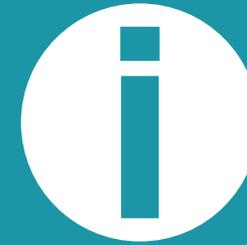


# Financing a Co-op (with or without share capital)



## Introduction

Under the Ontario *Co-operative Corporations Act* (hereafter the Act), co-operatives can incorporate in one of two ways: with share capital and without share capital. Each structure offers options and benefits for raising money or carrying on operations. The co-op's purpose and financing requirements will determine the correct choice.

The decisions around share structure and corporate structure can be complex, and will first require a clear idea of the co-op's purpose and business plan. It is often advantageous for a group to seek the guidance of a co-op developer, lawyer or accountant to help determine an appropriate share structure.

## Determining Financing Needs

Before making the decision about share structure, a group should try and answer the following questions about their business and what their financing needs might be.

1. Will the co-op need to purchase equipment, land or other assets before being able to start operations?
2. Will the co-op have to purchase supplies or maintain inventory on an ongoing basis?
3. Will the co-op need working capital during start-up or in the early project stages?

In many cases, both a share structure and a non-share capital structure may be able to provide the co-op with the necessary funds. Each choice carries benefits and drawbacks that may make different options available as time goes on, or restrict future choices. Banks and financiers may not be comfortable with the non-share capital structure, which can limit the ability of the co-op to raise money.

## Corporate Structure

### Share Capital

A co-operative can raise share capital by offering portions of the co-op (shares) to members or to outside investors in exchange for cash or items of equal value. Co-ops with share capital can offer membership shares and preference shares. Membership shares are available only to those people wishing to become members of the co-operative, and all members must buy one membership share. Preference shares are available for purchase by both members and non-members (outside investors).

Share capital is the sale of equity: an agreed-upon percentage of the co-op. The proceeds thereof can be used to buy equipment, land, buildings, and/or provide working capital that the co-op might need. When members or investors buy preference shares, they receive a return on their investment in the form of dividends – provided the co-operative has earned enough surplus to justify them.

- There are over 1,300 co-operatives, credit unions and caisse populaires incorporated and operating in Ontario, with 1,900 locations in 400 communities.
- In 2012 alone, 73 new co-ops incorporated in Ontario.
- Housing is Ontario's largest co-op sector (45%), followed by Financial Services (17%), Child care (17%) and Agriculture (6%).
- The co-operative sector in Ontario represents a very conservative \$30 billion in assets (2007).

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### Without Share Capital

Incorporating without share capital means that the co-op will have to rely on debt financing, since they cannot offer shares to members or investors to raise money. Co-operatives without share capital can issue securities like debentures and other debt instruments to both members and non-members. They can also use member loans (which may be a membership requirement, if stated in the bylaws), or loans paid out of the patronage that a member is eligible to receive.

This type of co-op structure is suited to covering operating expenses such as supply purchasing, generating working capital or inventory requirements. It is possible to purchase equipment and fixed assets using debt, but it can be more difficult to do so.

### What Does Capital Mean?

Capital is the money used by a co-op to do business – it generally refers to the amount available to the business as assets like cash or property, minus the liabilities that the co-op has. The Act refers to two types of capital: authorized capital and issued capital. Authorized capital is the maximum amount of capital that a co-op can have (expressed as the maximum number of shares that can be sold), while issued capital refers to the shares that have actually been sold, from which payment has been received. The amount of issued capital can never exceed the amount of authorized capital in a co-operative.

### Filing Requirements

Once a co-op has determined which share structure will suit its needs best, then it can incorporate and begin operations.

### Incorporation

When a co-operative files its Articles of Incorporation, it must indicate whether it will operate with or without share capital. In the case of a share capital co-op, the Articles must also indicate the characteristics of each type of share and the total amount of capital being issued as shares. For non-share co-operatives, the member loan amount and required investment must be specified in the Articles of Incorporation.

The Ministry of Government and Consumer Services has templates for the Articles of Incorporation on its website ([ontario.ca](http://ontario.ca)).

There are two different templates available – one specifically for co-ops incorporating with share capital, and the other for co-ops without share capital.

### Offering Securities

In addition to the material contained in the Articles, there are additional procedures and regulations associated with the sale of securities. The sale of shares and other securities (like debentures) is dictated by the *Co-operative Corporations Act*. If a co-op wishes to raise money through the issuance of securities, it must issue an “Offering

Statement” which is similar to a prospectus offered by a business corporation that is offering shares. An Offering Statement is not required if the co-op has less than 35 security holders. If a co-op has more than 35 security holders, it may still be exempt from having to do an offering statement if it meets one of the following conditions:

- Will be raising less than \$200,000 in the offering (and the first \$200,000 of any offering is exempt from requiring a statement)

OR

- Will sell less than \$1,000 of securities from any one member per year, or \$10,000 total in the members’ lifetime (but securities that are distributed as a part of patronage returns do not count towards this limit).

If the co-op will exceed any of the above limits through its offering of securities, then an Offering Statement has to be prepared. This is a document that outlines the securities being offered along with the risks and details of the co-op’s operations and financials. This Offering Statement must then be submitted to the Financial Services Regulatory Authority (FSRA), where it is then reviewed and receipted. Once the receipt has been given, then and only then can the co-op start selling securities.

- Three recent studies demonstrate that co-operative enterprises have significantly higher survival rates than other business corporations. In fact, a co-operative is twice as likely to be in operation after 10 years.
- Ontario co-ops employ and provide benefits to 15,500 people (greater than the total number of Ontarians employed in production of goods).
- 1.4 million Ontarians are members of a co-operative, credit union or caisse populaire (more than 10% of the population).

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An Offering Statement is never valid for more than 12 months and updated Offering Statements must be submitted to FSRA each year to allow the co-op to continue selling securities.

It is possible that circumstances related to the securities being offered will change during the course of the offering. Some of these changes may significantly affect the co-op's financial position or the offering itself. These are referred to as material changes, and have a specific definition in the Act. If the co-op is faced with a material change, then the co-op must inform its investors or potential investors that the offering statement as receipted is no longer accurate. In order to go forward, the co-op must file a Statement of Material Change with FSRA within 30 days of the change occurring.

Templates are available to facilitate the creation of Offering Statements. They can be found on our website: [ontario.coop](http://ontario.coop)

The Offering Statement process can be extremely complex and time-consuming and requires a high level of knowledge of the co-op's financial position and plans. Co-ops are strongly urged to consult the proper legal or financial advice during the Offering Statement process.

### Financing through Other Sources

#### Debt Financing

In addition to the ability to raise money from the membership and community investors, co-ops can also take on debt financing from financial institutions like credit unions or banks in order to finance their projects and operations. This can include obtaining a mortgage or loan to purchase property or equipment, opening a line of credit for the co-op to use, or other types of shorter term loans. The ability of a co-op to obtain financing of this type will depend on several factors, including:

- The available equity or collateral that the co-op can bring to the table;
- The perceived risk of the investment or the business of the co-op on the part of the financial institution; and
- The amount of money required

#### Business Plan

A co-op should have a business plan that outlines the co-op's financial situation or the proposed financials. Business plans can be presented to commercial lenders to help them understand the co-op and properly assess its needs. A business plan should identify:

- revenue or potential revenue deriving from the project or the co-op's operations – usually through the inclusion of financial statements or pro forma financials;
- key personnel involved in the co-op;
- timelines and status of the project;
- risks associated with the project and how the co-op has addressed them; and
- an assessment of the market for the product or service the co-op offers and the co-op's competitive advantage.

The business plan must demonstrate that the co-op has the skills and ability to move forward successfully. It must convince a lender or potential investors that the co-op will manage the project and mitigate or adapt to any risks that might occur.

- There are some **49,000 co-operative volunteers across Ontario, including over 10,000 board members who are actively involved in governing and leading co-ops, credit unions and caisse populaires in Ontario.**
- **World-wide, co-operatives operate in over 90 countries, employ over 100 million people and are supported by over 1 billion members.**

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### Grants

Some co-operatives, usually only those operating with not-for-profit or charitable status, can also access grants from charitable foundations or government agencies like the Ontario Trillium Foundation. There are some granting programs that are open specifically to co-operatives, regardless of their tax-status.

Grants are usually project-based and provide funding for a finite period of time. They usually do not provide ongoing operational funding, but may partially cover staff costs. Grants will generally require an application and approval process and not all applications will be successful.

OCA maintains lists of co-operatives and other organizations providing loans, grants and technical assistance funding.

### Government Subsidies or Support

Some co-operatives are eligible to receive government funding that does support their operations. This can be the case with co-ops that are providing a social service that is subsidized by the government, as in the case of some not-for-profit housing co-ops or some child care co-ops.

### References

- *Comparison Chart of Co-ops, Businesses and NFPs* – Created for the Ontario Co-operative Association by Brian Iler, Iler Campbell LLP and Russ Christianson of Rhythm Communications.
- *How to Talk to Lenders* – Created for the Ontario Sustainable Energy Association by Jens Lohmueller

### FOR MORE INFORMATION, CONTACT

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**More resources are available at:**  
CoopZone Network  
[coopzone.coop](http://coopzone.coop)

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