The Atmospheric Fund

Social Venture Development: Insights from the Incubation of Efficiency Capital Corporation

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INTRODUCTION

The Atmospheric Fund (TAF) incubated Efficiency Capital Corporation (ECC), a for-profit energy efficiency financing company over the course of three years, launching it in 2015 with a private investor. TAF's objective was to ensure availability of the required scale and type of financing given the market potential for energy efficiency retrofits of large residential buildings in Toronto and beyond. More specifically, ECC was conceived as a mechanism to scale up deployment of TAF's Energy Savings Performance Agreement (ESPA), a non-debt financing tool developed to address key market barriers to advancing multi-measure retrofits of large buildings.

Incubating a social venture was one impact investment strategy TAF chose to advance its mandate of reducing barriers to and mobilizing investment in energy efficiency retrofits, a key strategic carbon reduction imperative in cities.

In 2017, TAF hired Catherine Lang Consulting and Rhythm Communications to perform a third-party evaluation of the development (incubation phase) of Efficiency Capital Corporation. The evaluation's scope did not include the post-launch activities or performance of ECC; visit effeciencycap.com for an update on their current activities.

Fifteen key findings, lessons, and best practices emerged in four categories: venture development strategy, venture development process and risk mitigation, startup investment, and governance and decision-making. As an innovation-focused organization, taking the time and effort to evaluate will help TAF improve its programs, including development of any other social venture(s). We hope these findings will also be relevant to other not-for-profit organizations considering social venture development opportunities.

LESSONS & BEST PRACTICES

A. Strategy for Social Venture Development

1. Keep Mission Front & Centre

Venture development requires financial investment and expects a return on investment. A focus on financial results can overshadow social/environmental objectives instead of being a means to the end goal. It takes leadership and commitment to maintain the organization's mission as a priority or equal to the financial imperatives of a social venture.

2. Consider Venture Development in Relation to Other Change Strategies

Organizations use a variety of change strategies to advance their mandate. For example, TAF uses strategic grant making, impact investing, demonstration of policies, programs and technologies, policy reform, multi-sector convening, and social venture incubation. The latter requires significant investment of staff time and financial resources, so this strategy must be considered in the context of alternative, complementary, possibly less risky or challenging change strategies.

3. Ensure the Necessary Culture and Capacity

Venture development requires a risk-tolerant, entrepreneurial culture, a strong leadership vision, well-developed management systems, and resources. Organizations must ensure that the excitement and promise of entrepreneurial innovation and scaling up does not take precedence over developing the management systems and skills required to implement, monitor and make corrections during the venture development process.

B. Venture Development Process and Risk Mitigation

4. Communicate Aspirations and Assumptions at the Outset

Like any change strategy, social venture development is best-served by a process of articulating expected outcomes and change assumptions. The process needs to begin with a documented theory of change that is understood and endorsed by staff and the organization's governance structure. Reflecting on the theory of change throughout the development process helps to ensure that assumptions continue to hold or identify when adjustments need to be made. Changes, and the rationales for them, can then be transparent.

5. Perform Market Research and Testing

Despite perceived value of and enthusiasm for a new product or service, it is prudent to perform primary market research to identify and test demand and refine the concept before launching into a venture development process. Integrating feedback from customers or potential clients is an important way to mitigate risk and can lead to greater success down the road.

6. Set Realistic and Attainable Objectives

One of the most common mistakes made in developing a social venture is setting unrealistic objectives, including the time and resources required from concept through to launch/start-up. It is wise to create scenarios that include a best case and worst case, and ensure that there are contingency resources in the business plan.

7. Follow a Transparent Development Process

It is not uncommon for entrepreneurs to put most of their energy into day-to-day practical aspects of business development, and not give enough attention to the process, including monitoring progress and ensuring the necessary checks and balances. Establishing and following a tailored and transparent venture development plan with systems for documentation, financial controls, cost-benefit analysis, milestones and benchmarks, and go/no-go decision-making points will contribute to more effective and collaborative decision-making and accountability throughout the development process.

8. Use Proven Financial Control Systems

Financial variance analysis is a proven tool for monitoring venture development progress and making adjustments as required. Creating realistic and attainable financial forecasts for the business development costs, accurately documenting actual costs (including staff time), and performing a monthly variance analysis provides managers with the information they need to make good business decisions and assess the reality of getting their venture launched.

C. Start-up Investment & Timeframe

9. Access to Patient Capital Is Critical

Starting up a venture can be risky and costly in time and money. Not-for-profit organizations need to carefully consider whether they have access to sufficient capital and willingness to invest money, staff time, and volunteer capital in research and development, market research, business planning, communications and marketing, and management systems development.

10. Do Not Under-Estimate Incubation Costs

Unexpected costs are a reality of incubating a new business. Not-for-profit organizations can often benefit from *pro bono* expert advice and should seek perspectives and a 'reality-check' on projected costs and budget. One rule of thumb is to add 10-20 percent for contingencies; all the better if the contingencies don't happen. Dedicating time up-front to receive estimates and negotiate fixed price contracts with service providers can also be worthwhile.

11. Set Realistic Objectives and Timelines

It is common for entrepreneurs to be overly-optimistic regarding the time required to develop a venture; this is also true for revenue, market share and other objectives post-launch. Venture development timelines require careful assessment to ensure they are realistic given inevitable internal and external challenges.

D. Governance and Decision-making

12. Make Best Use of Not for Profit Governance

Many not-for-profit organizations have the advantage of well-developed governance structures and decision-making processes, which are not always present in early growth businesses. Using the built-in assets and best practices such as oversight and due diligence, communication and transparency, help mediate entrepreneurial enthusiasm and support solid outcomes. It is important to strike a balance – too much governance can detract from driving the mission and the business, where too little results in less management accountability and under-informed stakeholders.

13. Communicate Regularly and Effectively

During the long process of venture incubation, there is a risk that internal stakeholders may not feel well-enough informed. Even if unready for "prime-time," communication to external stakeholders can help lay the groundwork for a start-up. The key is to develop and implement effective and ongoing communications strategies – both for internal and external audiences – and make adjustments based on active listening. Building trust and mitigating risk are outcomes of transparent communications and accountability.

14. Learn from Others in the Field

Mission-driven not-for-profits, especially innovative and successful ones, have the ability to attract and engage expert volunteers who are willing to share their knowledge, experience and time to help the organization work towards its objectives. An external advisory committee of industry and social venture experts, separate from the volunteers with governance and fiduciary responsibilities, can provide complementary guidance during the venture development process.

15. Have an Exit Strategy

Determine the organization's tolerance for risk and investment in social venture incubation, and identify clear milestones that will provide objective signals to know when, why and how to exit.

SHARING INSIGHTS: CONCLUSION

None of these findings and lessons is unique to TAF's experience of incubating Efficiency Capital Corp. In fact, this summary echoes the literature on business development and entrepreneurship and the growing body of information specific to social enterprises. Although venture developers are unlikely to follow the 'text book' to the letter, some key insights are certain to reduce risks. Being deliberate on strategy, process, risk mitigation, governance, decision-making, and of course investment is a key take-away. Careful investment of time and intellectual capacity by staff and volunteers is crucial. A valuable practice for TAF was to keep the mission at the forefront of the incubation effort: incubating Efficiency Capital Corp. was and continues to be directly aligned with the objective of accelerating investment in retrofits, which offers the most significant and cost-effective carbon reduction opportunity in cities.

Thank you to our Consultants.

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