

Community Investing in Canada



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Community Investing in Canada

Introduction

Community investing is a strategy to address unemployment, environmental degradation, economic restructuring, poverty and social exclusion. It is a way of generating resources and opportunities for people and communities who are underserved by mainstream financial institutions.

This paper strives to describe the community investing sector in Canada. It will;

1. Explain the terminology used in Canada and the link between micro-lending and community investing in Canada
2. Describe the community investing sector in Canada
3. Describe innovations in the Canadian sector

Describing the community investing sector in Canada

Canada, like many countries in the world, has a percentage of its population that is unable to access mainstream financing for their businesses, to purchase homes or to pursue secondary education. These individuals do not meet the conventional financing criteria used by mainstream financial institutions.

Why can't individuals access financing in Canada?

Some reasons for a financing application being turned down in Canada include;

1. No credit history

Financial institutions access credit reports for every individual or enterprise with a loan application. The credit reports only show an individual's credit history in Canada. So immigrants and refugees to Canada are excluded when they do not have a credit history in this country. Another group that sometimes falls into this category is people who have recently divorced. Typically it has been women who do not have the mortgage or loans in their names and so do not have a credit history.

2. Poor credit history

While some people may be irresponsible with their credit, there are others who have been unable to make loan payments due to unemployment, illness, injury or other circumstances. It is the latter group who are usually eligible for community financing programs.

3. No security or collateral to guarantee the loan

Canadians living on low incomes, whether the working poor or individuals living on social assistance or employment insurance, are often unable to access financing because they have limited assets to serve as security or collateral.

4. Incomplete business plan

The borrower may need up front support to develop their business plan and/or refine their financing needs.

5. Lacking a track record

Individuals starting a business are required to provide two years of business statements making it extremely difficult to find financing for a start up business or organization.

In addition to these barriers, mainstream financial institutions will not extend loans or invest when the administrative costs of placing and monitoring loans can not be met by the return on capital. The loan may be perceived as too small or too risky.

It is not only individual Canadians who can be unable to access financing from mainstream financial institutions. There are many organizations that are unable to access financial services. They include for profit and non profit cooperatives, social enterprises, not for profits, community facilities and affordable housing projects. In Canada, these types of organizations are becoming widely known as belonging to the social economy.

Why can't social economy organizations access financing?

When a private sector business approaches a mainstream financial institution for financing, the institution makes a decision to invest or not, based on an evaluation of expected economic return.

Some non profits, coops and other social economy organizations are unable to attract the equity needed to leverage conventional debt instruments. This is because many social economy organizations have social outcomes as their primary goal. Social economy enterprises may have a limited return on investment capital expected (or no return at all). The social economy organization may have a high social value, good management and may be financially viable, but unable to access financing.

Another barrier to accessing financing is that the social economy organization's legal structure may not fit into lenders' commercial lending guidelines. Financial institutions look for investment control by the proprietors of the business. If a social economy organizations is a not for profit, there is no "owner". The non-profit, democratic and social nature of

the social economy enterprises means that they are not focused on benefiting the managers or owners.

At the other end of the continuum, many social economy organizations are unable to access grant financing from foundations because they do not have charitable status. Their business like structure or their mission may not fit within the limited definition set-out in the Charities Act. As many foundations make charitable status a requirement this can limit grant based financing.

In 2004, the Canadian federal government recognized the potential of this sector and budgeted for \$100 million over 5 years to provide social economy enterprises with access to patient capital. Due to a change in the party governing Canada, the launch of the new Social Economy Financing Program has been delayed. If it is launched, it will mark the first time the Government of Canada will offer both grants and patient capital to social economy organizations and enterprises.

Terminology - Micro-credit vs Community Investment

In Canada, the term micro-credit is only used to describe business loans for individuals. We use the term "community investment" to describe the provision of accessible capital and support services for both economically and socially excluded individuals and communities across Canada.

The term community investment encompasses loans, loan guarantees and equity investments to a wide range of target markets. In Canada, community investing is targeted at the following five markets:

Entrepreneurs

There are various types of loans and investments to help entrepreneurs start up or expand micro-businesses, small businesses, worker co-ops, and social

enterprises. In Montreal, ACEM - Montreal Community Loan Association make loans to small businesses and worker co-ops. PARO in Thunder Bay make peer loans available to women starting businesses.

Women, recent immigrants, refugees and minorities

There are funds that specialize in providing loans for training, post secondary education and business development to women, recent immigrants, refugees and minorities. The Black Business Community Investment Fund in Halifax, Fonds d'Emprunt Communautaire Féminin in Lachute, Quebec, and the Alterna in Toronto, have designed loan products to meet the needs of target groups such as women, convention refugees, immigrants, and specific ethnic groups.

Environment

Environmental funds lend to businesses, organizations, and community development projects that support conservation and that incorporate ecological and/or social values in their operations. Ecotrust makes conservation financing to projects and enterprises in British Columbia's coastal areas.

Underserved neighbourhoods and communities

Some funds, such as the Jubilee Fund in Winnipeg, specialize in financing essential services for socially and economically excluded urban and rural communities. They provide loans or equity support for the building of community facilities such as day cares, centres for seniors and special needs groups, employment training centres, recreation centres and others.

Individuals who need housing

There are different ways of making capital available to support affordable housing. Financing can be made available to support housing programs, including housing co-ops, non-profit rental or loans can be made to

developers to build rental housing. For example, the Quint Development Corporation in Saskatoon and VanCity Credit Union facilitate affordable housing loans. The Saint John Community Loan Fund and MCC Calgary offer security deposit loans.

Characteristics of the community investment sector in Canada

Community based

Typically Canadian community investment funds or programs are created by a community that has undertaken a strategic planning process or a needs assessment that has identified a lack of accessible capital as a barrier to development.

In Canada, most funds evolved independently in different regions of the country and almost each one has a unique structure and lending methodology. For example, some organizations have been formed independently as non profits or cooperatives. Sometimes organizations funded by the Federal government, called Community Futures Development Corporations, have initiated special financing programs. There are credit unions that partner with community organizations and /or with foundations to provide lending, deposit or granting programs. There are faith based group that operate loan funds.

Many Canadian alternative lending programs are community based and work hard to cultivate a sense of community ownership over projects.

Flexible and responsive

Community investment funds or programs are designed to be flexible enough to make loans and equity investments to groups within the social economy that would otherwise be excluded. Most community based lending programs are able to respond to local challenges or opportunities, adapt to particular clients constraints and be responsible to local issues and cultures.

Community controlled capital

Our members have created investment instruments, usually either funds or deposits. They seek capital on an on going basis to create a pool of money that is then used to make loans and/or loan guarantees and/or equity investment capital. Often local community members are on the loan review committee and the Board of Directors of the organization and as such, control how the capital will be used in the community.

Alternate risk assessment methods

The staff or volunteers managing the community financing program then identify borrowers, assess applications, manage risk and ensure the capital pool is both invested and repaid. Local community members are important to making this type of financing successful. The loan review committee can be made up of community members who conduct due diligence and make lending decisions based on their in depth knowledge of local markets, costs, opportunities, and local competition.

Need for operating dollars

While these community financing mechanisms are set up with an interest fees from borrowers and sometimes administrative fees, the cost of lending usually includes training, mentoring or other forms of technical assistance for the borrower.

Unlike a mainstream lending institution, which can cover its expenses with interest payments and fees, Canadian programs incur operating expenses supporting borrowers with technical assistance programs that must be covered by individual donors, foundations or government. Unlike some micro-lending programs in developing countries, funds in Canada typically only have 50 – 300 clients. For this reason, the majority are usually unable to operate self sustaining lending programs.

The report *Calmeadow Metrofund: A Canadian Experiment in Sustainable Microfinance* chronicles the experience of an organization that set out to “prove if the stand-alone microloan fund model could be sustainable in Canada” (p.54). Calmeadow operated a micro-loan fund in Toronto from 1994 to 1999. It was unable to achieve financial sustainability in those five years. Calmeadow Metrofund differed from many other funds in that it was located on Bay Street in Toronto rather than housed within a community based organization. It did not offer its clients business training courses although sometimes worked in partnership with other organizations to help clients with challenges they faced during the start up and/or expansion of their business. A corporate base, minimal technical assistance, in addition to high staff turn-over, may have contributed to higher than usual delinquency rates. As a result, Calmeadow ended its experience and turned the portfolio over to a credit union. It is now managed and operated through Alterna Savings Credit Union.

Further research needs to be conducted in Canada to see if particular lending models, such as micro-lending programs housed within a financial institution, or other types of programs (for example affordable housing mortgages) could achieve higher levels of sustainability.

Where does the capital for community investing come from?

Coro Strandber’s paper *The Emergence of Community Investment as a Strategy for Investing in Your Community*, states that community investment is

“an opportunity for the average investor or financial consumer to allocate a portion of their investment portfolio, or to invest their savings with financial intermediaries, that are dedicated to improving local or third world socio-economic and environmental conditions... community investments pay different rates of return from zero to less

than market, and in some instances market rates.. unlike a charitable donation, the principal is returned to community investors at the end of the investment period.” (p. 6)

In Canada, the sources of capital for community financing mechanisms are diverse but almost always come from within the country. They include contributions and loans from private donors, private investors, faith based institutions, foundations, government loan-guarantees, financial institutions, pension funds and other institutions.

While the capital in the fund is owned by the community where it is based, the investors do not control the fund.

The Canadian Social Investment Review 2004, written by the Social Investment Organization, reports finding \$546 million in community investment assets including community loan funds, community development venture capital and community development credit unions.
(www.socialinvestment.ca)

The Community Investment Study 2003 by the Riverdale Community Development Corporation and the Social Investment Organization found that “the capital invested in community financing mechanisms come from multiple sources. The level of risk assumed by investors varied with the type of fund. Credit union deposits are federally insured whereas community loan funds are not.” (p. 8)

Source of capital	% of funds w/ capital from this source
Private investors	50%
Private donors	44%
Government *	35%
Foundations	26%
Credit union Depositors	21%
Union	12%
Co-op develop. Fund	6%
Community Dev. Futures Corp	6%
Line of credit- financial institution	3%
Other	6%

(Table taken from the *Community Investment Study* p.8)

Why do Canadians make community investments?

The people who invest in community investment funds are called socially responsible investors. These investors often live in the same community where the loan program operates. They want their money to create local jobs, enterprises, affordable housing, essential community services, and provide financial services to low-income individuals in the social economy. The community investment sector is a branch of the social responsible investment sector.

Different types of community investing fall along a spectrum and carry different levels of risk. Some, such as deposit programs at a credit union, are insured. Others, such as investing in a community economic development

organization with a lending program, are not insured so the Canadian investor must carry out his or her own due diligence.

Innovative policy and programs that support the growth of community investing in Canada

Since 2003, Canadian community loan funds, social enterprise funds, co-op funds, micro-loan funds and credit unions with community financing programs have organized themselves into a Pan Canadian network.

The Canadian Community Investment Network Cooperative (CCINC) is a national co-operative that operates in French and English. As of June 2006, the network had 26 members from every region of Canada.

The network's mission is to strengthen the capacity of its members to expand access to capital and support services for

- 1) Social economy enterprises, and
- 2) Economically and socially excluded individuals and communities across Canada.

The network has five goals;

- To promote the community investment sector
- To support the sustainability and growth of member organizations and the sector
- To work to increase the amount of accessible and affordable capital for use by member organizations
- To improve the capacity of practitioners through improved practice and information sharing
- To work with all levels of government to improve the regulatory environment for community investment in Canada.

The network emerged because, prior to 2003 there were no national conferences, networking events or communication mechanisms for practitioners in this country. There are still very few published Canadian documents sharing lessons learned, or describing operating procedures etc.

In the 1980s and 1990s, Canadian communities that wanted to start up alternative lending programs would use American or international research, manuals, websites. Some would attend conferences of the Association for Enterprise Opportunity or National Community Capital Association to learn about other lending programs.

In 2003, a group of community loan funds, co-op funds, social enterprise funds and credit unions initiated a study to explore how to significantly increase the sector's scale and effectiveness.

Through the course of conducting focus groups and surveys for the feasibility study for the network, many ideas for strengthening the community investment sector in Canada were put forward. Every idea, from centralized wholesale funds to shared best practice online, required a national network to increase communication and collaboration among community investment funds. (Community Investment Study, 17)

The Community Investment Study concluded that among staff of community investment funds, potential investors and related organizations, the desire for a national network, as a means to enhancing the scale, size, sustainability and effectiveness of the sector in Canada, was strong. The sector wanted to work together to improve practice, share information and advocate for an improved policy and funding environment for the sector. (p. 16)

In 2005, the Canadian Community Investment Network incorporated, set up an office, established a board of directors, developed a three year strategic

plan, launched its website and e-newsletter, and hired an Executive Director. In 2006, a membership drive was initiated and the network held its first annual general meeting to be held in conjunction with a three-day national, bilingual Community Investment and Corporate Social Responsibility (CSR) Forum. The purpose of the event was to bring together practitioners from community investment organizations, credit unions and co-operatives to explore opportunities for leadership and collaboration in order to build more sustainable communities. More information on the network is available in French and English at www.communityinvestment.ca

In addition to the national network, there are some regions and provinces of Canada with innovative programs or policies that help to stimulate community investing. Here are some examples;

Programs that support operating costs of funds

The province of Quebec supports peer lending circles and community loan funds with core funding. Community loan funds can apply for \$80 000 annually and peer lending circles can apply for \$40 000 a year. Quebec is also a province with at least 30 different funds serving different types of social economy organizations. Quebec has by far the largest number of social economy financing organizations per province in the country. www.dec-ced.gc.ca/asp/ProgrammesServices/ProgrammesServices_intro.asp?LANG=EN&HEADER=PROG_SERV&SEL_MENU=CHOIX_REGION#1_Programs

The size and strength of the sector in Quebec stands in stark contrast to the province of Ontario, which has a population of over 12 million where there is no provincial support for community investing. There are only 4 community loan funds and one credit union with a micro-credit program in the whole province.

Raising Capital

Canada has ten provinces and each one has its own provincial securities regulations. In most provinces' securities regulations, there are no regulations for community loan funds or community economic development organizations with financing programs.

There are two provinces in Canada that have developed tax credits as incentives to investors to put their money to work locally; Manitoba and Nova Scotia.

In Manitoba there is a program called the Manitoba Community Economic Development Tax Credit. Eligible investments can be made into qualifying Manitoba community enterprises or indirectly into Community Development Investment Funds

(<http://db.itm.gov.mb.ca/Databases/BRC/ProgServ.nsf/0/0fcddf1f1953441b86256eaf006516e2?OpenDocument>).

The province of Nova Scotia has two initiatives; the Community Economic Development Investment Funds and the Nova Scotia Equity Tax Credit.

<http://www.gov.ns.ca/econ/cedif/background/default.asp>

Limited loan loss reserve

The federal government in Canada has regional development agencies. The one operating in Western Canada, in the provinces of British Columbia, Alberta, Saskatchewan and Manitoba has worked with financial institutions to create a specialized series of loan programs. The website for the regional development agency describes the programs;

These loan programs target industry sectors important to Western Canada and provide flexible debt capital on terms especially suited to

the unique needs and cash flow requirements of small businesses. The loan programs are provided on commercial terms by financial institutions such as chartered banks, credit unions, trust companies, and the Business Development Bank of Canada. Each lending institution funds its own program and makes the decision on all loan approvals.

By contributing to a "loan loss reserve" that helps to offset the higher risks associated with eligible loans, WD enables these financial institutions to supply loan capital to clients who would not otherwise have access to funding.

http://www.wd.gc.ca/mediacentre/facts/pan/pan1_e.asp?printVersion=1

Challenges for the Canadian Sector

While there are some innovative programs in different parts of the country, overall the Canadian sector is small and not well supported.

As part of the feasibility study for the Canadian Community Investment Network, the members of CCINC identified the following challenges that impede the growth of the sector in Canada;

- sustaining operations through funding crises and operating shortfalls as there are, at present, very limited sources of ongoing funding for these types of funds
- attracting investors and capitalizing funds (regulations do not facilitate investment in community loan funds and there is a very poor understanding of the concept of community investing by the average Canadian investor)

- locating information on trends, opportunities, funding sources, documented lessons learned, best practices or venues for information exchange
- finding training or development opportunities for staff of community investment funds
- starting up community investment funds in areas where there is a need for alternative financing/ creating new financing mechanisms for underserved markets

Conclusion

The community investing sector in Canada is small but well established. The movement started with pioneer loan funds in the early 1980's. There are now experienced practitioners who have been working in the field for decades. Many exciting innovations have occurred as funds have grown. In addition to lending products for small businesses, affordable housing and non-profits, new loan products for specific target markets, government guarantees, research, policy initiatives and networks have been developed in different regions of the country.

We are now working nationally to ensure that all Canadians be given the opportunity to transform their own lives and contribute to their communities. We see community-based finance as a mechanism for creating resilient communities as it can be used flexibly to adapt and respond to needs and opportunities identified locally.

The members of the Canadian Community Investment Network Cooperative believe the timing has never been better to work together as a sector to significantly increase our scale and effectiveness.

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