Community Equity Investment Fund

Description

CDLFs, in some instances in the U.S., have evolved an equity subsidiary, but Nova Scotia is the only Canadian site where community funds have been organized to include community equity investment functions. Cape Breton Island was the locale for an independent self-started group that began with raising solely private funds of $500,000 in 1990.

BCA Holdings Ltd., as it is called, was organized as a not-for-profit corporation by a group of local citizens, most of whom had been associated with New Dawn Enterprises, the first CDC in Canada. (For many years, New Dawn had been exploring the possibilities of a local investment fund.) While it holds not-for-profit status as a legal entity, it does, of course, offer a return to investors who supply its capital.

BCA also received substantial support from church-related CED investors. It had been given cause to believe a federal agency loan of $500,000 would be forthcoming after its private capital was raised; but in the end it took long intense negotiations over three years to get the additional capital. BCA contrasts with other community equity investment groups more recently organized in Nova Scotia in that it is not-for-profit, only for community benefit. Moreover, it did not depend upon government participation to get started. And it has never had any government support for its operational costs. BCA manages to operate without any direct dollar subsidies by strict cost controls and by using volunteer efforts for most of its analytic and deal-making activities. Its independence from the need for subsidies is cherished by its organizers.

Other community investment groups have arisen in Nova Scotia in response to provincial legislation, effective in 1998, that offers a tax credit, a partial guarantee, and RRSP/RRIF eligibility status to investments by individuals. Within the provincial program, these are called CED Investment Funds (CEDIFs). They are for-profit entities, empowered only to make equity investments, not to lend (except in a subordinated debt format).

There are two types of CEDIFs under the program: One is in a co-operative format, the other in a corporation format. There is also another Nova Scotia program that offers equity financing (repayable) for social assistance recipients to start their own business, under a specialized arrangement with a sponsoring co-op in their community. (See Co-operative Employment Partnership Program.)

BCA is currently trying to take advantage of the tax credit provisions, which would enhance its capacity to raise capital. For this purpose, it is organizing a for-profit subsidiary for which it has raised about $800,000 in private funds. Nevertheless, because it began without government help, it remains a powerful model for community-minded investors, showing that government participation is not necessary, even if the potential of later government participation will be a strong motivation to raise private financing.

Originally, BCA was stimulated by a history in Cape Breton of businesses that, upon retirement of the owner or because of troubled financial status, were sold to outside investors who often moved the firm off the Island. The BCA organizers believed that such losses in jobs and economic activity could, in some cases at least, be prevented if there was a group that would buy the assets and maintain them on the Island, at least until they could be divested to a resident entrepreneur. (In fact, in a sort of pilot of the model, one of the organizers had earlier been personally motivated to save a long-established firm, and bought it up himself without expecting to make a return so much as to protect a community asset.) So "banking community assets" was the theme that animated the initiation of BCA Holdings and gave it its abbreviated name.

BCA Holdings is now the umbrella for a number of subsidiaries, some for-profit, some not-for-profit, with a total capital base of about $1.3 million (not including the new tax incentive-related capital). It uses both equity and credit instruments. It has invested in the development of: a commercial centre that shored up the historic first credit union in the Atlantic region and gave the credit union necessary and attractive new quarters; a rope factory that is now very successful with a branch on the US West Coast; a hotel; a ski hill; a cement block factory; and a radio station. In each of these it has mobilized outside expertise and partners. It now has most of its capital committed, and so it is exploring the new source of capital from people who would be attracted by the tax credits.

The critical features of the CEIF, in this model, are:

- It is incorporated in a not-for-profit status, which protects it from outside investors and ensures it will always be able to concentrate on local financial opportunities.
- It minimizes operational expenses by depending heavily upon volunteers with financial and business expertise, who generally serve on its board or the board of a subsidiary.
- It stresses partnerships with people or firms that are specialized in the particular field of the investment, rather than specializing itself in one particular field, as do most venture capital firms. In this manner, it can respond to any opportunity and thus deal with threats to any of a variety of local closures or transfers, as well as promote new ventures.

These features are joined, of course, with the usual concern for general management competence, careful financial controls, and so on, as befits any sustainable business or financial institution.

Benefits

The CEIF offers the flexibility of using the equity format, which is more powerful than credit for business development and therefore job creation or job retention. Without a new equity investment, many businesses cannot be helped over a temporary problem, or expanded at a critical juncture, or saved from closure.

Major challenges

Equity investments are by nature much more risky than credit arrangements. So it is much more difficult to raise that sort of capital, especially for a not-for-profit entity. Also, like any other development finance instrument, it poses a central problem in balancing community benefits with sustainability of the capital program itself.

If, as with BCA, the fund takes all business sectors as its scope, it is stretched to find competence and expertise in every different sector it enters. As a community institution it may take on such a broad responsibility, but that certainly is a challenge that no conventional venture capital group would accept.

Some practical steps

How a community might go about establishing a CEIF will depend in part upon its existing resources. With a CDLF or other credit fund already operating, it may well be the best strategy to begin from that base. BCA began independently, but it arose by virtue of helpful collaboration with institutions (like New Dawn and the University College of Cape Breton) which had already been active parts of the local CED scene. A CEIF will, in short, be more likely to arise out of a local CED tradition, relying on leadership from those who have an established reputation for CED accomplishments.

Resource organizations & contacts

BCA itself, and its key organizer, Greg MacLeod, are probably the best sources of orientation to this strategy (tel. 902-539-1777).

Publications

- BCA itself is described by Greg MacLeod in "Breaking the Rules," *Making Waves* (Autumn 1998) 9, 3:.20-22 (tel. 888-255-6779); and in more detail by Harvey Johnstone, "Financing Ventures in a Depleted Community," Chap. 5, in Gertrude MacIntyre, ed., *Perspectives on Communities: A Community Economic Development Roundtable* (Sydney, NS: University College of Cape Breton Press, 1998).

- The second edition of *Guide to Community Economic Development Investment Funds*, under the Nova Scotia Equity Tax Credit program, Nova Scotia Economic Development and Tourism, is available by telephoning: 902-424-1259.