

CREATING A TRULY "SOCIAL" STOCK EXCHANGE

FRAMEWORK STUDY OF SEVEN GLOBAL EXCHANGES
AND INDIA'S PROPOSED SOCIAL STOCK EXCHANGE



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Authors

Ms. Anushree Parekh

Ms. Shivina Jagtiani

Ms. Amiya Walia

Expert Advisors

Ms. Priya Naik

Ms. Julie Hunter

EXECUTIVE SUMMARY

Over the last two decades, Social Stock Exchanges (SSEs) have evolved as a potential funding mechanism for non-profit organisations and for-profit social enterprises. The SSEs instituted to date have functioned across the spectrum of impact funding, from simple grants to innovative finance to impact investment.

As India, the world's largest democracy, gears up to construct an SSE customized to the needs of the Indian organisational ecosystem, a comprehensive analysis of the experiences, structures, and learnings from SSEs across the world can aid civil society, policymakers and the private sector in their endeavour to create a more enabling environment for social organisations.

SSEs across the world have been established to direct resources and capital towards social organisations. However, their structure and design have differed depending on the maturity level of financial and philanthropic ecosystems, the participation of the corporate sector in social and environmental development, and the government's role in regulating the social sector.

This report reviews seven SSEs in Brazil, Portugal, South Africa, Jamaica, the UK, Singapore and Canada, providing general takeaways (outlined below) as well as detailed appendix analyses. Based on these findings, the report analyses the SSE recommendations proposed by India's SSE Working Group and provides some additional suggestions.

Key Findings from SSEs Across the World

DOMESTIC REGULATIONS AND TAXATION LAWS PLAY A KEY ROLE IN INFLUENCING SSE STRUCTURE

Some countries provide legal recognition to social enterprises to facilitate their listing and ensure that such organisations generate financial as well as socio-environmental returns. Others allow non-profits to earn revenue, in addition to receiving donations, enabling them to float debt instruments. Some countries have specific mechanisms on stock exchanges that allow unlisted securities to be traded or provide exemptions from full disclosure and sale requirements.

MOST SSEs INCLUDE BOTH FOR-PROFIT AND NON-PROFIT ORGANISATIONS

Developed countries with mature financial and capital markets have used SSEs to strengthen impact investing spaces for revenue-earning non-profits and for-profit entities, while developing countries have tried to be more inclusive of non-profits. The SSE structure may favour organisations not necessarily based on their quality or efficiency, but on their size, ability to speak the language of the markets, or employ English-speaking talent from the private sector, in lieu of smaller, local and/or grassroots organisations. All SSEs offer a variety of capacity-building services to social organisa-

tions, ranging from basic support to meet the eligibility criteria and monitoring and reporting assistance, to customized services such as business consulting.

SSEs FOCUS ON CERTAIN VISIBLE, THEMATIC AREAS

While SSEs are generally cause-agnostic, they are likely to perpetuate funding imbalances towards thematic areas that are more visible and lend themselves to revenue streams. A review of 123 projects listed on six SSEs showed that environment projects were the most popular (25% of all projects), likely because of the dominance of social businesses in sectors such as clean technology. These were followed by projects focused on livelihood, healthcare, and people with disabilities. Mental health, gender-based violence, care of the elderly, and policy-advocacy projects were less common. Most SSEs prioritize project financing over raising core funds to help set and scale organisational processes and systems.

WHILE SSEs ALLOW DIFFERENT TYPES OF DONORS/INVESTORS, INSTITUTIONAL INVESTORS ARE MORE COMMON

All existing SSEs allow both retail (individuals with one-off and smaller donations) as well as institutional investors (foundations or high-net-worth individuals with regular and larger donations). However, opportunities for retail investors are limited because of regulatory restrictions, lack of suitable products that balance risk and returns, and the high cost of servicing them. Most SSEs also place significant emphasis on investor/donor education to create demand for their services and sensitize stakeholders to the requirements and nuances of funding social organisations.

SSEs HAVE STRONG MEASURING AND REPORTING METRICS BUT DO NOT ALWAYS CAPTURE IMPACT

All SSEs require impact measurement and reporting from social organisations pre- and post-listing, but reflect the challenges faced by the social sector in developing robust, contextualized outcome metrics and templates. Output indicators, such as coverage in terms of the number of people impacted, are the most commonly reported metrics. Some SSEs require mandatory third-party verification of reported impact. Most SSEs measure their own impact based on the number of projects and thematic areas they have supported along with the amount of funds raised. Very few SSEs are able to capture wider changes to the social organisation ecosystem, including the enabling, standardizing policies and lower transaction costs they claim to catalyse.

SSEs FACE CHALLENGES OF SUSTAINABILITY AND SCALE

Of the eight SSEs considered in the study, three are active (Canada, Jamaica, Singapore), one (India) is proposed and four (Brazil, Portugal, South Africa, UK) are no longer in operation. Social stock exchanges' ability to cover their costs, as well as the experimental nature of early SSEs, were highlighted as relevant factors in SSE sustainability. Seven SSEs received philanthropic funding to conceptualize and kickstart operations, but this was often insufficient to finance operating costs as SSEs did not generate enough income through their fee structure, due to lack of scale and demand for their services.

SSEs HAVE THE POTENTIAL TO PLAY A ROLE IN BUILDING THE SOCIAL SECTOR

Most SSEs have played a role in strengthening social sectors in their respective countries through the introduction of standardized impact reporting and benchmarks, prompting policy changes to empower the sector, encouraging transparency and building trust among various stakeholders such as the government, social organisations, businesses and the public. However, this role has been limited by the relatively small reach and duration of many SSEs.

India's Proposed SSE

India's proposed SSE is still in development. The Securities and Exchange Board of India (SEBI) first constituted a Working Group (WG) in 2020 and then a Technical Group in 2021, with representation from civil society, to develop the framework for SSE. Our report applies findings from the comparative study of SSEs to SEBI's proposals, with the following conclusions:

WG PROPOSAL: HOUSE THE SSE UNDER AN EXISTING STOCK EXCHANGE, REGULATED BY SEBI

Analysis:

- Linkage with an existing stock exchange will likely benefit the SSE by providing it with access to infrastructure, processes and knowledge capital, as well as credibility and an investor pool.
- However, it is critical for a conventional stock exchange to possess the willingness and ability to create mechanisms that recognize SSE's social purpose, as well as a nuanced understanding of risks and returns in the social sector.
- Participative decision-making should be undertaken by a body representative of all stakeholders, with significant representation from civil society and diverse social organisations.
- A sustainable revenue model should be designed early in the process, considering a mix of fees, philanthropic seed funding, and government funding.

WG PROPOSAL: ALLOW BOTH FOR-PROFITS AND NON-PROFIT ORGANISATIONS TO LIST

Analysis:

- A key expectation from the SSE that differentiates it from other platforms is that of 'scale' – being able to reach a significant proportion of non-profits and social enterprises.
- In order to achieve scale, India's SSE should consider entry criteria for listing that allows a wide base of social organisations to participate, rather than favouring only certain types and sizes of social organisations.

WG PROPOSAL: NO LEGAL DEFINITION FOR SOCIAL ENTERPRISES

Analysis:

- This approach is intended to provide flexibility to an organisation to pursue socio-environmental objectives, regardless of legal form. However, the SSE must safeguard against impact washing by enforcing independent impact reporting measures to review and assess the self-declared impact objectives of participating organisations.
- The SSE should provide capacity building and resources to non-profit organisations to assist with meeting reporting requirements.

WG PROPOSAL: LEVERAGE OR CREATE FINANCE INSTRUMENTS, ESPECIALLY FOR NON-PROFITS

Analysis:

- The Indian SSE proposes to leverage existing instruments such as Social Venture Funds (SVFs) and Mutual Funds (MFs), and to introduce new tools such as Zero Coupon Zero Principal bonds, to mobilize increased amounts of capital for non-profits.
- Similarly, pay for performance instruments recommended by the SSE could raise capital and allow flexibility and autonomy in execution, while emphasizing outcomes.
- The SSE should encourage the use of such instruments for under-resourced and difficult issues rather than only for issues that can be easily measured.

WG PROPOSAL: CREATE A MINIMUM STANDARD FOR IMPACT AND FINANCIAL REPORTING

Analysis:

- While the Working Group's minimum reporting standard for both non-profits and social enterprises sets a floor standard, the template will need further contextualization and refinement over time.
- Financial reporting standards for non-profits created in association with the Institute of Chartered Accountants of India should be careful to avoid blind blueprinting of corporate standards to non-profits.
- All organisations, not just those listed on SSEs, should be encouraged to follow these standards to create a more streamlined and uniform reporting culture in India.

WG PROPOSAL: INCENTIVIZE INVESTORS/ DONORS AND SOCIAL ORGANISATIONS TO PARTICIPATE

Analysis:

- The SSE has suggested a range of tax incentives for donors, such as allowing 100% tax exemption on donations to all non-profits on the SSE and removing the 10% cap on income eligible for deduction. This could potentially increase donations to some non-profits, as well as the SSE's volume of engagement.
- Given that India has one of the lengthiest registration processes for non-profits in Asia, the SSE's proposal to fast-track certification and license renewal processes for listed non-profits could be beneficial. However, this might also privilege certain non-profits, particularly those with greater resources and capacity, over new, small, or grassroots organisations, potentially reducing sector diversity.
- Instead, measures that streamline registration and other reporting processes could be extended to all non-profits adhering to SSE standards and guidelines, not just those listed on the SSE.

WG PROPOSAL: ALLOW A VARIETY OF FUNDERS/INVESTORS TO PARTICIPATE IN THE SSE

Analysis:

- The SSE plans to allow a wide spectrum of investors and donors, including smaller individual (retail) investors, to meet its goal of raising new capital.
- Failure to create a sufficiently large and broad market for giving or social investing resulted in many SSEs shutting down.
- Additional thought should be given to building demand and capacity of investors to participate in the SSE, to help differentiate the Indian SSE from other fundraising platforms and ensure sustainability.

General recommendations for SSEs

DEFINE AN SSE'S MISSION AS AN AGENT OF CHANGE

SSEs differ from conventional stock exchanges in their purpose and must reflect the same in their conceptualization and operations. They should be participative and representative, with the voices of civil society, non-profits, and marginalized groups represented in SSE leadership and consultations. While SSEs can benefit from the credibility, support and networks of conventional stock exchanges, they should retain independence in decision-making. Conventional stock exchanges should support an SSE's social mission, including ensuring access to different types of social organisations and causes and respecting the different forms and needs of civil society.

BRIDGE THE INEQUALITY IN ACCESS TO CAPITAL

SSEs should strike a balance between for-profits and non-profits by creating separate platforms for each, combined with different reporting requirements and instruments, and exploring small or mid-cap funds within each platform. SSEs should ensure that tax and other incentives for those investing in either for-profit or non-profit projects are at least equal, if not greater for non-profits. SSEs should allocate funding for capacity building and reporting to enable smaller organisations to list.

PROMOTE UNDER-RESOURCED CAUSES

While SSEs can be cause-agnostic, they should also consider featuring thematic areas that are under-resourced and in need of support, in consultation with civil society. SSEs can encourage the use of innovative financing instruments to achieve such social outcomes. The choice of financial instrument should be decided based on a variety of factors such as suitability for a cause, flexibility and decision-making afforded to the non-profit, ease of design and execution, value-add over a simple grant, and costs. In addition to raising project financing, organisational funding should also be allowed.

ACTIVELY ENGAGE INVESTORS AND DONORS TO ACHIEVE SCALE AND SUSTAINABILITY

In order to ensure sustainability, SSEs have to proactively generate demand through investor/donor education, convenings, workshops, and large-scale campaigns. It is important to bring individual or small donors under the fold, despite smaller donations and higher costs, to ensure that the concept of SSE gains wider acceptability. SSEs should strike a balance between providing donors and investors with the flexibility to choose their investments, versus pooled funds that do not offer any personalization.

IMPLEMENT A ROBUST MEASUREMENT AND REPORTING SYSTEM FOR SOCIAL/ ENVIRONMENTAL IMPACT

Impact measurement tools must be selected on the basis of their relevance, objectivity and rigour while paying attention to the practicalities of time, cost, and skill required. During the nascent stage, reporting systems can be preliminary, but the SSE should continually push reporting thresholds to ensure maximum effectiveness.

ARTICULATE SSE'S OWN SUCCESS METRICS AND CONSCIOUSLY MEASURE IMPACT

SSEs should devise metrics to measure their institutional impact. They can employ a combination of direct metrics measuring the quantum of funds raised, the number of organisations impacted (across themes, size and location) as well as indirect metrics such as the impact on civil society, changes in stakeholder attitudes and improvements in impact reporting by organisations listed.



1126 16th Street NW, Suite 400
Washington, DC 20036 USA

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