POST-GRADUATE STUDENT RESEARCH PROJECT

Understanding the Financial Challenges Faced by Indian Social Enterprises

Prepared by

Anirudh Gaurang

MA in Social Entrepreneurship
Centre for Social Entrepreneurship
School of Management and Labour studies
Tata Institute of Social Sciences, Mumbai

Barkha Jain

MA in Social Entrepreneurship
Centre for Social Entrepreneurship
School of Management and Labour studies
Tata Institute of Social Sciences, Mumbai

Supervised by

Nadiya Marakkath

Assistant Professor
Centre for Social Entrepreneurship
School of Management and Labour Studies
Tata Institute of Social Sciences, Mumbai

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Prepared by Anirudh Gaurang and Barkha Jain*

This research is an exploratory study undertaken to understand the struggles faced by social enterprises in India, especially from a financial perspective. Through this exploration, an attempt is made to identify the ways in which Indian financial regulations can be made more enabling for social entrepreneurs. Using a literature-based analysis and a series of interviews of social entrepreneurs, we recommend changes in the existing legal structure and foreign funding norms applicable to Indian social enterprises. We expect that the findings of this study will draw regulatory attention to those aspects that need change in order to improve the financing climate for social ventures in India.

* Anirudh Gaurang and Barkha Jain are second-year students of the M. A. Social Entrepreneurship Programme at the Centre for Social Entrepreneurship, School of Management and Labour Studies, Tata Institute of Social Sciences, Mumbai. The authors would like to thank their guide Prof. Nadiya Marakkath whose guidance and constant support made this research possible. The authors are also grateful to the NSE for giving them this opportunity and for providing them a research grant for the same. The authors can be contacted at anigaurang87@gmail.com and jainbarkha31@gmail.com.

Understanding the Financial Challenges Faced by Indian Social Enterprises

1. Introduction

Social entrepreneurship is the application of innovative, practical and sustainable approaches to benefit society in general, with an emphasis on those who are marginalised and/or poor (Schwab Foundation, 2012). Institutions that undertake social entrepreneurship are known as social enterprises; they are non-profit and for-profit ventures with a blend of social, economic, and environmental values (Nicholls, 2010). An example of such a venture would be a cafeteria that employs differently-abled people to make organic ham and cheese sandwiches. Although this venture appears to be simple conceptually, it has immense potential to create value across domains by economically and socially empowering the disabled, through a model that can confer them their due dignity, through sustained livelihood options. Moreover, by using organic products, the venture remains environment-friendly, and since it is woven around an economic activity, it has the potential to return profits.

Thus, with this blended value potential, the concept of social entrepreneurship attracts wide popularity. Everyone wants a share of this highly appealing fruit, although the hardships associated with its operationalization have not been fully understood or discussed. Therefore, for a better understanding of the dynamics in the operationalization of this concept, we begin this report with a review of some of the accepted views on social entrepreneurship, which reflect the practical issues that stand in the way of translating the concept into action.

To begin, we quote Martin and Osberg (2007: 39), who highlight the need for clarity in the definition of social entrepreneurship:

> Our view is that a clearer definition of social entrepreneurship will aid the development of the field. The social entrepreneur should be understood as someone who targets an unfortunate but stable equilibrium that causes the neglect, marginalization, or suffering of a segment of humanity; who brings to bear on this situation his or her inspiration, direct action, creativity, courage, and fortitude; and who aims for and ultimately affects the establishment of a new stable

equilibrium that secures permanent benefit for the targeted group and society at large.

This definition, when read in correlation with the example of the cafeteria employing the disabled, shows that though the process of social entrepreneurship may appear to be a simplistic model woven around an economic activity, it is an extremely time-consuming one that restores dignity to society. This calls for high levels of dedication; nonetheless, it is a satisfying journey. For a social entrepreneur who undertakes this process, it ultimately fulfils a social objective, related to a problem that disturbs her/him and forces itself onto her/his consciousness to manifest itself as her/his life's mission.

Thus, a social enterprise is driven by the inner voice that incentivises the social entrepreneur's zeal to act and rectify a social pain perceived by her/him as a social wrong. In order to fulfil this social mission, the entrepreneurial efforts they put in require multiple resources, the procurement of which needs financial support. However, since social impact is hard to evaluate, and it does not result in immediate financial returns, the investment climate for the social entrepreneurship sector at large remains bleak.

Consider the following scenario. Organisations such as the Ashoka Foundation, the Skoll Foundation, the Acumen Fund, and so on came forward to support social entrepreneurs who are committed to addressing the most pressing social issues in the society. Their approach aims at recognising, promoting, and sustaining entrepreneurs to enable collective progress of society and to counter the common problems of the society in an innovative manner. For this, they provide 'fellowships' or 'seed capital' to these entrepreneurs, as well as mentoring assistance.

Although the support provided by such foundations is a boon to social entrepreneurs worldwide, very few conscious regulatory support mechanisms have been devised to recognise and promote such initiatives in a majority of the nations (barring a few recent provisions made in the U.S. and the U.K.).

This study shows that in India, a nation with innumerable issues related to social justice and equity, such a regulatory support system is largely missing. We undertook this study to understand the financial challenges faced by Indian social entrepreneurs; their experiences highlight the need for financial provisions and support mechanisms, which would consciously encourage investments and recognise the work done by social ventures in the nation. Without such systemic support, entrepreneurs often face a formidable task to sustain their social ventures. This could result in the early death of their ventures due to the lack of financial assistance.

Such sustenance-related challenges faced by social ventures due to the lack of an enabling ecosystem is a loss for the nation, especially at a time when India is considered to be on the verge of becoming a dominant global power in the near future. Given that the nation still falls behind when it comes to social justice and equality for its vast population, it is imperative for India to put in place support mechanisms that recognise and promote the prominent role played by social entrepreneurs in filling this gap and in making its growth trajectory more equitable and inclusive.

In this study, we interviewed a few Indian social entrepreneurs to know how best such provisions and support mechanisms could be devised / modified to address their sustainability-related challenges.

2. Problems Faced by Social Enterprises

In India, a social enterprise can be registered in one of three ways: as for-profit entities, not-for-profit entities, and as non-profit entities. Despite the legal distinction between for-profit and non-profit organisations, attracting early-stage investments has been a universal barrier for all social entrepreneurs.

Most of the existing financial support mechanisms for social enterprises becomes available only after an enterprise has been operational for a few years. Hardly any support systems are available during the initial period of their existence, barring the fellowships offered by a few foundations.

For this reason, non-profit social enterprises have suffered due to their complete dependence on external agencies for their sustenance. Their options to raise funds for themselves from financial institutions have been highly limited. Despite the support offered in the initial stages by prominent organisations such as the Ashoka Foundation, the Skoll Foundation, and the Indian Angel Network, it is extremely difficult for social enterprises in the initial phase of their operations to find a firm footing.

Most of these foundations are keen on offering fellowships or grants to those non-profits that have been around for a long period or have been running their operations for a few years. This policy has caused many start-ups to suffer and eventually die. This problem is aggravated in the Indian sector because of the scarcity of investors who are ready to invest and the non-income-generating nature of some of the ventures (especially those that work for the poorest of the poor).

For-profit enterprises have comparatively easier access to finance as these enterprises have a clear income stream. However, this often leads to the debilitating problem of mission drift—due to the large revenues being expected by the investors and generated by the organisation, the focus soon moves away from the entrepreneur's original social mission.

For the profit-oriented enterprises, the U.K. has come up with the concept of impact investment, which is now gaining popularity. This involves the concept of a Community Interest Company (CIC), wherein investments are made primarily with the objective of establishing a measurable social impact, with the potential for the ventures to financially scale up.

The CIC is a legal vehicle designed for social enterprises that are non-charitable (i.e., for-profit) but whose primary objective is the welfare of the society. These institutions were created to address the lack of a specific legal vehicle for non-charitable social enterprises in the U.K. (Pratt, 2009). The assets and profits earned are re-invested for the development of the community, and there is an asset lock limiting the distribution of profits and assets among its shareholders. A maximum of 35% can be distributed as profits,[1] and the funds are mainly used for the social welfare of the society. This helps to prevent mission drift and caters to the cause for which the organisation was originally started. Thus, the objective of a CIC is not to maximise profits for the shareholders but to re-invest and use the profits earned in the interests of the community. The regulator keeps a check on whether the profits and assets are being utilised properly, and it ensures that no conditions are violated and the community is not exploited in any way. The CICs are limited liability companies—either a company limited by guarantee or a company limited by shares. A charity can convert into a CIC with the consent of the Charity Commission (Schwab Foundation, 2006), but it will lose all the benefits of charitable tax exemptions. The CICs have fewer regulations than charities have.

[1] "Changes to the dividend and interest caps for community interest companies" (2013, Dec 10), Department for Business Innovation and Skills. Available at https://www.gov.uk/government/news/changes-to-the-dividend-and-interest-caps.

Individuals and corporates that invest in community development finance institutions (CDFI)[2] receive tax relief for the amount invested, known as Community Investment Tax Relief (CITR). The CDFIs should be accredited to be eligible for the CITR scheme; these CDFIs can then invest in CICs and other such enterprises that indirectly benefit from this tax relief, which makes them different from other companies. However, investors or corporates need to invest for a minimum period of five years to avail the tax relief of 5% of the amount invested for each year. Further, depending on the activities that they undertake or according to the location, they may be eligible for other tax benefits.[3] In order to get more information, the Office of the Regulator of Community Interest Companies was contacted to know about the tax benefits, if any, associated with investing in a CIC. According to the official, "Community interest companies (CICs) operate the same as ordinary companies and can secure investments from those interested bodies who wish to help promote the CIC's social purpose. There are no tax benefits for those investing in CICs."[4]

Thus, one can conclude that there are no direct tax benefits for investors investing in CICs; however, indirect tax benefits through CDFIs do exist for investments in CICs. Such indirect tax benefits for Indian for-profit social enterprises are largely absent, which is an additional setback, given the limited access to financial support from a large number of investors.

Thus, the for-profit social enterprises in the U.K. have a unique scope for attracting investors because their financial and securities markets actively promote 'impact investments,' taking into account the possibility of mission drift and devising measures to preempt this. The absence of any such incentives in India hurts budding social entrepreneurs as it leads to a lack of investors who are willing to invest in a social enterprise.

The weak financial structure in the Indian context has made it extremely difficult for a social entrepreneur to avail concrete financial support from formal financial systems. With no standardised legal model to cover the social enterprises in India, this issue of financing gets further exacerbated. Together, these factors result in a fragile environment with regard to the sustainability of these enterprises, often causing them to shut shop. On a personal level, as

[2] CDFIs provide financial support and other related support to communities that are disadvantaged and difficult to reach.
[3] "What is a Community Interest Company?" (n.d.), *Businesslegal Limited*, available at http://www.businesslegal.ltd.uk/php/community_interest_company.php.
[4] This information was gathered by one of the researchers (through email correspondence) when clarification regarding whether investors would get any tax benefits from investing in a CIC was sought from the Case Manager of the Office of the Regulator of Community Interest Companies.

students studying social entrepreneurship at the Tata Institute of Social Sciences, Mumbai, we witness first hand all these problems faced by various social entrepreneurs in this nation that are in a start-up stage and are in search of seed capital.

If we relate our personal observation to a review of the Responsible Investment and Philanthropy Services (RI-PS) framework put forward by Credit Suisse in 2012, the current nascent level of engagement of Indian investors in the social space can be better understood, and therefore, is reiterated below using this conceptual approach.

As per the RI-PS framework (shown in Figure 1), there are three forms of investments in social enterprises: philanthropic services, impact investments, and sustainable investments (Schwab Foundation, 2012). Going by this categorisation, we find that India is still at a nascent stage in terms of funding, where the majority of services are dependent on philanthropic services. In fact, philanthropists often struggle to measure the social impact delivered relative to the investments made. Financial regulations are needed to guide investors in relation to philanthropic investments. New regulations may be required to facilitate the smooth and safe transition to the next levels of investment, namely, impact investments and sustainable investments.

Figure 1
The Responsible Investment and Philanthropy Services framework
Source: Credit Suisse

Source：Credit Suisse

Thus, the investment climate for social enterprises in India is yet to reach maturity. The RI-PS framework defines a mature social investment climate as one that fosters impact investments, which are investments made with the primary intention of creating a measurable social and environmental impact, with the potential for some financial benefits as well. Thus, investors who decide to park their funds in social ventures value and monitor impact across disciplines; they understand the blended value of a social enterprise and are not motivated merely by the financial returns. Impact investors believe that such investments are more sustainable than a commercial investment that would mainly focus on financial returns. In India, such an optimistic investment climate for social investments is yet to materialise.

3. Research Objectives

Against the backdrop of the problem described in the previous section, in this research, we intend to explore the challenges faced by Indian social enterprises; we attempt to understand what would make the markets more enabling for social entrepreneurs in India. The study is driven by the following research objectives:

1. To study the challenges faced by Indian social entrepreneurs in accessing financial support.
2. To understand the perspective of Indian social entrepreneurs on the present regulatory mechanisms that are in place and to discuss the feasibility of modifying the system so as to make it more enabling for social impact investments.

3.1 Challenges Faced by Indian Social Entrepreneurs

A social entrepreneur who has struggled to establish her/his enterprise could best describe the challenges she/her faced during the formation of her/his enterprise, especially in terms of financial sourcing.

Therefore, we interviewed Indian social entrepreneurs belonging to various categories (for-profit and non-profit); these interviews helped us better understand the challenges faced by Indian social entrepreneurs. We assumed that the insights gained from the interviews would help us propose possible modifications to the existing system that would make it easier for social entrepreneurs to gain access to financial investments.

We interviewed the co-founder of Sampurn(e)arth Environment Solutions Pvt. Ltd., which provides context-based decentralised solid waste management solutions. It is a for-profit social venture that aims to operate sustainably to reduce and recycle waste, by employing marginalised rag pickers in their biogas plants and advocating environment-friendly principles of waste management. The choice of a for-profit model—though it was in line with their business model, which had income streams from the biogas plants and recycled waste—also had links to the social investor mind set in India. When asked why they chose the legal structure of a private limited company, the co-founder replied that it was also because investors look for stakes in a company. There are expectations of returns when the venture scales up; even if a private limited company were to shut shop, an investor would be able to recover some part of her/his money by selling the assets available in the organisation. Thus, overall, the for-profit private limited legal structure appeals to investors. Further, a private limited company structure helps to attract good talent and provide good salaries. Notwithstanding these benefits, he added that in this structure, as the organisation expands, there is a high possibility of mission drift creeping in. When asked whether a model similar to CICs would work in India, he was of the opinion that while the asset lock might help prevent mission drift, there would be other problems. For instance, since profit distribution is already locked by a cap, there would be problems in attracting the investors to this space unless there were direct tax benefits for the investors investing in CICs. This indicates that social investors in India are looking at something tangible in financial and taxation terms when it comes to their social investments, even if they were meant to support a social cause. The existing systems in India do not seem to have well-thought provisions for addressing these investor sentiments or the measures to prevent mission drift on account of these investor expectations.

Understanding this lacuna in our system, our next conversation was with the founder of Grassroutes (a for-profit model, registered as a private limited company), a social enterprise based on the concept of responsible rural tourism—tourism is run, managed, and owned by local village communities. He did not buy the argument that an asset lock could benefit a for-profit social enterprise as it did in a CIC context. He stated that instead of trying to follow the U.K.'s CIC model, it would be better to introduce tax benefits customised according to geography and schematics. Tax breaks for the outreach programs, training programs, and various other such initiatives of social enterprises would be extremely beneficial. Additionally, he advocated that enterprises working in remote areas should be given special status similar to the special economic zones (SEZs). He added that social enterprises face the problem of getting money, clients, and working capital, which meant that they did not have enough turnover. Additionally, these enterprises have to pay various forms of taxes. The problem of working capital is a major pain point as getting loans from banks and financial institutions is not easy for social ventures. Therefore, when a social venture chooses to opt for borrowed funds instead of equity, there are fewer options available. He proposed the following change to the current legal structure to address this gap: the working capital for social enterprises should be included in priority sector lending norms for banks; this would help them to obtain capital at a cheaper cost and would allow borrowing from banks. The fact that social ventures are addressing social causes that relate to the vulnerable and weaker sections of the society qualifies them for the priority sector category of the banks; this could also qualify them for cheaper and softer loans from financial institutions, instead of being valued on standard commercial lending norms.

With this understanding, we interviewed the founder of ESAF Microfinance & Investments Private Limited, which is a non-banking finance company (NBFC) classified as an NBFC-Microfinance Institution (MFI) by the Reserve Bank of India (RBI). Being a microfinance player, as per the existing norms of inclusive finance sector, it already qualifies for the priority sector lending norms of commercial banks; thus, in this respect, MFIs were better off compared to other social ventures in terms of financial access for on-lending. However, being in a sector where maximum cases of mission drift have been alleged in for-profit models of pro-poor lending, the ESAF founder found the CIC model relevant for India. He was of the view that this model would be ideal for social enterprises, as a certain percentage of the assets and profits need to be permanently retained within the CIC, which could be used exclusively for community benefit. He emphasised that this would prevent mission drift and not leave the commitment to the social cause to the integrity of the founders alone, with no active regulatory mechanisms to monitor and prevent dilution of the mission by investors. Such mechanisms are crucial to prevent commercial ventures from camouflaging as for-profit social enterprises, which profit their investors in the name of social good. Thus, we see that regulatory mechanisms should not just be enabling for supporting social ventures but should also be vigilant in preempting a crisis on account of nongenuine players masquerading a social ventures, especially in the for-profit models, where there is scope for maximising financial returns and lucrative exit options.

With this understanding of the gaps in the for-profit space, we conducted the next interview with the founder of SOCH (Society for children), a non-profit organisation working to rescue and rehabilitate children. Its focus is on orphans and children who had run away from their homes. This organisation tries to improve their lives by giving them appropriate livelihood skills; it has been involved in this work for the past two years. Thus, they are still in the nascent stages of operation, a period that is of critical importance for any social enterprise. Currently, they are registered as a trust and their main sources of financial aid are grants. They can never levy charges from their orphans and runaway children. They consider other market-oriented revenue streams at this inception stage when they are addressing a social pain, which is much more deep-rooted and interlinked than is externally perceived. Therefore, they have only a few donors, supporting organisations, and philanthropic funders who relate to their problem and understand their nature as a non-profit cause and the gravity of the issues they deal with without tainting them with the conventional mind set of commercial investors. However, the financial aid they receive from these limited circles is highly inadequate. They plan to scale up their services, but they are falling short of funds to take this plan ahead. Thus, their financial health has poor prognosis. Further, their non-profit legal structure severely hampers their chances of getting funds from investors other than donors and philanthropists. Impact investors seldom see any incentive to invest in them, for most of these investors are 'finance-first and impact-next investors'. This makes scalable and sustainable for-profit social ventures much more impressive to invest in compared to the non-profit ventures that are never going to have income streams or may have them as a miniscule portion of their total income mix. Thus, in comparison to scalable for-profit social ventures, the non-profit structure hinders their access to financial aid.

Despite this bleak impact investment scenario, there are many foreign supporters who relate to non-profit causes in their true spirit. However, the acceptance of foreign funds is governed by the Foreign Contribution (Regulation) Act, 2010 (FCRA), and start-ups would most likely not qualify for a FCRA certification[5]. The founder of SOCH stated that while many foreign donors

[5] The FCRA registration rules state the timeline of three years of operation as directory in nature. However, to operationalize the regulatory intentions of conferring it to only non-fraudulent and genuine players, it generally calls for scrutiny of three years of

have approached him, he has not been able to get donations from them as his organisation had not met the timeline needed for obtaining an FCRA certification. This, he says, is a big loss for the organisation as it needs all kinds of financial support in the initial phase; operating in this period is the toughest due to a lack of investors who are willing to invest in an enterprise that is social in its outlook and is in its nascent stage.

Another social entrepreneur we interviewed was the founder of Make a Space. Make a Space is a non-profit enterprise registered as a trust that works with orphans and destitute youth. They work with orphans and destitute children who are soon going to turn 18 and will be removed from their respective institutions, which were their only shelter until then. This is a major transition in their life, for they are exposed to the opportunities in the world all of a sudden, with not enough preparation to face the challenges ahead; yet, they are expected to withstand the competition and sail ahead smoothly. Some of them wish to pursue higher studies after they turn 18, and others wish to acquire skills related to livelihood options. Filling this gap, this social venture hopes to either associate these children with universities so that they can continue their education or provide them with the skills necessary to help them sustain their livelihoods. Despite such noble intentions, they find the going tough. Most institutional donors and social investors shy away from investing in such non-profit ventures primarily because of the risky nature of their work. All the work that they plan to do is still struggling to gain traction due to this non-profit model that they have adopted. Apart from this, it was sad that this organisation could not receive any financial support from foreign donors due to the stringent FCRA clauses discussed earlier. The founder was of the opinion that the timeline restriction in the FCRA should be done away with, which would benefit budding social entrepreneurs tremendously. He pointed out that although there is a danger of funds being misused by people who start organisations that exist only on paper, the rules (while being prudent) should not be oblivious of the presence of genuine start-ups who are hungry for funds. Therefore, the relaxation of the time requirement should be based on stricter monitoring methods and field verifications so that policy measures would be of real help to social entrepreneurs.

A similar view about the FCRA emerged in the final interview we conducted with the founder of the Equal Community Foundation (ECF). ECF works for the promotion of gender equitable

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track record of the performance of these institutions, as it brings more transparency in verifying the genuine purposes of the non-profits in action. Source: Registration Rules: http://www.fcraforngos.org/registration.htm behaviour and the reduction in violence against women. They are a non-profit organisation registered as a trust. The founder clearly stated that he had an extremely hard time in getting financial aid to keep his organisation running. He went on to state that his financial troubles were far from over; he is in dire need of financial support, and his current legal structure does not help in this regard. On the issue of the FCRA, his views were similar to those of the other two founders of non-profit enterprises that we had interviewed. He was also of the view that the timeline clause must be relaxed, with stricter monitoring mechanisms, to encourage new entrepreneurs to take up challenges head on instead of shying away.

3.2 Current Regulatory Mechanisms and Possible Modifications: Perspective of Indian social entrepreneurs

The various Indian social entrepreneurs we interviewed had their own views about the existing regulatory mechanisms. These opinions varied depending on what type of organisation they were in charge of and how their organisation was registered.

Almost all the private limited social enterprises we interviewed discussed how CICs would and would not work in India. The efficiency of the CIC and its capacity to attract investors were discussed. Regarding the mission drift seen when companies plan to expand and scale up, the social entrepreneurs belonging to for-profit social enterprises believed that a model like the CIC might help to prevent mission drift to some extent. However, the entrepreneurs were of the opinion that since social enterprises in India were still in the evolution phase, such rules and regulations, which would make the system more robust, could be made by the government only once the enterprises matured sufficiently.

The non-profit social enterprises clearly mentioned that the biggest hurdle they faced was with regard to financial access, especially in the initial period of operations. The primary reason for this was that the majority of social investors still understand social enterprises as ‘social businesses’ and fail to appreciate the relevance of why certain causes need to have a non-profit entrepreneurial model, which would be less business-like but still entrepreneurial in nature. The strict FCRA guidelines and the time period restriction for the FCRA grant also severely hurt their cause, when it comes to foreign funding. They strongly advocated a change in this context, as can be seen from their responses.

The founder of SOCH said that a relaxation in the FCRA regulations would greatly benefit budding social entrepreneurs. This is an extremely important step that needs to be taken to encourage budding social entrepreneurs. A similar sentiment was echoed by the founder of Make a Space who said that relaxations in the FCRA regulations should be put in place to encourage new social entrepreneurs along with adequate monitoring measures to ensure that no instances of fraud occur; these measures would lend credibility to both the legal structure as well as the non-profit social entrepreneur sector. The founder of ECF also agreed with the idea of relaxing the FCRA norms to benefit social entrepreneurs.

4. Inferences, Implications, and Recommendations

We wanted to understand the various challenges that Indian social entrepreneurs faced as well as the potential modifications to the existing system that would help create an environment that would benefit these entrepreneurs, by providing them with easier access to finance. We interviewed entrepreneurs working on diverse social issues. We identified a few common themes that recurred in all the interviews. This exercise threw light on some very interesting as well as intriguing aspects of running a successful and sustainable social enterprise in India.

Four broad themes were identified, which are discussed in detail in the following subsections.

4.1 Limited Access to Finance and Legal Structure

Almost all the social entrepreneurs we interviewed made it clear that the biggest hurdle for them is the poor access to finance, which severely hampers their growth. Since the social investment climate in India is still assuming evolving, most often, they are left to find funds for themselves. They eventually have to be supported by organisations or foundations such as the Ashoka Foundation or the Skoll foundation. Even these organisations extend help only after the entrepreneur has survived the initial days on her/his own. Thus, the biggest problem for such organisations has been to attract investors and gain their trust with regard to their mode of operations, which does not ensure any monetary returns in the near future. However, most often, the existing legal structures such as Trusts and Societies are found incapable of ensuring a democratic and professional approach in operational governance. Among the limited options available to them, they find the Section 25 company format to be the best in terms of governance and regulatory compliances. However, not all social enterprises were found to assume this form.

A similar dilemma occurs in the case of for-profit social enterprises. It is easier for them to access finance compared to the non-profit enterprises; however, compared to the purely commercial entities, they lack the firm support of investors. When they manage funds, most often their investors are not too concerned about the social cause that they are working for; instead, investors are generally focused on the possible monetary returns that come with the scalability of the venture models. Additionally, once these for-profit operations scale up, there are fewer regulatory measures (i.e., in the private limited company format that they assume) to prevent investor pressure and mission drift.

Thus, for non-profit as well as for-profit social enterprises, there is no proper legal structure that can help them obtain funds by showing their good governance mechanisms to potential investors. Further, there is no legal form that can address the danger of mission drift that can happen due to investor pressure at the time of scaling up.

4.2 FCRA and Modifications to Existing Structure

A common theme that emerged in all the interviews we had conducted, especially in those with non-profit enterprises, was related to the Foreign Contribution Regulation Act (FCRA). The FCRA is a set of regulations that oversees foreign donations to Indian organisations. The biggest beneficiaries of these donations are Indian NGOs, who are dependent on such contributions for funding due to the lack of investors who are ready to invest in them. From a regulatory perspective, organisations need to be certified by the FCRA to ensure the credibility of these organisations. However, the FCRA has a time clause attached—an organisation becomes eligible to receive foreign donations only after it has functioned for a period of three years. Though this time clause is directive and reasonable in the case of the NGOs, this restriction has serious implications for non-profit social enterprises. A social entrepreneur struggles the most at the beginning of her/his operational phase, and it is at this juncture that she/he needs the maximum access to financial contributions. A common opinion that emerged in all the interviews was that the FCRA timeline norms must be relaxed for the social entrepreneurs—many of them had been approached by foreign donors who wished to help, but they were unable to accept this assistance as they were not legally allowed to do so. All of the enterprises interviewed wanted the government to do away with the 3-year cap to promote existing start-ups and new budding social entrepreneurs. This would also differentiate them from an ordinary NGO, and therefore, would help in creating a brand for social enterprises.

Additionally, we asked them about the best current legal structure that could ensure this relaxation was beneficial, with proper compliance and credibility checks in place. All of them proposed registering as Section 25 companies as the solution. According to them, this would provide more chances of attracting investors when compared to registering as a Trust, as the governance and compliance mechanisms are higher for Section 25 companies. When asked why they had opted to register as a Trust when they were aware of the alternative, the major reason given was they wanted to prevent mission drift. A minimum number of members of the company are required to form a Section 25 company; to have such a team of people means that the entire team must be convinced of the vision that the entrepreneur herself/ himself has. This was not something they had encountered so far. If people get together merely for the sake of forming a team, there would be a very strong chance of mission drift in the future, as the others in the team would not have entered the fray with the same vision of tackling the social problem that the entrepreneur had started off with. Additionally, a minimum amount of capital would be needed for registration as a Section 25 company. Small social entrepreneurs would generally be unable to manage these aspects. This is validated by the responses of the interviewees. When asked about registration as a Section 25 company, the founder of SOCH said that it was difficult for him to find members with the same outlook towards rehabilitating children and giving them a new lease of life. This, coupled with the lack of initial capital that was needed and the complex and time-consuming process of getting the organisation registered, stopped him from registering as a Section 25 company. The founder of Make a Space had something similar to say: there was a chance of mission drift as people with a similar outlook towards the work they are doing were very difficult to come across; if they took in people just for the sake of numbers, chances of mission drift would arise in the future. For him, the mission of the organisation is sacrosanct and is not to be messed with.

Thus, if proper mentoring for team building and funding opportunities are available for such entrepreneurs through incubators and other governmental support systems, they can register as Section 25 companies, which would help them attract more investors. With a set structure in place, it would be easier to monitor such organisations and prevent them from committing fraud. All of this leads us to recommend a relaxation of the rules related to the FCRA for such companies, which would tackle the issue of access to finance from the entrepreneur's point of view as well as the issue of monitoring and fraud prevention from the government's point of view.

4.3 Tackling Mission Drift in For-Profit Enterprises

To understand what problems the for-profit social enterprises face and how to tackle them, we interviewed a few private limited companies. We explained how countries that pioneered the concept of social entrepreneurship (such as the U.K.) have been tackling this issue. We told them about CICs, how they operate, and all the regulations related to their formation and operations. The integral part of running a CIC was explained to them—the introduction of an asset lock, which would ensure that there was no mission drift and that excess monetary benefits are not misused or cause the entrepreneurs to lose their way.

The entrepreneurs we interviewed had very strong opinions regarding the implementation of regulations similar to CICs in India. Most of them did not agree that a uniform structure similar to that of a CIC would benefit for-profit entrepreneurs. The founders of Sampurn(e)arth and Grassroutes believed that the CIC is not the answer to the problems of Indian entrepreneurs. However, the NBFC we interviewed was clearly in favour of CICs. They felt that this model of CICs would be ideal for social enterprises, as a certain percentage of the assets and profits must be permanently retained within the CIC and could be used solely for community benefit. This would prevent mission drift.

Thus, the entrepreneurs were found to be largely in favour of an asset lock mechanism to prevent mission drift; however, they were wary about the efficacy of CICs in India considering the poor interest of investors in the social space. Indian regulators need to learn from the mechanisms to prevent mission drift in a CIC model and to think of a more customised legal form tailored to the needs of for-profit social enterprises in India.

4.4 Tax Breaks and Priority Sector Recognition

Another recommendation put forward by a for-profit social entrepreneur was the introduction of tax breaks for private limited social enterprises. The tax breaks should be provided according to the location in which these enterprises are working, because many such enterprises work in difficult terrains and in areas that are extremely backward. The entrepreneur strongly advocated tax benefits for enterprises working in such areas; further, special status similar to the special economic zones (SEZs) should be granted to them.

He also suggested that investments in social enterprises could be made within the priority sector lending ambit of the banks if the enterprises work for the vulnerable and weaker sections of the society. This would lead to a situation where such enterprises would not have to be completely dependent on donors, but can approach the banks for financial assistance. Thus, access to finance would become easier as they would have greater financial resources at their disposal.

5. Conclusion

This study was undertaken to understand the financial challenges faced by Indian social enterprises and the changes in regulations that are required to address these challenges. The study throws light on the areas where the Indian financial system can be made more enabling for social enterprises. We have recommended changes in the legal mode and foreign funding norms of social enterprises based on this understanding. Such regulatory interventions and an enabling ecosystem (such as incubators) that can foster early-stage mentoring and funding are critical for social enterprises to continue doing good for the society. When implemented, these changes can be expected to provide a boost to the social investment climate for India, enabling the nation to make an indelible mark in the field of social entrepreneurship.

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