FACTSheet

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Co-ops With and Without Share Capital

2012 International Year of Co-operatives

Introduction

Under the Ontario *Co-operative Corporations Act*, co-operatives have two different forms to choose from when incorporating: with share capital and without share capital. Each structure offers different options and benefits for raising money or carrying on operations. For the most part, this decision will be made based on the purpose of the co-operative and what types of financing are required.

The decisions around share structure and corporate structure can be complex and will depend on having a fairly good idea of what the co-op's purpose and business plan will be. It may also be advantageous for a group to seek the guidance of an accountant and lawyer familiar with co-ops to assist them with the decision making process and determining an appropriate share structure.

Share Capital

Share capital refers to shares offered by the co-operative to members or to outside investors. 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, but preference shares are available for purchase by both members and non-members (outside investors).

Share capital is generally referred to as equity, and the proceeds thereof are usually used to buy equipment, land, buildings, or provide working capital that the co-op might need. When members or investors buy shares, they receive a return on their investment in the form of patronage dividends – provided the co-operative has earned enough surplus to justify paying them.

Without Share Capital

Incorporating without share capital means that the co-op will have to rely on debt financing in order to get money. Shares cannot be offered 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. Co-ops without share capital can also use member loans, which are loans required for people to pay in order to be members in the co-operative, or loans that are paid out of the patronage that a member is eligible to receive.

This type of co-op structure can be 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.

Determining Financing Needs

Understanding what financing will be needed for the co-op's operations will help the group to decide whether or not the group needs to incorporate with share capital or without.

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 in its start-up phase or while a project is being developed?

In many cases, both a share structure and a non-share capital structure may be able to provide the co-op with the funds needed for its particular situation. However, there may also be different benefits or restrictions in choosing one form over another that may make different options available as time goes on, or restrict the co-operative from choosing other options. Some banks and financers may not be comfortable with the non-share capital structure, which may in turn limit the ability of the co-op to raise or borrow money.

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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 or not it is a co-op with or without share capital. In the case of a share capital co-op, the Articles must also indicate the total amount of capital being issued as shares and what the characteristics of each type of share are. For non-share co-operatives, the member loan amount and required investment must be specified in the Articles of Incorporation.

The Financial Services Commission of Ontario has templates for the Articles of Incorporation on its website (www.fsco.gov.on.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 that must be contained in the Articles related to share structure, there are also additional procedures and regulations associated with the sale of securities. The sale of shares and other securities (like bonds or 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 somewhat similar to a prospectus offered by a business corporation that is offering shares.

There are certain cases where an Offering Statement is not required for a co-op to sell securities. An Offering Statement is not required if the co-op:

- Has less than 25 security holders

OR

- 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).

The regulations to the Act provide a more detailed description of the conditions required to be exempt from creating an Offering Statement. Co-ops are urged to review the requirements carefully before beginning the capitalization process.

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 Commission of Ontario (FSCO), where it is then reviewed and receipted. Once the receipt has been given then, and only then, can the co-op start selling securities.

An Offering Statement is never valid for more than 12 months and updated Offering Statements must be submitted to FSCO 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. 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 FSCO within 30 days of the change occurring.

Templates are available to facilitate the creation of Offering Statements. They are available on the Ontario Co-operative Association's website www.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.

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References:

Comparison Chart of Co-ops, Businesses and NFPs – Created for the Ontario Co-operative Association by Brian Iler, Iler Campbell LLP.

CO-OPERATIVE ENTERPRISES BUILD A BETTER WORLD

FOR MORE INFORMATION, CONTACT:

The Ontario Co-operative Association
450 Speedvale Avenue West, Suite 101
Guelph, ON N1H 7Y6
Phone: 519.763.8271
info@ontario.coop   www.ontario.coop

Le conseil de la coopération de l'Ontario
435, boul. St-Laurent, bureau 201
Ottawa, ON K1K 2Z8
Phone: 613.745.8619
info@cco.coop   www.cco.coop

More resources are available at:
CoopZone Network
www.coopzone.coop

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Quick Facts About Co-operatives in Ontario:

- There are over 1300 co-operatives, credit unions and *caisse populaires* incorporated and operating in Ontario, with 1900 locations in 400 communities.
- The co-operative sector in Ontario represents a very conservative $30 billion in assets (2007). Non-financial co-ops had revenues that totaled more than $2.1 billion in 2004.
- 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)
- Over 10,000 board members are actively involved in governing and leading co-ops, credit unions and *caisse populaires* in Ontario.
- There are some 49,000 co-operative volunteers across Ontario, including board members.
- 50% of Ontario's co-ops are located in central Ontario.
- Housing is Ontario's largest co-op sector (45%), followed by Financial Services (17%), Child care (17%), and Agriculture (6%).
- Over 2,000 students at various post-secondary institutions live in Ontario student co-op housing, including Waterloo Region which is home to the second largest student housing co-operative in North America.

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