

## **Nico Echo Park, Benefit Corp.**

Preliminary learnings from the first Neighborhood REIT™

November 11, 2021

## Executive Summary

The Neighborhood Investment Company (Nico), Inc (“**Nico**”) was founded with a mission to localize and democratize wealth creation. Our first initiative towards this mission was the formation and launch (in March 2020) of Nico Echo Park, Benefit Corp. (“**Nico Echo Park**”), the world’s first Neighborhood Real Estate Investment Trust (“**Neighborhood REIT™**”) in the Echo Park neighborhood in Los Angeles.

After roughly 1.5 years in business we do not believe that the business is sustainable at its current scale. Earlier today, we published a proposal to our stockholders for a merger transaction that would effectively wind down Nico Echo Park, while returning capital invested plus a 5.4% return above capital invested to our REIT stockholders.

We share this preliminary white paper to reflect on key learnings, successes, and challenges that we experienced in piloting this model in Echo Park. This paper should be read in conjunction with the information statement and other documents distributed to stockholders and filed with the SEC earlier today, Nico Echo Park’s previous public filings<sup>1</sup> and other public documents including our non-financial reports.

## Context

Nico was founded to pilot an ambitious new model towards the amelioration of our society’s ever widening wealth gap within the context of the neighborhood, with the hope that we could gain as much learning as possible throughout the pilot. It is commonly observed that there is greater economic disparity in our society than ever before, and the damage done by this worsening trend cannot be overstated - it has led to further marginalization of already disadvantaged groups, to the erosion of trust in our cultural and political institutions, and has contributed to the fraying of our social fabric. While not claiming expertise on the full spectrum of forces driving this trend, we feel more confident than ever identifying a broken and outdated system of real estate ownership at the neighborhood level as a major factor, and one that has only been highlighted and amplified by the stresses of Covid.

The events of the past year and a half have rapidly accelerated the underlying, and long accruing, instability of the current system of wealth and power creation and the desire for equitable new models for ownership and community wealth creation are top of mind for many.

The spirit of Nico’s community is one that seeks to build an inclusive, sustainable, and abundant future. Our mission to localize and democratize wealth creation is rooted in a belief that in order to move towards a sustainable and inclusive society, we must evolve how wealth is defined and created.

Our theory of change in this mission has three underlying tenets:

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<sup>1</sup> <https://sec.report/CIK/0001781961>

1. Market forces are powerful, leverage them by creating products that are attractive within a larger market.
2. Leverage the power of community to shift wealth creation from an individual act, to an act of community building and community wealth creation.
3. Define success in terms of financial, social, and environmental objectives.

### **Nico Echo Park, Benefit Corp.**

Our first pilot in support of our mission to localize and democratize wealth creation was the world's first Neighborhood REIT - Nico Echo Park, Benefit Corp. Nico Echo Park was created and launched in the Echo Park neighborhood of Los Angeles in March 2020. Echo Park is a neighborhood with a rich culture and history, and which has experienced (and continues to experience) a significant amount of gentrification. A Neighborhood REIT is a new type of company designed to facilitate ownership of local real estate by a diverse group of stakeholders including local investors (with investment starting at \$100) and traditional real estate investors including bank lenders and institutional investors.

The foundational “theory of change” for this community wealth building project was to introduce an alternative ownership model for a portfolio of neighborhood real estate that allowed for a broad and diverse group of stakeholders within a community to participate in place based wealth creation and in decision making. Over time, we believe that broad local participation in a Neighborhood REIT could drive inclusive economic growth, while reducing displacement and financial exclusion for neighborhood stakeholders.

To our knowledge, Nico Echo Park is the first (and to date only) housing REIT to organize as a Benefit Corporation<sup>2</sup>. This means that unlike most companies, which have a legal responsibility to “maximize stockholder value” above all else, Nico Echo Park has a legal responsibility to balance the financial returns generated for our stockholders with the social and environmental impact that our business has on a wider group of stakeholders.

As part of our business, we have worked with community stakeholders and others to develop an Impact Assessment Framework<sup>3</sup> that outlines Nico Echo Park's non-financial objectives.

The five impact areas are:

1. Increased financial inclusion and wealth creation
2. Distributed power and stakeholder alignment
3. Improved environment and quality of life
4. Neighborhood diversity and stability

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<sup>2</sup> Benefit Corporations are also called Public Benefit Corporations, depending on the state in which they are domiciled.

<sup>3</sup> <https://mynico.com/wp-content/uploads/2019/12/Nico-Impact-Assessment-English.pdf>

## 5. Supporting a strong local economy

Our preliminary results in these areas were published in our 2020 Neighborhood Impact Report<sup>4</sup>.

### **A long-term vision for the Neighborhood REIT**

Our vision for the Neighborhood REIT model at scale is somewhat different from the relatively small scale initial pilot project that was launched in Echo Park.

At scale, we envision that a Neighborhood REIT could be among the largest owners of housing and local real estate within a neighborhood. By organizing as a Benefit Corp. (or Public Benefit Corp.), the non-financial objectives prioritized by local stakeholders could be part of each Neighborhood REITs unique charter and measure of success.

Over time, the ownership of this Neighborhood REIT could grow to include thousands of local stockholders, and be a conduit for large scale investors to invest capital alongside and in partnership with a diverse group of community stakeholders. These local stockholders could be active in determining the strategic priorities of the company (in service to local stakeholders, beyond just stockholders) - though the company itself would be managed by a third party organization that aggregated management expertise and resources on behalf of many independent Neighborhood REITs.

Over the mid- to long-term, the scope (number of local stockholders and capital invested or granted to local stockholders) and value (market value of the shares) would increase such that the local stockholders would likely grow to own a significant stake in (perhaps even a majority of) the Neighborhood REIT - a long-term local vehicle for community wealth creation, ownership, and decision making.

But community ownership itself is not the end goal here - it's a tool to ensure that as neighborhoods change (as they always have, and always will), they do so in a way that includes a broad coalition of longtime residents, businesses, and other stakeholders as principal decision makers. It's about the agency that ownership confers - the rights that owners have to participate in decision making and to determine, for themselves, how financial wealth generated through ownership can best serve them . It's also about enabling everyone within a community to have pride of ownership and about the types of community positive outcomes that we believe broad pride of ownership enables.

### **Current Status of Nico Echo Park**

At launch in March 2020 (and as of publication of this report), Nico Echo Park owns three rent stabilized multifamily rental properties in the Echo Park neighborhood, which are home to a

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<sup>4</sup> <https://mynico.com/wp-content/uploads/2021/05/Nico-Echo-Park-2020-Neighborhood-Impact-Report.pdf>

socioeconomically diverse group of approximately 120 residents and four small businesses<sup>5</sup>. The buildings were acquired using conventional real estate bank loans and equity raised from a group of mission-aligned private investors, who remain majority owners of Nico Echo Park Operating Partnership, L.P.<sup>6</sup>

The results to date have been encouraging — we’ve seen early signs that this model can play a role in increasing financial inclusion, improving quality of life with our residents, and supporting a strong local economy. Still, we expect it to take some time for such a radically different model to achieve wide-scale adoption and impact. Our experience in launching and running Nico and Nico Echo Park has increased the team’s level of conviction in the core premises of community wealth building models and the early movement towards new models for place-based community wealth building that we have been a part of. However, we view this movement towards large scale adoption of community wealth building models as being very early.

Nico Echo Park has been a beautiful and innovative early pilot in place-based community ownership, but it has not achieved sufficient scale to continue in its current form without unduly risking stockholder capital, given our current belief that the community ownership space will develop more slowly than we had initially hoped.

While we believe that Nico Echo Park has been successful in a number of important ways, management has made a proposal for a stockholder vote on a merger transaction that, if approved by stockholders owning a majority of the outstanding shares, would result in Nico Echo Park effectively winding down. Under this scenario, an affiliate of our Manager would acquire all outstanding REIT shares from stockholders for a price equal to 105.4% of initial capital invested. The board of directors for Nico Echo Park has unanimously determined that the merger transaction is advisable and in the best interests of Nico Echo Park, Benefit Corp and its stockholders.

### **Reasons for recommending a wind down**

The Covid-19 pandemic has been responsible for a challenging operating environment. Nico Echo Park’s full existence as a public company has been during the Covid-19 pandemic. While it is difficult to untangle the specific impacts of Covid on Nico Echo Park from the general changes that the Covid-19 pandemic has wrought on the neighborhood and world at large, we have a few observations:

- Given our commitment as a Benefit Corporation to engender neighborhood stability and support a strong local economy, Covid compelled us to prioritize the housing stability and security of our residents and commercial tenants over recruitment of new local investors.

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<sup>5</sup> We have previously published data on the length of occupancy (“LOO”) for our residents in our **2020 Neighborhood Impact Report**

<sup>6</sup>Nico Echo Park Operating Partnership, L.P. is a related partnership that is currently minority owned and managed by Nico Echo Park

In response to this urgent need for housing stability we designed, launched, and administered the Rent Assistance Program (“RAP”)<sup>7</sup>. This shift demonstrated a commitment to our stated values and genuinely helped our residents remain housed during this crisis. It also took the bandwidth of our small team away from efforts to build local investor participation in the model, especially during 2020.

- In a Covid-induced environment of severe volatility in the capital markets, we have had difficulty attracting enough capital to scale our portfolio as anticipated. While the fundamental performance and value of our properties remain strong, the overhead and administrative expenses of being a public company are not sustainable at the current size of our portfolio. We believe that it would unduly risk REIT investor capital to continue to incur these overhead expenses without a significant capital commitment that would enable us to scale the portfolio and have a larger base of revenue over which to spread these overhead and administrative expenses.
- Collections - ongoing impact to our residents has reduced our expected collectable cash significantly since April 2020. Though we are supportive of strong protections for renters impacted by Covid-19, this has been a significant reduction in cash available to Nico Echo Park.

**Key outcomes<sup>8</sup>**

- Stockholders earned a 5.4% return (above capital invested) by investing in Nico Echo Park, Benefit Corp., while helping to pioneer this new model for community wealth building and generating the following tangible social and environmental outcomes<sup>9</sup>:

Non-financial objective	Key outcomes
Increased financial inclusion and wealth creation	<ul style="list-style-type: none"> <li>• Among our 347 non-accredited REIT stockholders, 36.9% had annual income under \$50,000, and 71.2% had income under \$100,000</li> <li>• Among those with annual income under \$100,000, 35.6% established automatic recurring investments</li> </ul>
Distributed power and stakeholder alignment	<ul style="list-style-type: none"> <li>• Over half (60%) of our residents at 1412 Echo Park Ave provided</li> </ul>

<sup>7</sup> <https://mynico.com/blog/news/community-stability-expansion-of-nicos-rent-assistance-program/>

<sup>8</sup> Key outcomes should the merger transaction be approved and proceed

<sup>9</sup> Data referenced is as of year end 2020 and is referenced from the 2020 Neighborhood Impact Report

	<p>substantive input on our landscape renovation project prior to and during installation, including 3 residents who were able to integrate their own gardens into the project through design sessions</p> <ul style="list-style-type: none"> <li>• Among follow-up resident survey respondents, 60% reported that the upgrades increased opportunities for connection with neighbors</li> </ul>
Improved environment and quality of life	<ul style="list-style-type: none"> <li>• Approximately \$158,000 invested in common area gardens, including installation of a greywater system estimated to have saved 48,000 gallons of water. Among follow-up resident survey respondents, 90% reported these upgrades contributed to well-being</li> <li>• Energy efficient appliances utilized for 85.7% of appliance installations</li> </ul>
Neighborhood diversity and stability	<ul style="list-style-type: none"> <li>• 30 of our residents received some form of support from RAP, including \$48,696 in security deposits released and \$91,679 in direct assistance from our Community Fund</li> <li>• Of these 30 residents, 43.3% had lived in Echo Park for 5 years or more</li> </ul>
Supporting a strong local economy	<ul style="list-style-type: none"> <li>• 100% of our commercial tenants were able to remain open during the pandemic, in part due to the \$29,423 allocated through RAP</li> <li>• 81.0% of vendors engaged for property management services were based in LA County</li> </ul>

Nico Echo Park has supported and inspired a number of other efforts around the country to launch similar models and served as an important reference point for an evolving community of practice around community wealth building.

We believe that some of the key challenges we have experienced with Nico Echo Park can be mitigated through intentional design of the community wealth building vehicle, upfront coalition

building, and capitalization that both accommodates the pace of trust building and includes low barrier to entry mechanisms for encouraging participation from first time investors.

## **Key Learnings**

### *Trust building is essential*

Any community wealth building effort must include community from its inception and earn trust through actions. Trust is not itself the product, but a base level of socialized trust is important for people to engage with any effort that is community oriented. It is also important to understand that new ideas will most likely be met with resistance from some stakeholders. This resistance is informed by failed past efforts, generational distrust, and systems exclusion.

- Find balance between patience and progress. Community trust building requires patience; market-based products require progress.

### *Proving the model (and building trust) take time*

Some portion of our potential investors may have elected not to invest due to uncertainty around the time frame in which they and/or the larger community would realize financial and/or social returns. The time hurdle presented an even greater challenge as a new company without a prior track record of investment returns. We believe that community wealth building efforts centered around collective ownership of real assets should invest in safe assets, which by definition will produce slower and lower returns than higher risk investment options. The north star for Nico Echo Park - what happens when a building, block or neighborhood is majority owned by its residents - is a proposition that necessarily looks well into the future, which we believe may in turn have reduced the urgency/immediacy of the call to action for stakeholders to back the model early.

- Our belief is that successful place-based community wealth projects in the future should allow for a minimum of 3-5 years of time after launch to establish trust and a track record of investment returns.

### *First time investor hesitancy*

On countless occasions we heard some version of “This sounds amazing. It’s so needed right now. I just need to learn more about investments first.”

In exploring these conversations with people who had not previously engaged with investment products or made a self-directed investment, we perceived there to be:

- a hesitancy to invest before becoming familiar with the broader universe of available investment options and investing generally
- a consequential impulse to bucket the decision to invest similar to other healthy practices to be initiated at some later date, such as starting an exercise regimen or eating healthier

In order to address the knowledge and psychological barriers that are often connected to a first time investment decision, future place-based community wealth projects may seek to overcome these hurdles. For example, pairing tailored financial literacy/knowledge building with widely available share grants to achieve broad awareness and community alignment without requiring

first time investors to put capital at risk in order to participate.

### **Next steps**

We will be updating this preliminary white paper within 12 months with a more complete analysis of data related to Nico Echo Park and including results from stakeholder surveys that we expect to distribute before the end of 2021.

At Nico we believe that our work on community wealth building is just beginning. We are planning to continue to process lessons learned with Nico Echo Park as we evolve our mission, products, and tools towards supporting new models for community wealth building and democratic ownership.

If you are working on a community wealth building project and would like to further discuss Nico Echo Park and our key learnings, we are available for limited pro-bono project consulting and knowledge sharing.