Financial instruments and mechanisms of funds’ allocation to Social Economy

Recommendations for implementation financial instruments

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Content:
1. Annotation .......................................................................................................................... 3
2. State of play, stakeholders of SE and their needs .................................................................. 5
3. Support of social entrepreneurship at EU level ..................................................................... 10
4. To match the financial needs of social enterprises ............................................................. 13
   4.1. The quality of the business environment and regulatory framework for social enterprises 13
   4.2. The quality of the financial environment for social enterprises .................................. 17
   4.3. Strengthening the capacity .......................................................................................... 21
List of abbreviations ............................................................................................................... 23
1. Annotation

The learning Network for better future of Social Economy (NBFSE) was a project of 7 EU member states: Poland, Belgium-Flanders, Sweden, the Czech Republic, Italy-Lombardy, the UK-England and Finland represented by national or regional authorities and their experts. Apart from participation of the core partners - ESF Managing Authorities, other public authorities, experts and social economy representatives at the local, regional, national and European level participate in the project. The leader of a transnational partnership was the Ministry of Regional Development in Poland; the Czech Ministry of Labour and Social Affairs is responsible for managing the strand Financial instruments and mechanisms of funds’ allocation to social economy.

Activities of working group “Financial instruments” were focused on:
1) The identification of financial instruments and mechanisms of financing, particularly in countries of NBFSE partners;
2) The analysis of financial instruments, the process of their shaping, aims, conditions for the recipient, ensuring capacities, and mechanisms of assessment (evaluation);
3) The assessment of strengths and weaknesses, transferable elements, the role of ESF (ERDF) and
4) The evaluation of the legal framework for the implementation of financial instruments.

This document presents main outputs and outcomes of Financial Strand shaped into series of recommendations.

The proposed recommendations should contribute:
- to increase of capacity building of policymakers at national and regional level,
- to share of best practices,
- to enforce successfully proposals submitted by SBI and new generation of the cohesion policy 2014 +.

Outputs are closely correlated with the activities and recommendations of other strands of the NBFSE. An analysis of individual financial instruments and mechanisms that we have provided repeatedly faced to the confusion regarding the application of state aid rules. Managing authorities emphasized the complexity of these issues, which resulted in postponing start implementation of some tools. Progress made in this area have become an important factor affecting the viability of a number of plans of managing authorities.

The issue of social franchising is closely tied to the theme of financing of social enterprises. Experience in providing resources for the development of these networks, financial relations within this structure represent a stimulus for the formulation of new financial instruments.

Modification SROI methods for the needs of social entrepreneurship can use this tool for assessing the effects of various types of financial instruments and mechanisms.
The present recommendations aims to help policymakers and ESF and ERDF managing authorities to organise the implementation of a financial mechanism particularly through financial engineering in the frame of their social entrepreneurship policy. The document considers role of stakeholders and touches the main decision points in a policy shaping process. It is based on practical examples from NBFSE countries and regions which were analyzed in terms of their functioning. These examples may be described as innovative and can be considered as good practice.

It is obvious that the different stage of development of social economy in individual countries and regions have to be reflected in the intensity of using various tools. However, understanding the quality of the environment in the field of SE is necessary to define the needs and sequence of steps that will address them.

The ESF represents an unique tool that allows solving most problems of SE. ESF is able to support most of the measures linked to the development of SE. Its resources can be used to finance the vast majority of the identified needs such as:

- to **provide resources to strengthen the capacity of the business** (education, business skills, creating business plans, financial management needs);
- to **promote the consulting services supply supporting SE in time of their creation, but also in the business**;
- to **improve access to capital (investment, working)** - loans, equity;
- to **encourage local financial intermediaries** - increase of resources;
- to **strengthen the capacity of financial intermediaries** - their ability to work with SE.

However, problem is the **creation of comprehensive financial mechanisms** (rules of combination resources affect the ability to create complex products - financial tools plus consulting services and education of stakeholders) and inadequate experience of some countries and regions with non-grant financial mechanisms. Uncertainties regarding the application of state aid may represent another problems - in many cases (because of doubt) solved only by de minimis rule. This attitude results in addressing the consequences, but not the causes of problems.

We identified cases of insufficient willingness to provide service to applicants - strengthening entrepreneurial skills, increasing the capacity of social entrepreneurs and low willingness of financial intermediaries to use additional resources to the creation of products for social enterprises (oligopoly at market of financial services). It is a system deficiency that must be overcome or compensated by appropriate setting of public policy. To solve these problems it is necessary to take action and make interventions that are possible to finance from the ESF substantially.

Social enterprises should be supported by different types of tools in order to influence their development, functioning in various stages of development. The idea is to create an environment that will enable effective and sustainable functioning of social enterprises (social and economic criteria).
Supporting tools should combine grant and non-grant incentives (it is possible to create one overarching mechanism or series of consecutive tools). Since it cannot rely on public resources only, it is necessary to activate funds of the financial sector, third sector, citizens, etc. Access to money is only one element in the promotion of social economy and social entrepreneurship. There are also important activities in increasing capacity, entrepreneurial skills for social entrepreneurs - before and during their business, awareness of the importance of social economy among local actors (including politicians).

2. State of play, stakeholders of SE and their needs
The issue of social entrepreneurship in many countries and regions is getting in the focus of the entire society. It is subject of extensive societal debates on the role of social entrepreneurship in solving societal and social problems and the degree of involvement of the public sector (state, regions, municipalities) in resolving them. However, the achieved level of development of social economy and social business is very different. This situation is associated with the 1) value orientation of society and the attitudes to marginalized groups of population, 2) role of the governments and public sector to address social inclusion and employment, 3) level of development of civil society, 4) political and institutional tradition. Although most values are now due to role of ESF very similar, what is concerning policy focus and range of financial instruments used and the accompanying mechanisms, than there are significant differences. However, it is possible to trace some common features of attitudes of actors in social entrepreneurship and focus on their effective interaction.

Social entrepreneurs are recruited from different target groups. They are individuals from the non-profit sector, where they served as social service providers, organizers or volunteers. Furthermore, this also includes businesses growing from so-called third sector, often strongly community-based, reflecting the mutuality and shared responsibility. Another group represents people with business experience who share social and environmental values and try to apply the practice in the business (provide social services, produce environmentally friendly products, employ disadvantaged people, involve democratic way of managing of the enterprise). Different group of entrepreneurs recruits from marginalized population groups vulnerable to labour market (disabled or disadvantaged, young graduates, persons over 50 years, ethnic and national minorities, etc.).

When starting a business they face many problems. Social entrepreneurs often have an innovative business idea, based on the needs of local communities. Their enthusiasm, however, faces a lack of realistic assessment of business opportunities (setting up a sustainable business strategy) and limited access to capital for realizing their ideas and plans. Problem is in poorly developed entrepreneurial skills, low business experience and or limited knowledge of the business environment including also rules of regulatory framework (entry into the business, conditions of employment for disadvantaged people, financial and tax aspects). However, successful start-up business is to overcome this handicap. Therefore it is important to invest in human resources, strengthening their ability to operate in the
changing business environment, be able to capture the business opportunity to acquire the necessary skills, etc. Strengthening the capacity of social entrepreneurs before starting and in the course of business is an important moment influencing the success of a business plan.

The positions of the social entrepreneurs differ in willingness to take the business risk. Entrepreneurs from the third sector and NGOs are more risk averse. When seeking to minimize it they may reject business plans that could have a chance to push the market. Another major problem is lack of capital for launch business or next qualitative development of social enterprises.

Financial market imperfections can lead to de facto exclusion of applicants - social entrepreneurs, when assessing applications for credit or venture capital. The usually presented reasons are long return of investment, lack of own resources for co-financing the project, lack of property as a guarantee for the loans, a short business history, etc. If it is not possible to rely on third-sector financial institutions (foundations, ethical banks) this situation legitimizes take action on the public sector. Its aim is to modify the conditions of the capital market, create a set of alternative financial instruments and mechanisms that would address the needs of social enterprises. Financial institutions and financial intermediaries provide allocation of free funds from savers, investors towards the entrepreneurs who bids for capital to start the business.

Financial institutions have traditionally been very conservative in assessing business opportunities and risk-averse strongly. They always try to carefully distinguish types of risks and allocated them between the financial institution (such as a bank) and the applicant.

The moral hazard of some banks which took place in recent years and caused the financial crisis leads to a re-tightening of lending rules. Implementation of Basel II and Basel III rules will greatly affect the banking practice. This development will have adverse impacts on funding of social enterprises.

Borrowed funds have to be often covered by several guarantees. This applies to both investment loans and working capital. At times it is more difficult to raise funds to finance business operations than to obtain long-term or medium-term investment credit. This policy, however, significantly reduces the chance for starting social entrepreneurs to obtain loans on the financial market.

Knowledge of the specifics of the social entrepreneurship among financial institutions and banks differs considerably. While many of them do not distinguish between traditional small and medium-sized enterprises and social businesses and therefore they applied the same scoring and evaluation rules in process of assessing the business plans, some financial institutions understood the social dimension of business and are willing to take him into account. Banks can offer special products designed for social enterprises. Motivation of banks may also result from the corporate strategy based on CSR. It is possible to demonstrate examples of products for social enterprises closely linked to marketing and promotion policy. On the other hand, for a number of large banks is creating special products for social enterprises and their financing so
expensive that they do not find these strategy as a profitable and they do not provide these services.

**Smaller financial institutions** operating in the region have greater understanding to the needs of social enterprises. These mutual financial institutions, credit unions, ethical banks know local business environment and business opportunities well, usually are able to better reflect local needs. Although the procedure for assessing business plans and applications are similar and results from efforts to reduce risks, greater knowledge of the social environment, personal contact with the applicant, close familiarity with his situation, possibilities, as well as the ability to appreciate his social capital, it increases the chance of receiving funds. Ethical banks, in addition to assessing the financial and business risks, examine the consistency of the business plan with the values of banks, with the values shared by stakeholders. There is also an opportunity to invest available funds of savers only into thematically narrowly defined areas. In addition to increased caution on lending social entrepreneurs may be another problem the lack of cheap capital that could be converted into loans.

Another aspect is the **market situation in the segment of financial intermediaries**. In many countries there is a wide structure of small and large banks, credit cooperatives, municipal unions and other financial institutions operating nationally or regionally, that due to high competition in the market segment they are able to distinguish their products according to the special needs of target groups. A different situation is on oligopolistic market controlled by large banks, which have little interest in dealing with small interest groups, or invest in development of a new segment of financial products.

In the case of equity instruments is the situation in many continental countries long precarious. These financial instruments are not widely offered on the market. This means that neither the dominant financial institutions due to lack of experience are not ready to offer these instruments massively to social enterprises. The great promise in this regard is the possibility of using the ESF and ERDF to kick off of these financial instruments. Legislative support for the establishment of European Social Entrepreneurship Funds or European Venture Capital Funds (as proposed by the European Commission), can then create the necessary institutional framework for the functioning of these mechanisms.

Yet, when trying to increase access of social businesses to funds, need to reckon with these institutions. The reason is unfamiliarity with finance practices and effective risk management on the public side, the narrow range of financial services provided by the state or regional-owned development banks (financial institutions) and the lack of a larger volume of free capital. Therefore, the public sector usually focuses on the treatment conditions on the financial market than to create alternatives to these financial institutions.

The activities of the public sector are focused on these basic financing barriers. The first is to reduce risk to an acceptable level at which the bank is able to give social enterprises the desired products. Usually they are the guarantees for a particular loans or credit portfolio.
Another strategy is to provide cheap capital to financial intermediaries for providing their own products aimed at social enterprises. It can be also used to create joint products. The advantage is in addition to the use of existing know-how also utilization of established distribution channels, allowing reach the target group in the area. Last but not least it is also the use of leverage, allowing accumulation of public and private sources.

A different model of cooperation is related to the capacity utilization of financial intermediaries for distribution products established by public sector financial institutions.

The public sector, represented by the central government, regional and local authorities, gradually appreciates the importance of social entrepreneurship to address the situation on the labour market. Creating employment opportunities for people excluded or at risk of exclusion on the labour market, increasing employment of individuals, difficulty engaged, is a major benefit of social entrepreneurship.

It turns out that even part-time jobs created naturally by social entrepreneurs contribute to the activation, self-assertion of these people, improve their quality of life. The public sector can affect the quality of the business environment by creating more favourable market conditions for social entrepreneurs. Besides the tax assignation and contributions to employment, actions in the field of education, investment in human resources - self-employed, employees, and last but not least access to financial resources play important role. These measures should improve the capacity of social entrepreneurs in a highly competitive market.

The activities of the public sector are focused on influencing four target groups:

- the social entrepreneurs, to affect their business motivation, reinforces entrepreneurial skills and competencies - the ability to detect market opportunity, creating a realistic and sustainable business plans, to lead the company, to lead and motivate employees. In addition to educational activities (here is a large contribution of the ESF), it is also the possibility of using specialized consulting services for entrepreneurs, coaching and mentoring;

- the employee, to support the acquisition and strengthen the necessary core competencies and skills, professional knowledge;

- the financial intermediary, to influence their decision on the financing of business plans - reduction of risks, providing of additional financial resources;

- to citizens; less common is an public effort to mobilize citizens to directly finance social enterprises, although are known cases of these activities at the regional level, it is more a community issue. Accumulation of capital is associated with the purchase of secured bonds, or by creating mechanisms linking investors (depositors) and the applicant (social enterprises).
The public sector can create alternative financial mechanisms to make available investment resources especially for social enterprises. These financial instruments generally require the involvement of other sources, at least co-financing of projects by the applicants. **Fiscal limitations and the current debt problems** of the public sector lead to the search for innovative approaches that would allow to mobilize financial resources and knowledge of other entities - financial intermediaries, business, NGOs, citizens. These tools should be complementary to existing mechanisms provided by private profit and non-profit sectors.

In countries with an interrupted tradition of civic engagement and civil society operate strong non-profit, mutual organizations that can provide input (equity) or lending capital. They also create a network of companies, through which borrow available funds to ensure the operation of their social enterprises. They focus on mobilising citizens in order to provide resources for financing investment activities of social enterprises, usually social services.
3. Support of social entrepreneurship at EU level

The European Union pays attention to developing the social enterprise and social economy for some time. This is evidenced by both the European Social Fund activities in many countries and regions and the creation of tools like Progress.

New dynamism represents Social Business Initiative action plan as part of a package of measures entitled the Responsible Business Initiative. The aims are to increase access to finance, particularly by streamlining the structural funds, creating a framework for social investment funds and spreading microfinance. In terms of the financing the needs of social enterprises are crucial four priorities of this Initiative:

2. Favouring the development of microcredit in Europe, in particular its legal and institutional environment (from 2014).
3. Setting up a European financial instrument of €90 million to improve social businesses’ access to funding (operational from 2014).
4. Introducing an investment priority for social enterprises in the regulations ERDF (European Regional Development Fund) and ESF (European Social Fund), as proposed in the regulatory package on the Structural Funds 2014-2020.

A comprehensive view of the need to promote of social entrepreneurship does not leave aside the issues of education, administrators’ capacity building or simplifying the implementation of rules concerning state aid.

Two key funding mechanisms will be available for development of social enterprises. The first channel represents European financial instrument, an initiative, which will provide an easier access to finance for social businesses. It will be a part of the European Union Programme for Social Change and Innovation and will amount to circa EUR 90 ml. This program will be directly managed by the European Commission. Together with the European Social Fund and European Globalisation Adjustment Fund is the third pillar of the EU Employment and Social Inclusion 2014-2020. This programme will integrate three previously separate existing programs and expand their scope. This is a Community program PROGRESS (Programme for Employment and Social Solidarity), EURES (European Employment Services) and the European Microfinance PROGRESS for employment and social inclusion. This will allow the European Commission to strengthen the political coherence and impact of its instruments, which have common objectives and thereby contribute to the Europe 2020. PSCI will promote policy coordination, sharing of best practices, capacity building and testing of innovative policies to expand the most successful measures for ESF support.

In addition, the support of social enterprises under national and regional cohesion policy programmes will be financed from European Social Fund (ESF) and European Regional Development Fund (ERDF) interventions in the Member States and regions.

Drafts of new regulations were published in relation to the preparation of the next programming period of cohesion policy. The ESF 2014-2020 could divide EUR 84bn, of which more than 20% must be focused on social inclusion and combating poverty.
The 6 of the 18 investment priorities are closely related to social economy and social entrepreneurship: active inclusion, integration of marginalised communities, combating discrimination, enhancing of access to services, promoting social economy and social enterprises, community-led local development. These draft regulations for the programming period 2014-2020 is now discussing with the Member States.

In proposal of Common Strategic Framework\(^1\) is very strongly supported promoting the social economy and social enterprises:
– capacity-building and support structures for the promotion of social enterprises, in particular through social entrepreneurship education and training, networking, the development of national or regional strategies in partnership with key stakeholders, and the provision of business development services and easier access to finance;
– mobilisation of funds to support initiatives in the social economy and social entrepreneurship.

Citizens, social businesses and investors into social businesses (i.e. social or impact investors), will be the main beneficiaries of the measures proposed by the Commission. These measures are designed to boost social businesses which are social in their means, or in their ends, as they e.g.:
- produce goods or services through social and professional integration of disadvantaged people, and thus creating jobs in social inclusion businesses, or
- provide social services and/or goods and services to the local community, or to vulnerable persons (access to housing, health care, assistance for elderly or disabled persons, dependency management, access to basic banking services, child care, employment and training services, etc.).

Imperfections in the venture capital led to the following acts on the draft new European framework for the functioning of these institutions.

The European Commission presented a proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on European Venture Capital Funds (EVCF), regulating venture capital. According to the Commission’s apparent need for this regulation in relation to the financial crisis and a general denial of funding for small and medium enterprises. In this context, consider that a balanced measure consisting of a regulation that encourages investment in SMEs in the EU, in combination with direct support from public funds.

The proposal provides for a uniform set of rules for this type of administrative entity under the name “European venture capital.” European venture capital fund must meet three basic requirements: 1 invests at least 70% of assets in SMEs; 2 These SMEs provide equity or quasi-equity funds (ie “new capital”); 3 does not use financial leverage (ie the fund does not invest more capital than investors who put in and so the fund does not indebted to). When raising funds throughout the EU, all funds that operate under

\(^1\) Elements for a Common Strategic Framework 2014 to 2020 the European Regional Development Fund, the European Social Fund, the Cohesion Fund, the European Agricultural Fund for Rural Development and the European Maritime and Fisheries Fund ANNEXES
that name, uniform rules and meet the quality (including requirements for disclosure of information to investors and operational requirements). This single set of rules to ensure investor understanding about the implications of investment in European venture capital funds. Only then the fund may use the title "European venture capital."

Furthermore, the Commission on 7 12th 2011 presented a proposal REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on European Social Entrepreneurship Funds (ESEF). The aim of the draft of regulation is to lay down the strong foundations for a vital European market of social investment funds. It introduces a new term "European funding for social enterprise" in order the investors could distinguish funds that focus on investments in European social enterprises. Fund which wants to be accepted as the "European Fund for Social Enterprise" will have to show that spends a high share of investment (at least 70% of assets held by investors) to support social enterprises. Due to a uniform disclosure rules, investors will receive clear and concise information about these investments.

The proposal also sets out the requirement to inform investors about how the funds will proceed in monitoring and reporting the impact of their activities. Furthermore, the proposal will simplify the rules of the Member States focused on this type of fund.

Due to the fact that investing into social enterprise brings a number of risks (including risks losing the entire investment) will be able to invest in these funds so-called professional investors only. After introduction of legal framework, the Commission may review the measures that make available these investments to the public.

Design of the EVCF of the proposed regulation ESEF complementary (with the exception of the investment strategy is a material change in essentially the same). Both proposals however aim to achieve different objectives and the two proposals, if enacted, will exist as separate legislation.
4. To match the financial needs of social enterprises
4.1. The quality of the business environment and regulatory framework for social enterprises

The legal system and regulation does not create an immediate barrier to business development. However traditional legal forms of profit oriented entities are subject to specific requirements relating to their status. In the case of business entities it is to maximize profits (which is not the purpose of social entrepreneurship), regular framework can impose restrictions on business behaviour of different forms of NGOs (foundations, charities). On other side, most countries and regions indicated that the system does not provide sufficient support for the operation and development of social enterprises. In other words, entrepreneurs in the social economy in some countries faced with insufficient institutional support from the government. The reason is the lack of harmonization of employment policies, social inclusion and social entrepreneurship. The cause may be also unclear relationship between support of small and medium enterprises and social entrepreneurship, which is roofed by different authorities.

The natural development of entrepreneurship was in some countries previously interrupted and suppressed civil society, the lack of institutional support can significantly slow the development of social entrepreneurship. It is also emphasized the lack of co-ordination between the various support systems and policies including weak cooperation central, regional and municipal authorities. We must not forget that social entrepreneurship grows out of local society and is always closely connected with local and regional economy. Inappropriately set the regulatory framework, public policies misalignment, low willingness to establish cooperation between the public sector and social economy entities harming the business environment and business climate for the creation and development of social enterprises.

It seems that public administration in many countries is not ready to take advantage of huge potential associated with a growing dynamism of social entrepreneurship.

Recommendation:
Policy makers and ESF MA:

It is necessary to align active employment policy, social inclusion and promoting social entrepreneurship. It is appropriate to seek solutions that will harmonize support for social enterprise with development policy for small and medium enterprises.

The harmonization of national support to social entrepreneurship with Social Business Initiative.

It is need to strengthen the issue of social entrepreneurship in the National Reform Programmes in relation to Strategy EU2020.
It is necessary to set up complex support schemes combining traditional instruments of active employment policy - such as education, training, among other things aimed at strengthening business skills, ability to formulate a business plan and manage their own business.

Support of development of social entrepreneurship requires a close coordination with formal and informal education, etc. It is necessary to spread awareness about the value of social entrepreneurship from primary school level. It is appropriate to support the development of entrepreneurial thinking, strengthen entrepreneurial skills through training in secondary schools and universities, to develop them through continuing education. What is important is the involvement of representatives of social enterprises in teaching, which allows quick acquisition of practical skills.

When setting up these schemes is required to make links between actors from different areas with different competencies. The close cooperation of central and regional authorities is usually necessary.

It seems that in some countries and regions has created support mechanisms, containing all the above elements leading to the effective promotion of social entrepreneurship.

**Hefboom, Flanders, Belgium**

Hefboom was founded in 1985 as a cooperative society for ethical investing. It was originally a private initiative which is now also supported by the Flemish government. The social partners, financial institutions, private foundations participate, by own funds, in the activities of the Hefboomu (some of them are also share holders of Hefboom). Some operational costs are covered from the funds established by the Flemish government.

Hefboom offers ethical investment products for individuals, organizations, companies and public institutions. Hefboom supports employment and training initiatives for disadvantaged groups, projects in welfare, projects focused on environment and sustainability. Hefboom supports organizations in two ways: with short and long term loans and also with advice on various aspects of enterprise policy. It is also the parent company for other initiatives such as Trividend allowing access to equity.

However, the expansion of social entrepreneurship and the ability to compete with other businesses, brings the need to clarify (modify) the application of **state aid rules**. Uncertainties regarding the application of state aid are in many cases (because of doubt) solved only by **de minimis** rule. This attitude results in addressing the consequences, but not the causes of problems.

Support from public funds and use of social clauses in the case of **public procurement** is often avoided due to the creation of unequal market position and harming competition. Simplification and clarification of these rules for makers of financial instruments would greatly accelerate the implementation of these tools into practice.

**Recommendation:**

[Image of logos: ESF, European Commission, Operational program, etc.]
**EU and European institutions:**

To facilitate the use and mutual combination of tools developed at European level. It is necessary to set clear rules for state aid in promoting of social enterprises. To strengthen the capacity of social economy actors in the field of state aid and public procurement regulated by EU legislation. Significant progress would be a formulation of the methodology that would include procedures to effectively address the issue of state aid. It could contain examples of good practice in supporting the creation of various financial mechanisms with the participation of public resources.

One of the mechanisms that can be used in order to improve the business environment to social enterprises is the application of tax breaks and preferential accounting practices. It can be, for example, preferential amortization of assets and other accounting operations that accelerate the consumptions of costs during a year. In the case of reporting profits is often applied mechanism of deductible items, the creation of funds, as well as providing tax relief or tax remission.

### In Italy

The tax support system of social entrepreneurship is complex and considerably vary depending on the Region. Social enterprises are taken out of paying the tax on company’s income (IRES tax in Italy). Regional law No 1/2008 provides a tax break for NGOs (among which we find social cooperative as well) which reduces workforce costs by 4.25%.

The social enterprises do not pay taxes on profits if they are classified as indivisible reserve (i.e. reserves which cannot be distributed to the associates). Other legal support instruments - Law No 460/97 establishes that social enterprises have to be “ONLUS” i.e. non-profit making and socially useful. For this reason, they are entitled to other special terms such as the exemption from the stamp tax (i.e. a tax normally paid to produce official documents and certificates) and other specific taxes such the tax on government concessions.

### In Lombardy

In Lombardy, there are tax subsidies on employees of social enterprises for social cooperatives in accordance with National law No 381/91. Social cooperatives employing disadvantaged people do not pay National Insurance contributions of those employees. Subsidies on newly created jobs for work integration of disadvantaged people (particularly disabled) benefit from regional funding known as “Disabled Work Dowry”.

All taxpayers in Italy have the possibility to earmark a small percentage of the taxes they owe State (i.e. 5x1000) to support no-profit organisations (social enterprises as well as universities, research centres etc.).
The tax advantages not only concern social enterprises themselves, but also those that provide financial resources, capital for social enterprises. It can then act as a relief on income tax. In the UK specific tax incentive exists - Community Investment Tax relief which is due to finish in 2012.

**Community Investment Tax Relief in the UK**

The Community Investment Tax Relief (CITR) scheme, set up under the Finance Act 2002, offers a tax incentive to investors in accredited community development finance institutions. It is run jointly by HM Revenue & Customs and the Department for Business, Enterprise & Regulatory Reform. CITR was made possible by a state aid exemption by the European Commission, which will expire in 2012.

CITR is available to any individual or company with a UK tax liability investing in an accredited community development finance institutions where the investment is held for at least five years. The taxpayer, who can either be an individual or company, receives a relief to offset against their income or corporation tax liability of 5% of the amount invested in the year the investment is made, and a further 5% in each of the subsequent four years. The total relief is worth up to 25% of the value of the investment. This tax relief is in addition to any interest or dividend paid by the community development finance institutions. Community development finance institutions lend and invest in deprived areas and markets that cannot access mainstream finance. They provide financial services to enterprises and individuals with the aim of achieving both financial and social returns.

**Recommendation:**

**Policy makers and ESF MA:**

*The introduction of simplified accounting practice for social enterprises could contribute to smooth functioning of social enterprises. It is for example preferential speedy amortization of assets during years.*

*In terms of tax there is a broad range of options such as the creation of special tax reserves, reserve funds to cover possible future losses due to greater sensitivity of social enterprises to fluctuations in the market, on the economic crisis. Other instruments are tax relief, tax abatements, etc.*

*Wider use of tools to support employment of disadvantaged groups by social enterprises - discounts on insurance, drawing on contributions to cover part of the wage costs.*

The problem is also in underdeveloped culture of collecting and processing information about the needs of social entrepreneurs. Similarly, at the level of supported products
and services is necessary to strengthen the belief that they match the clients’ needs. To make sure it is also important to carry out regular evaluations of the support measures.

4.2. The quality of the financial environment for social enterprises

Financial market imperfections weaken the possibility of social enterprises to obtain the asked resources on the open market. The usually presented reasons are long return of investment, lack of own resources for co-financing the project, lack of property as a guarantee for the loans, a short business history, etc. Private financial institutions have traditionally been very conservative in assessing business opportunities and risk-averse strongly. Implementation of Basel II and Basel III rules will greatly affect the banking practice and will result in a re-tightening of lending rules. This development will have adverse impacts on funding of social enterprises. Borrowed funds are often covered by several guarantees. This policy, however, significantly reduces the chance for beginning social entrepreneurs to obtain loans on the financial market.

Knowledge of the specifics of the social entrepreneurship among financial institutions is generally weak. Most of them do not distinguish between traditional small and medium-sized enterprises and social businesses and therefore they applied the same scoring and evaluation rules in process of assessing the business plans. Smaller financial institutions operating in the region have greater understanding to the needs of social enterprises. These mutual financial institutions, credit unions, ethical banks know local business environment and business opportunities well, usually are able to better reflect local needs.

In the case of equity instruments is the situation in many continental countries long precarious. These financial instruments are not widely offered on the market. This means that neither the dominant financial institutions due to lack of experience are not ready to offer these instruments massively to social enterprises. From this perspective, great benefit represents activities supported by the EU. The possibility of transformation structural funds to the equities, foundation seed funds’ and other similar tools is great leap forward. Support of financial engineering instruments within framework of cohesion policy was enforced already in 2006. Further progress in this area could bring European Social Entrepreneurship Funds.

The public sector can deal with this situation in three ways. Public authorities traditionally create grant mechanisms that aim is to provide initial capital for start-ups.

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2 The “Small Firms Enterprise Development Initiative”, founded in 1996. SFEDI, a not-for-profit organisation led by existing entrepreneurs and business owners, is recognized by the UK government as the national standards setting body for business support for microenterprises and entrepreneurs. SFEDI has developed standards for entrepreneurs, business advisors and staff working with potential entrepreneurs.

It provides standards to government funded departments, agencies and bodies and to major small business support organisations (banks, trade associations, major training providers and educational institutions). SFEDI standards can be downloaded here: http://www.sfedi.co.uk/standards-setting-body/standards/downloads.
Global grant “Investment support of social economy”, Integrated operational programme (ERDF), Czech Republic

It is providing the initial capital to start a business. This scheme is focused on social services providers, employers and other entities in the social economy wishing to do business, future and existing social enterprises including self-employed individuals and most forms of entrepreneurial and non-profit legal entities. Intensity support ranges from some EUR 12,000 up to EUR 200,000 (de minimis regime). A subsidy is available up to 80% of eligible project costs; the recipient will provide at least 20% of eligible project costs from his own (other) sources. Grants are distributed through mechanism of calls announced by the Ministry of Labour and Social Affairs.

The strong features of the approach are:
• the existence of financial instruments to start social entrepreneurship able to cover initial investment costs,
• applicants have opportunity to use mutually complemented grant mechanism (co-funded by ESF); MA plus IB provide support to draw resources from both programmes/instruments.

Weaknesses are:
• mechanism does not support access to working capital,
• lack of links with other tools that would allow access to capital (non grants instruments - preferential loans, microcredits, guarantees, equity)
• insufficient institutional support for the development of social entrepreneurship
• lack of follow-up care,
• insufficient anchor of support in public policies, low ability to draw funds from existing tools by applicants.

It may focus its activities on the financial intermediaries, influencing their decision on the financing of business plans - reduction of risks, providing of additional financial resources. It uses the mix of tools that are supported by the public sector, but is implemented by private financial intermediaries. A typical example is provision of guarantees for loans, provision capital to create new financial instruments administered by financial intermediaries or provision additional capital for the joint financial product.

The public sector using for this purpose funds from public budgets. The structural funds - ERDF (guarantees, loans and resources for JEREMIE program) and ESF (microcredits, JEREMIE Lombardy) play an important role.

JEREMIE ESF Lombardy is designed to promotion easier access to credit to micro, small and medium enterprises (objectives of JEREMIE) and access to employment and education to disadvantaged people in the EU (unemployed, women, disabled, etc. – ESF objectives). JEREMIE initiative as a part of ROP ESF Lombardy together with selected financial intermediaries that provide loans to disadvantaged workers who are shareholders in social cooperatives. After that, beneficiaries subscribe equity (extra or
The public sector can also create alternative financial mechanisms to make available investment resources especially for social enterprises. These tools should be complementary to existing mechanisms provided by private profit and non-profit sectors.

**Trividend – venture fund and subordinated loans, Flanders, Belgium**

Trividend participates as a shareholder of company’s equity. It becomes a minority shareholder without direct participation in the Board of Directors, but with influence on running business. Exit arrangement is usually after 6 years maximum, but it is possibility to extend it. Trividend also provides subordinated loans to companies and associations. Maximum duration is normally 10 years.

Trividend cvba is a cooperative that provides venture capital to organizations with new social co-operatives shares in a place where they carry on business). The local financial intermediaries provide credits to disadvantage people (cooperative shareholders) amounting to EUR 4,000. JEREMIE contribution is 50% - bullet component, 5-year loan for zero interest rate, with single refund. Financial institution provides the rest - amortizing component. It is also 5-year loan but with fixed rate and monthly refundable.

What is concerning a bullet component, if the beneficiary works in the cooperative for the duration of the loan and refunds the amortizing component, no refunding is required. If not than is covered by the guarantee fund (10%). In the case of amortizing component if the beneficiary does not work in the cooperative for the duration of the loan then advanced refunding. Coverage of the guarantee fund is also 10%.

Lombardy region created Jeremie fund and chose a manager – Finlombarda. The Jeremie fund manages funds in the amount of EUR 20 M. Financial intermediaries that distribute the fund’s resources were subsequently selected. After the first call in 2010 Banca Popolare di Bergamo and Federazione Lombarda BCC – each of them received EUR 5 ml.; in 2011 Banca Popolare di Bergamo, Banca Popolare Etica, Banca Popolare di Sondrio each of them obtained EUR 3 ml.

Strengths of this approach are:
- provision earmarked resources directly to disadvantaged people,
- direct focus on engagement of (potentially) excluded people,
- coherency with ROP and EU provisions and new recommendations,
- activation of local financial intermediaries to match needs of social inclusion,
- high level of co-financing by the private sector ensured,
- unique combination of loan and equity instruments,
- possibility of forgiveness the of loan repayment (ESF resources) in case of meeting project objectives,
- indirect support of financial stability of local social cooperatives.

Weaknesses are:
- limiting the use of ESF resources (orientation on inclusion),
- only a partial possibility of transfer outside Italy due to the different structure and regulation of the social economy (focus on social cooperatives).

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social value. Trividend is a public-private partnership created by the Flemish government and stakeholders of the social economy. Trividend invests money (in the form of risk capital and subordinated loans) but also offers business support in the form of guidance (shaping business plan), support and monitoring. The Trividend name refers to the "triple bottom line": people, planet and profit. Trivident provides capital directly. Direct investment up to EUR 150,000 per customer.

Strengths of this approach are:
• direct focus on social entrepreneurship,
• emphasis on real shared values of social entrepreneurship on side of applicants,
• wide range of measures,
• possibility of long term funding,
• participation of private financial intermediaries and other stakeholders (employer’s organizations, trade unions) as shareholders of Trividend.

Weaknesses are:
• uncertainties regarding the sustainability of financing during the financial and economic crisis,
• the question of financial stability of co-owners from private sphere(banks).

Recommendation:
Policy makers and ESF MA:
It is necessary to set up complex support schemes combining traditional grant mechanisms with new instruments of financial engineering. The aim is to make available funds in the different stages of development of social enterprise. Providing the initial capital investment without ensuring the sustainability of financing the firms is inefficient. It means it is also necessary to consider the availability of working capital, bridging and other similar loans.

Access to capital without the corresponding business services will not lead to accelerating the development of social enterprises segment.

Cooperation of the financial sector, non-profit sector and public sector in providing funding for social enterprises is necessary. From this perspective, it is needed that local financial intermediaries understood the role and needs of social enterprises well.

Policy makers and MA should well understand the problems of financial intermediaries, which cause lack of funding for social enterprises. Lack of capital or increased risk of lending is then possible to solve by involving of public resources.

When monitoring product development and risk management must be clear how it will occur to cover potential losses. It is a relationship between societal objectives and economic efficiency of support. The allocation of risk between the support provider (loans, equity), public sector (such as MAs of ESF programs) and applicants determine the extent of support.

EU and European institutions:
It would be appropriate to continue to strengthen the ability and capacity of Managing Authorities and other policy makers to create sophisticated financial mechanisms financed by the ESF or ERDF.
It would be fruitful to continue to promote exchange of experience among Managing Authorities regarding the provision of support for innovative solutions in ensuring resources for social enterprises.

To facilitate the use of ESF funds together with the resources of other structural funds for development of social entrepreneurship in urban and rural areas.

4.3. Strengthening the capacity

Social entrepreneurs face many problems when starting their business. Their enthusiasm, however, faces a lack of realistic assessment of business opportunities (setting up a sustainable business strategy) and limited access to capital for realizing their ideas and plans.

It involves poorly developed entrepreneurial skills, low business experience and or limited knowledge of the business environment including also regulatory framework. However, successful start-up business is to overcome this handicap. Therefore it is important to invest in human resources, strengthening their ability to operate in the changing business environment, be able to capture the business opportunity to acquire the necessary skills, etc. **Strengthening the capacity of social entrepreneurs before starting and in the course of business is an important moment influencing the success of a business plan.** This is a necessary prerequisite for the initiation and operation of sustainable social business.

Unfamiliarity with the financial environment and financial products represents only part of the problem. To increase efficiency of support for the development of social entrepreneurship is necessary to see all these aspects. **Therefore it is needed to set chain of interconnected, complementary measures that will also focus on skills development.** Many countries and regions have recognized this, i.e. already mentioned Hefboom.

The ESF presents a unique tool that allows solving most of these problems. ESF may be used for **strengthen the capacity of the social entrepreneurs, their employees** - business skills, marketing, management, financial management, creating business plans, professional knowledge etc. Resources can also be used for capacity building of providers these services.

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<th>A sub-measure 7.2.2 Support to social economy, Human capital OP, ESF, Poland</th>
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<td>Under this sub-measure is possible inter alia provide grants to (individual and group) advisory as well as trainings facilitating obtaining knowledge and skills necessary to set up and run social cooperatives,</td>
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<td>Sub-measure 7.2.2. Support social economy is focused on building the support system for SE institutions on the regional level – based on the call for proposals for already established institutions (at least 2 in the region) which provide: legal, bookkeeping and marketing services, advisory centres / points, social economy incubators, training on</td>
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how to start up and lead social economy entity, building local partnerships for SE development, promotion SE as a source of employment. These institutions are called Social Economy Support Centres.

Strengths of this approach are:
• multidimensional and integrated support (training, advisory, partnership),
• broad promotion of social entrepreneurship,
• influence of regional authorities, strategies,
• long term planning, building local/regional coalitions for social economy development.

Weaknesses are:
• funds dispersion among too many social economy entities - Social Economy Supporting Centres,
• short life of these centres and their dependency on ESF financing.

Resources can also be used to strengthen capacities of other actors in order to better understand the needs of social enterprises and adapt their products and services for this business segment (such as local financial intermediaries).

**Recommendation:**
**Policy makers and ESF MA:**

Social entrepreneurs are recruited from different target groups. Their enthusiasm to do business may be faced with a lack of readiness to operate in the market successfully. It is therefore necessary at various stages of functioning of the social to acquire needed skills and knowledge. Only this way is possible to increase the sustainability of their actions.

It is unable to separate the investment in social enterprises from investment into human capital. ESF should be significantly focused on strengthening the capacity of entrepreneurs and their employees, on developing consulting services in coaching, mentoring for segment of social enterprises.

**Strengthening the capacity of financial intermediaries is one of the ways to raise their ability to work with the SE.**

**EU and European institutions:**
It would be appropriate to support solutions that will assist each other in removing various bottlenecks associated with the development of social economy. ESF should be prepared to fund these solutions.

It is about creating projects, which will include an educational role, focus on strengthening the capacity of actors to offer investment in human resources development and access to resources for business development of social enterprises.
List of abbreviations

CITR  Community Investment Tax Relief
CZK  Czech crown
EC  European Commission
EIB  European Investment Bank
EIF  European Investment Fund
ERDF  European Regional Development Fund
ESF  European Social Fund
EU  European Union
EUR  Euro
HC OP  Human Capital Operational Programme (Poland)
HRE OP  Human Resources and Employment Operational Programme, the CR
IB  Intermediate body
JASMINE  Joint Action to Support Micro-finance Institutions in Europe
MA  Managing Authorities
NBFSE  Network for the Better Future of Social Economy
NGO  Non-governmental Organization
OP  Operational Program
PLN  Polish złoty (new)
ROP  Regional Operational Program
SFEDI  Small Firms Enterprise Development Initiative
SME  Small and Medium Enterprises
UK  the United Kingdom