased Under the Program (\$ in thousands) |
|------------------------|---------------------------------------|------------------------------|----------------------------------------------------------------------------------|--------------------------------------------------------------------------------------------------|
| | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | |
| January 1—January 31 | 115,961 | \$ 1.81 | 115,961 | \$ 414 |
| February 1—February 28 | 52,000 | 1.75 | 52,000 | 323 |
| March 1—March 31 | — | — | — | 323 |

(a)

On May 22, 2012, the Company's Board of Directors authorized the Company to repurchase shares of its common stock up to a maximum of \$5 million through July 5, 2013. On March 19, 2013, the Company's Board of Directors extended the share repurchase authorization for an additional one year period (through July 5, 2014) and the remaining authorization was reset to \$5 million.

Item 6. Exhibits.

The following exhibits are filed as part of this report.

| Exhibit Number | Description |
|----------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 10.1 | Note Repurchase Agreement Between Cambium Learning Group, Inc. and GoldenTree Asset Management dated April 22, 2014 (incorporated by reference to Exhibit 10.1 to Cambium Learning Group, Inc.'s Current Report on Form 8-K dated April 22, 2014 (File No. 001-34575)). |
| 31.1 | Certification of the Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.2 | Certification of the Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.1 | Certification of Chief Executive Officer pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 32.2 | Certification of Chief Financial Officer Pursuant to 18 U.S.C Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 101.ins | XBRL Instance Document. |
| 101.def | XBRL Taxonomy Extension Definition Linkbase Document. |
| 101.sch | XBRL Taxonomy Extension Schema Document. |
| 101.cal | XBRL Taxonomy Extension Calculation Linkbase Document. |
| 101.lab | XBRL Taxonomy Extension Label Linkbase Document. |
| 101.pre | XBRL Taxonomy Extension Presentation Linkbase Document. |

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has caused this report to be signed on its behalf by the undersigned duly authorized officer of the registrant.

CAMBIUM LEARNING GROUP, INC.

Date: May 8, 2014 /s/ Barbara Benson
Barbara Benson,
Chief Financial Officer (Principal Financial Officer)

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