

Social Stock Exchange – A way for Economic growth with Human development and Human Capital formation

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Knowing that the public sector funding, socially responsible investment, corporate philanthropy, and CSR spends will fall short of filling up the funding gap to meet the thrust of India's historic social intent (a Welfare state) along with the 2030 Agenda adopted by Member states of United Nations, setting up of Social Stock Exchanges (SSE) will open up new avenues of fund raising for the social enterprises bringing up the transparency and trust among the investors and providing them a platform to channelize their investments into social enterprises who have proven track record capable of making a deeper social impact.

Economic development of any country is not enough until it is accompanied with the activities that contribute to human capital formation and human development. Constitution makers of India were aligned with this fact and that is why, they decided that India would be a welfare state. The preamble of Indian Constitution describes India as a "sovereign socialist secular democratic republic" state. Accordingly, the Constitution has extensive provisions to ensure social and economic welfare of the people of India. Directive Principles (Article 36 to 51) in the constitution also talks about principles promoting Social and Economic Equality. (Directive Principles are basic guidelines for the state to frame rules / laws and policies).

Social Enterprises – Existing fund raising opportunities.

Over the years various efforts have been made by corporate and non-corporate organizations (NPOs / NGOs / Social Enterprises) to support the government in its various public welfare initiatives like health, education etc. Historically, Fund raising options available to these organisations are government grants, donations through personal Solicitation, Network fund raising, crowdfunding, fund raising from abroad (in case NPO has foreign contribution Regulation (FCRA) Certificate).

Government of India, also put efforts into NPO financing via providing exemption to the donors in income tax for the funds donated to these NGOs under Section 80G of Income Tax Act, introduction of CSR concept in Companies Act 2013 and through creation of online portal, NGO DARPAN. The online portal, NGO DARPAN was a step to and speed up financing process and thus promoting and creating a healthy relationship between government and NPOs. With introduction of CSR, new funding opportunity is available where in the corporates integrate the social and environmental concerns in their business operations and interaction with their stakeholders. It was made mandatory for specified companies to contribute 2% of the average net profits of the preceding 3 years towards CSR.

Challenges in fund raising through conventional methods:

Fund raising through conventional methods is always a challenge faced by all NGOs specially in developing countries.

Major challenges faced by the NPO's in fund raising are unawareness within the society and unethical practices by some of the unregistered NGOs and communities which ends up being the crucial reasons for the investors and common people to not trust and backout from donating.[i]

Another key challenge, NGO faces in fund raising is identifying and connecting with Indian philanthropists/HNIs.”[ii]. In India, the social welfare activities can be carried out by the charitable trusts registered under Indian trust Act 1882, by Societies registered under Societies Registration Act, 1860, Companies incorporated under Section 8 of the Companies Act 2013. Apart from these non-profit organisations, corporate houses, sole proprietorship firms, partnership firms also contribute towards creating a human development and capital formation.

Since such regulation are governed by different laws and regulations there is lack of comparability and uniform accounting policies and disclosures that leads to lack of transparency and difficulties in fund raising.

Social Stock Exchange – the Need of Hour

Despite of the various provisions in Constitution of India related to welfare state and numerous welfare scheme run by Government of India like the Swachh Bharat Abhiyan Sanitation programme, the Jan Dhan Bank Yojana program to bank the unbanked, make in India, Skill India and Smart cities scheme, in addition to support provided to non-profit organisations and existence of large NGOs like Ashoka, SELCO Solar, Aravind Eye Care, Narayana Hrudayalaya Charitable Trust etc, India ranked 132nd out of 191 countries as per report on the 2021 Human Development Index (HDI) released by the United Nations Development Programme.[i]

In 2015, all UN member states adopted 17 Goals for People and for Planet called Sustainable Developmental Goals (SDG) as part of 2030 Agenda for Sustainable Development. At the SDG summit in September 2019, world leaders called for a **Decade of Action** and delivery for sustainable development, and pledged to mobilize financing, enhance national implementation and strengthen institutions to achieve the Goals by the target date of 2030, leaving no one behind.[ii]

Harnessing private investment and improving access to capital have emerged as the key enablers in India to bridge the financing gap to attain the United Nations' Sustainable Development Goals (SDGs) by 2030. According to a recent Standard Chartered report titled “Opportunity 2030 SDG Investment Map”, the country requires investment to the tune of \$2.64 trillion to achieve the SDG goals and the scenario creates investment opportunities for the private sector amounting to \$1.12 trillion by 2030 in three of the 17 SDGs viz Water and Sanitation, Affordable and clean energy, Industry, innovation and infrastructure (SDG 6,7 &9).[i]

Integrating the agenda of India's historic social intent with the 2030 Agenda adopted by Member states of United Nations and sensing that the public sector funding, socially responsible investment, corporate philanthropy and CSR spends will fall short of filling up the funding gap, Indian Finance minister, Mrs. Nirmala Sitaraman, for the first time in her 2019-20 budget speech, proposed to initiate steps towards creating a fund-raising platform, under the regulatory ambit of Securities and Exchange Board of India (SEBI) for listing of social enterprises and voluntary organizations. In the budget speech, the Hon'ble Finance Minister said:

“ It is time to take our capital markets closer to the masses and meet various social welfare objectives related to inclusive growth and financial inclusion. I propose to initiate steps towards creating an electronic fund-raising platform – a social stock exchange - under the regulatory ambit of Securities and Exchange Board of India (SEBI) for listing social enterprises and voluntary organizations working for the realization of a social welfare objective so that they can raise capital as equity, debt or as units like a mutual fund.”^[i]

Subsequently, SEBI in September, 2019 constituted a working group (WG) under the chairmanship of Shri Ishaat Hussain (Ex-Director, Tata Sons) to inter-alia, make recommendations w.r.t possible structures and mechanism within securities market domain followed up by constitution of Technical Group on SSE under the chairmanship of Dr. Harsh Kumar Bhanwala (Ex-Chairman, NABARD) in September 2020.

Followed by submission of the reports of the working committee and technical group, SEBI on 25th July 2022 amended the following regulations which opens the way to establish Social Stock Exchange in India.

- Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018 (“**ICDR Regulations**”),
- Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 (“**LODR Regulations**”)
- Securities and Exchange Board of India (Alternative Investment Funds) Regulations, 2012 (“**AIF Regulations**”) were amended to provide a broad framework for Social Stock Exchange.

Social Stock Exchange – Potential benefits

As per the amended regulations, Social Stock exchange shall be a separate segment of a recognized stock exchange having nationwide trading terminals permitted to register Not-for-Profit Organizations (NPO) and / or list the securities issued by Not-for-Profit Organizations. The SSE will list only securities that raise money for ‘non-for-profit’ or ‘for-profit’ ‘social enterprises.’

Also, a NPO can simply register itself on the SSE in order to be recognized as a ‘Social Enterprise’.

A social Enterprise whether for the profit or Not for the profit organisation will benefit in the following ways through registration on Social Stock Exchange

1. Opening new avenues other than conventional one

In addition to conventional fund-raising opportunity as mentioned in earlier part of the article,

a. A Not-for-Profit Organization may raise funds on SSE through:

- issuance of Zero Coupon Zero Principal Instruments to institutional investors and/or non-institutional investors
- donations through Mutual Fund schemes as specified by SEBI;
- any other means as specified by SEBI from time to time.

The introduction of instruments like Zero Coupon Zero Principal (ZCZP) via public issue or private placement shows that the Indian capital market has grown to a level similar to developed markets in addition to bringing much-needed clarity to funding and utilisation. Zero-coupon Zero Principal bonds are neither pay any interest nor return principal on maturity. On expiry of the period or on fulfilment of the purpose for which ZCZP were issued, these were written off in investee books.

b. A For-Profit Social Enterprise may raise funds through:

- issuance of equity shares on the main board, SME platform or innovators growth platform or equity shares issued to an Alternative Investment Fund including a **Social Impact Fund**.
- issuance of debt securities.
- any other means as specified by SEBI from time to time

Securities issued by For Profit Social Enterprises shall be listed and traded under the applicable segment of the stock exchange with an identifier stating that the scrip is that of a For-Profit Social Enterprise and such For-Profit Social Enterprises shall meet the eligibility criteria for the main board, SME Platform or innovators growth platform, as applicable.

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2. Building Trust through transparency

Another challenge faced by NPO's that would be met by getting themselves either register or listing on stock exchange is generating trust of various stakeholders through predefined norms and regulations for registration / listing on the social stock exchange and stringent listing requirements. Following are the extract of regulations that

ensures the transparency and build trust of investors:

a. Eligibility criteria of the Social Enterprise defined under regulation 292E of SEBI (ICDR) Regulation 2015 as amended on 25.07.2022.

As per the regulations any 'for-profit' or 'not-for-profit' entity that establish social intent through carrying of any of the activity specified in the regulation will be a social enterprise. In addition to the above, the Social Enterprise shall target under-served or less privileged population segments or regions recording lower performance in the development priorities of central or state governments; Further, the Social Enterprise shall have at least sixty-seven per cent of its activities, qualifying as eligible activities to the target population, to be established through one or more of the following:

- **Percentage of Revenue** : at least sixty-seven per cent of the immediately preceding three-year average of revenues comes for providing eligible activities to members of the target population.
- **Percentage of Expenditure** : at least sixty-seven per cent of the immediately preceding three-year average of expenditure has been incurred for providing eligible activities to members of the target population.
- **Percentage of Target population** : members of the target population to whom the eligible activities have been provided constitute at least sixty-seven per cent of the immediately preceding three-year average of the total customer base and/or total number of beneficiaries.

Further, Corporate foundations, political or religious organizations or activities, professional or trade associations, infrastructure and housing companies, except affordable housing, shall not be eligible to be identified as a Social Enterprise.

b. Credibility norms for registration of a Not for profit organisation

Following entities are entitled for registration

- (i) a charitable trust registered under the public trust statue of the relevant state;
- (ii) a charitable trust registered under the Societies Registration Act, 1860
- (iii) a charitable trust registered under the Indian Trusts Act, 1882
- (iv) a company incorporated under section 8 of the Companies Act, 2013

Above entities should

- have a valid registration certificate under relevant statue for a period of 12 month and should be at least 3 years old.
- Have valid PAN card with no income tax scrutiny ongoing,
- Carry income tax exemption certificate u/s 12A, 12AA, 12 AB valid for next 12 months.
- Must have at least 50 lakhs annual spent in past financial year.
- Must have raised funds of Rs, 10 lakhs in past financial year.

c. Disclosure requirements

Social Enterprises has to follow disclosure requirement as applicable to them. This will not only build trust of the investors/ donors but also raise a sense of accountability among office bearers of the social enterprise.

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- **An NPO in need of funds while raising the funds through Zero coupon Zero principal bonds has to make necessary disclosures not limited to vision, target statement, strategy, governance, management, operations, finance, compliance, credibility and what social impact the current and past program bring in.**
- **All Social enterprises whether registered or listed have to disclose general, governance and financial aspects within 60 days of end of financial years with minimum contents specified in SEBI (LODR) regulations.**
- **All Social Enterprises have to provide audited annual impact report (AIR) to Social Stock Exchange within 90 days from the end of financial year capturing all the contents as mentioned in guidance note issued by SEBI as annexure II of the circular on Social Stock Exchange framework issued on 19.09.2022.**
- **Listed NPOs who have raised funds through Social Stock exchange have to submit statement of utilisation of funds on quarterly basis within 45 days from the end of the quarter.**

Above eligibility, registration and disclosure requirements will meet the requirement of transparency being public scrutiny is the best way to bring in the transparency and Social stock exchange will provide that platform for public scrutiny. Information will be available in comparable forms as uniform accounting practices as well as standard disclosures will be prescribed for all social enterprise in addition to audit of the impact they made on the society in human development and human capital formation.

Social Stock Exchange – the key challenges and road ahead

First social Stock Exchange was established in 2003 by Brazil (named as Socio environmental investment Exchange), after that six more countries had introduced similar concept but at present only 3 out of 7 are active (Jamaica social stock exchange- Jamaica, Impact Investment Exchange- Singapore, and Social Venture Connexion- Canada). While, Jamaica (JSIM) allows fund raising through donations, Singapore IIX allows raising of funds through bonds. Canada (SVX) allows fund raising through loans, private Equity and preference shares.

While other Social Stock exchange in world offer fund raising either by “for the profit” or by “Not for the profit” organisation – India provides platform to both type of entities.

Though Social stock exchange setup with an objective to act as a bridge among investors / private sector and social sector, it carries challenges to be successful and it is an evolving concept. To be more attractive and successful Government may take following measures in the coming years:

- **for donors to buy securities on SSE Ministry of finance may look at to amend tax deduction U/s 80 G to make incentive of 100% tax deduction as opposed to a current 50% tax deduction on making a regular donation or grant.**

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- Making investment in ‘zero-coupon, zero-principal’ instruments/bonds issued by Not-for-profit social enterprises listed on the SSE, eligible for 100% tax deductions through amendment in Income Tax Act 1961.
- Giving incentives to Risk investors to provide funds to the social enterprises.
- Purchase / investment in securities issued by NPOs or FPSEs will be eligible as CSR expenditure.

Unquestionably, the advent of Social Stock Exchanges is a positive development for the charity and stock markets. While “for the profit” and “Not for the profit” will enjoy equal status getting registered or listed on the social stock exchange will enhance their visibility and credibility. At the same time, this will build the confidence of investors / donors through increased transparency and accountability of the office bearers of the Social enterprises.

[1] <https://www.cxooutlook.com/major-challenges-faced-by-ngos-in-india-shortage-of-funds-and-infrastructure/>

[2] <https://timesofindia.indiatimes.com/blogs/developing-contemporary-india/the-fundraising-challenges-plaguing-indian-nonprofits/>

[3] https://hdr.undp.org/system/files/documents/global-report-document/hdr2021-22pdf_1.pdf

[4] The Sustainable Development Agenda - United Nations Sustainable Development

[5] Social stock exchange to boost investability of social impact projects - The Economic Times (indiatimes.com) & Standard Chartered Opportunity 2030 (sc.com)

[6] https://www.indiabudget.gov.in/budget2019-20/doc/Budget_Speech.pdf