The Triumphant take-off for Social Stock Exchanges in India - Transforming the Social Enterprise Financing Landscape

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Abstract

The present article delves into the need and rationale behind the creation of Social Stock Exchange (SSE) in India. It also endeavors to examine the recent developments, opportunities and challenges associated with the newly developed Indian SSE framework, while exploring its influence on the recent transformation in the Social Enterprise (SE) financing landscape in India.

Introduction

In 2003, the global emergence of the SSE concept began with Brazil taking the pioneering step to support its socially and environmentally focused enterprises. Following Brazil's initiative, several other countries of the world including South Africa, Portugal, Canada, Singapore, the U.K. and Jamaica established their SSEs subsequently. Many years later, India accepted and introduced the SSE concept in its (2019-20) Union Budget for leveraging its capital market for its SEs. The Securities & Exchange Board of India (SEBI), consequently formed two crucial groups, a Working Group (WG) and a Technical Group (TG), to facilitate the SSE's structural formation and regulatory framework development, respectively. The recommendations from the WG in June-2020 and suggestions from the TG in May-2021, paved the way for the necessary amendments to the Issue of Capital and Disclosure Requirements (ICDR-2018 Regulations), Listing Obligations and Disclosure Requirements (LODR-2015 Regulations) and Alternative Investment Funds (AIF-2012 Regulations), successively. These amendments laid the groundwork for the establishment of the SSE framework in India. Notably, the formation of a Social Stock Exchange Governance Council (SGC) became mandatory before opening an SSE segment in any existing Stock Exchange, in accordance with the SEBI norms. Next, in September 2022, SEBI released the final SSE framework, leading to the establishment of two SSE segments in India within the existing structures of the Bombay Stock Exchange (BSE) and the National Stock Exchange (NSE) in December 2022 and February 2023 respectively, and thereby, integrating the social and financial considerations of the investors as well as SEs into the SSE's operational structure, while underscoring India's commitment towards achieving its Sustainable Development Goals (SDGs) by transforming its SE financing landscape through developing a more socially reliable and responsible investing mechanism.

Social Stock Exchanges (SSEs) in Indian Context

SSEs, basically, are specialized electronic platforms, working as distinct segments within the operational structures of the recognized stock exchanges in India to facilitate a controlled, structured, transparent and responsible meeting ground where the SEs

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can interact with their investors and donors to have financial supports through a variety of financial instruments. Thus, SSEs are specially designed mechanisms to bridge the gap between the SEs and potential fund-providers, ensuring the fact that the funds are used efficiently and for the intended social impact. By leveraging a regulated environment, SSEs offer a secure and credible space for financial transactions and thereby, enhancing the trust of investors and donors in the SEs. The diverse funding options enable the SEs to scale their operations, innovate and address various social issues more effectively. SSEs, therefore, play a pivotal role in mobilizing resources for the SEs, fostering a collaborative ecosystem where social impact and financial returns coexist. This innovative approach not only empowers the SEs, but also attracts a broad spectrum of investors who are keen to contribute to social change while ensuring their investments are handled with the utmost integrity.

In India, the newly formed SSE segments (in the NSE and BSE) are regulated by SEBI and thus, offer well-delineated electronic platforms for the SEs to raise funds using diverse financial instruments to maintain their social objectives. Under the SEBI's guidance, the SSEs ensure regulatory adherence, transparency and investor safeguarding while fostering investment opportunities for the social impact generating activities and sustainable developments in the country.

The Rationale behind

SSE's core purpose is to connect the potential investors with the organizations that are actively participating in creating tangible social impacts in India, spanning across the target areas like education, women empowerment, financial inclusion, poverty and health and so on. By encouraging a hybrid or mixed kind of financing mechanism, SSEs endeavor to mobilize both traditional capital and social investment to tackle the prevailing societal challenges in the Indian economy. Notably, the Indian SSE framework distinguishes itself from that of the other countries in terms of offering better inclusivity and catering to the demands of both the SEs and the potential fund providers in a more scientific and reliable way. Most importantly, transparency and efficiency lie as the central theme of the present SSE mechanism in India to attract investors through its clear and streamlined operational and regulatory frameworks that aim at channelizing social contributions made by such investors in order to generate positive social impacts by the activities of the enrolled SEs. This approach stands in contrast to the existing milieu of Corporate Social Responsibility (CSR) and philanthropic investments which often lack uniform accessibility to the required amount of finances, needed by the SEs. In essence, the present Indian SSE framework, represents a significant step towards bridging the gap between the needs of the social investors and that of the social enterprises, as well by offering a promising avenue for sustainable social investments to foster an equitable distribution of resources among the SEs, as far as practicable and thereby, transforming the SE financing landscape in India.

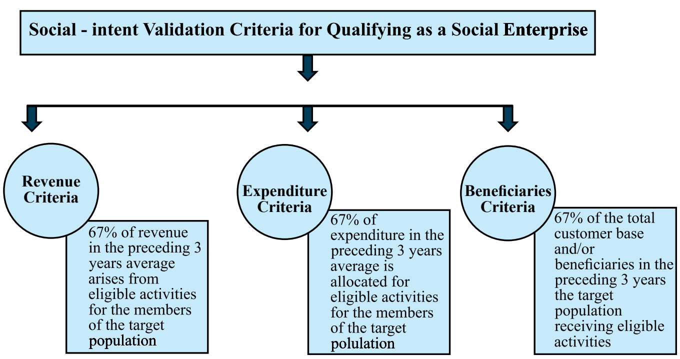
Furthermore, SSE also appeals to those investors who seek some financial returns accompanied by tangible social or environmental impacts. And, for encouraging the SEs to articulate and measure their societal impacts, SSEs offer a structured approach for social impact reporting and thereby, facilitating the assessment of their social initiatives. Such a framework also instills credibility and acknowledgment for the SEs. Moreover, being listed on the SSE, brings in a bigger responsibility upon the enrolled SEs to foster positive social change by maintaining responsible business/social practices and thereby, enhancing the trust of the investors specifically and that of the society at large.

Transformation in Social Enterprise Financing Landscape in India

The SEs, in India, play a vital role in the economy by bridging the gap between their societal aspirations and actual development and thereby, accelerating the other Governmental efforts for the overall societal development. To align with the current SSE framework in India and to become eligible to operate under the same, a SE must have to undergo certain criteria' tests such as Social-intent validation, Registration, Target segment and Eligible activity.

Firstly, in order to qualify as a SSE participant and ensure its entry into the SSE framework, a SE must meet at least one of following three social-intent validation criteria namely, Revenue, Expenditure and Beneficiary Criteria:

Chart 1: Social-intent Validation Criteria



Source: NSE database on SSE

However, any other "corporate foundations, political or religious organizations or activities, professional or trade associations, infrastructure companies and housing companies (excluding affordable housing companies)" are excluded from the SE qualifying criteria, in the present SSE framework in India.

Secondly, within the present SSE framework, the SEs in India, are allowed to operate through two modes or categories - Non-Profit Organizations (NPOs) and For-Profit Social Enterprises (FPSEs). Here, an NPO must be a registered charitable trust (under the Indian Trusts Act, 1882 or any State Public Trust Statute) or a Society (under the Societies Registration Act, 1860) or a Company incorporated under section 8 of the Companies Act, 2013 or any other entity as specified by the SEBI. Conversely, FPSEs meeting the qualifying criteria are typically for-profit entities dedicated to both social impact generation and profit-making under the ICDR-2018 Regulations, excluding Section 8 companies of the Companies Act, 2013.

Thirdly, these entities must be aiming at addressing various societal development priorities of the less privileged or underserved population segments or regions of the country.

And fourthly, these entities must engage in one or more of the 16 prescribed eligible activities (shown in Chart 2) under regulation 292E of the SEBI (ICDR) Regulations, 2018.

However, the list of eligible activities shown in Chart 2 can be extended further to include any other activity or area, if the Board or the Government of India decides so.

SSE Fundraising Modes and Financial Instruments - Transforming SE Financing

While accommodating both NPOs and FPSEs, the SSE framework mandates the NPOs to register first with the SSE platform to raise funds, whereas, FPSEs, can directly expedite listing of securities without following any prior registration. However, both the NPOs and FPSEs utilize distinct instruments prioritizing social impacts over financial gains, in line with the SSE's objective of balancing social development and

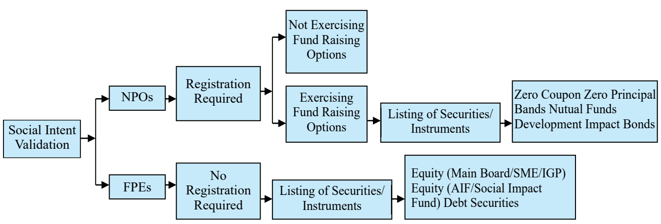
Chart 2: List of Eligible Activities

Serial No.	Eligible Activities	Serial No.	Eligible Activities
1	Work for eradicating hunger, poverty, malnutrition and inequality	*9*	Supporting non-profit ecosystem in fund raising and capacity building
2	Promoting health care services (including mental health, sanitation and supply of drinking water etc.)	*10*	Work for enhancing income of small and marginal people specially in the non-farming sector
3	Supporting education, employability and livelihoods	*11*	Facilitating sustainable living environment by promoting slum area development, providing affordable housing etc.
4	Encouraging gender equality through empowerment of women and LGBTQIA+ communities	*12*	Disaster management activities
5	Addressing issues like climate change, forest and wildlife conservation etc.	*13*	Advancement of financial inclusion
6	Protecting national heritage, art and culture	*14*	Settling land and property issues for disadvantaged group of people
7	Imparting several sports training programmes such as Rural sports, Paralympic sports and Olympic etc.	*15*	Promoting digitization by removing the issues of misinformation and ensuring data protection
8	Supporting incubators of social enterprises and entrepreneurs	*16*	Helping migrants and displaced persons

Source: NSE database on SSE

financial objectives. The following exhibit provides an overview of the fundraising instruments and modes available for NPOs and FPSEs.

Chart 3: Fundraising Modes and Instruments for NPOs and FPSEs on SSE-Platform



Source: NSE database on SE – Instruments and Process Overview

SEs, while entering into a SSE, must exhibit and prove its social intent. A NPO's registration on the SSE, with the choice to or not to raise funds, stay valid for 12 months. Conversely, FPSEs can directly list securities, highlighting their social missions.

Financial instruments for fundraising for the NPOs and FPEs include:

1. Zero Coupon Zero Principal (ZCZP) Bonds Exclusively available for NPOs, these prioritize social impact over monetary returns, concluding upon maturity or goal attainment. These bonds are generally issued by the NPOs to collect funds for a particular project or activity neither holding any obligation to repay the principal nor to pay any interest. ZCZP bonds are listed on the SSEs and are non-transferable in nature. These bonds are subject to the minimum issue size and application size of Rs. 50,00,000 and Rs. 10,000 respectively while maintaining a minimum subscription size of 75% of the proposed amount to be raised.

2. Mutual Funds: These are specially tailored for

NPO financing, presently known as Social Impact Funds (SIFs). Unlike the Social Venture Funds (SVFs), SIFs can also be used by the NPOs with no guarantee or restriction for paying off any muted return to the investors. NPOs can collect such funds by issuing of Social Units (SUs) for which investors are not allowed to claim any financial returns in future except social benefits or social returns.

3. Development Impact Bonds (DIBs): These bonds are issued to fund social projects taken up by the NPOs with pre-defined goals and involves a number of private investors such as Outcome funders who disburse funds upon goal achievement and thus, incentivize the success achieved, whereas, Risk funders provide funds on pre-payment basis and bear the associated project risks. Furthermore, at the end of the project, independent evaluators ensure impartial assessment and thereby, ensure transparency in the whole DIB funding mechanism.

4. Equity through Main Board/SME/IGP and AIF/SIF, Debts Securities and others: FPSEs aiming to issue equity shares on the Main Board, SME Platform or Innovators Growth Platform of the Stock Exchange must adhere to the eligibility criteria specified in the SEBI ICDR-2018 Regulations. Similarly, compliance with the relevant SEBI regulations is mandatory for the FPSEs for issuing equity shares through (AIFs/SIFs) and for collecting funds through debt securities or any other permitted financial instruments. This ensures regulatory consistency and transparency throughout the issuance process across various investment avenues for the FPSEs.

It is also contextual to note that under the present SSE funding mechanism, retail investors are allowed to invest in securities offered by FPSEs on the Main Board only. However, securities issued by the NPOs are restricted to institutional investors (such as Mutual Funds (MFs), Venture Capital Funds (VCFs), Insurance Companies, Scheduled Commercial Banks, etc.) and non-institutional investors (excluding retail and institutional investors). Moreover, registration with the SSEs is exclusively open for Indian entities while, foreign investors are not permitted to invest through such mechanism, presently.

Disclosure Requirements for SEs in the Present SSE Framework

In India, the SSE disclosure framework operates on a ‘self-declaration’ basis by the participating SEs and where the SEs classify themselves based on their commitment towards social objectives and other prescribed qualifying norms. The SEs must primarily focus on proving their social intents through performing specified eligible activity(s), targeting the under-privileged population groups or regions and reporting their past activities as per specified norms to justify their social intent to qualify for listing on the SSE platform. The reporting standards ensure transparency and accountability for both the FPEs and NPOs. The SE’s disclosure reporting covers social impact, governance and financial aspects (including guidance notes and fund utilization report) and thereby, helping the stakeholders in assessing an organization’s dedications and effectiveness towards social impact creation. Additionally, both the FPSEs and NPOs must produce an Annual Impact Report (AIR) within a specified time period, audited by a Social Audit Firm (amended further, recently and mentioned under the next section) for their credibility assurance.

Recent Developments and Achievements in the SSE Landscape in India

India’s SSE segments, backed by the BSE and NSE, are gaining huge attention with some renowned organizations like SGBS Unnati Foundation, Green Age, Routes 2 Roots, Sarthak Educational Trust, Ekalavya Foundation, Mukti etc. joining in. As of April

1st, 2024, BSE-SSE has 36 registered entities while, NSE-SSE has 58. Recent developments include SSE framework revision, amendments to financial instruments' issuance and disclosure requirements and incorporation of some important regulatory and developmental advisories. These developments signify the SSEs' dynamic feature for maintaining transparency and develop impactful social investment opportunities. The important recent developments are therefore, now briefly explained below:

- ***Enhanced Scope for Registration***

Previously, only entities registered under Sections 12A/12AA/12AB of the Income Tax Act and possessing a valid 80G registration were eligible for NPO registration with the SSEs. Now, entities registered under either Section 10(23C) or 10(46) of the Indian Income Tax Act, can also register. Additionally, NPOs under scrutiny by the Income Tax department can now apply for SSE registration by disclosing such scrutiny details. Further, the SSEs are now permitted to reject NPO registrations, if such scrutiny poses significant amount of risks.

- ***Flexibility in Initial Reporting***

SEBI has now relaxed the initial reporting requirements of the NPOs to report their past social impact assessment, acknowledging the unnecessary costs and delays involved in the registration process. Now, NPOs are only required to report some key parameters such as the number of the beneficiaries, cost per beneficiary and some other relevant financial aspects etc. for initial reporting.

- ***Streamlining Financial Instruments***

A registered AIF, known as a Social Impact Fund (SIF), is now made available to raise funds through the SSEs. FPSEs can issue equity shares, while NPOs can issue ZCZP bonds under the AIF mechanism. 'Social Venture Fund' (SVF) has now been replaced by the SIF. Furthermore, specific conditions related to the issuance of ZCZP instrument have been outlined. These conditions include requirements for dematerialized form, non-transferability, minimum issue and application size, as well as a minimum subscription requirement.

- ***Fund Raising Instances***

In a recent press release, dated 14th March, 2024, the NSE has announced its five pioneering listings on its SSE platform, namely, Swami Vivekananda Youth Movement (SVYM), Transform Rural India, Mukti, Ekalavya Foundation and SGBS Unnati Foundation which have emerged as trailblazers in impact-driven finance in India. The report further clarifies that these innovative listings have collectively mobilized an impressive sum of approximately Rs. 8 crore and such funds are earmarked for an array of developmental initiatives, including education, skill development, agriculture, livelihoods and women empowerment. This milestone certainly highlights the SSE's unwavering dedication in promoting sustainable social change through innovative financial strategies, in India, in the coming times.

- ***Social Impact Assessment***

According to SEBI ICDR Amendments in December 2023, the term 'Social Auditor' has now been replaced with 'Social Impact Assessor', the term 'Social Audit Firm' has now become 'Social Impact Assessment Firm', and 'Social Audit' has been changed to 'Social Impact Assessment' to make it more commensurate with the changing social impact assessment, reporting and governance scenario both nationally and internationally.

- ***Introduction of the 'Eligible Investors' Terminology***

Regarding eligible investors criteria, the words 'institutional investors' and/or 'non-institutional investors' are henceforth, substituted with the term 'eligible investors'.

• *Setting-up of Capacity Building Fund (CBF)*

A CBF, valuing Rs. 10 crores initially, has recently been set up. The CBF is made up of contributions received from the NABARD, SIDBI, NSE and BSE to aid in conducting nation-wide online and offline awareness programmes for making the NPOs and the other stakeholders aware of the SSE processes and instruments.

• *Consideration for CSR expenditures*

The SEBI and the Ministry of Corporate Affairs (MCA) are initiating joint efforts to extend the Corporate Social Responsibility (CSR) benefits for ZCZP donations via SSE route, in near future.

Prevalent Challenges in the SSE Mechanism

In India, the SSEs, while functioning as separate segments within the existing frameworks of the BSE and NSE, are experiencing the following crucial challenges:

• *Difficulties in Entry for Smaller Firms*

Expanding the SSE's scope to include a broader range of entities engaged in societal activities can enhance the impact and diversity within the country's social sector landscape and thereby, alleviate the challenges faced by social sector enterprises in meeting the prevailing SSE inclusion criteria. Moreover, by offering some relaxations in the operational and reporting norms for the smaller firms, Indian SSEs may attract smaller firms to enhance its inclusivity.

• *Social Impact Evaluation/Assessment*

Social impact evaluation is inherently subjective, posing serious challenges in assessment using readily-available metrics. Thus, conducting thorough research is very crucial to develop accurate and standardized evaluation metrics and which seems to be a daunting task for the SSEs.

• *Nascent Phase of Development*

The SSE mechanism in India is in its early stage. As a result, some of the proposed benefits for the investors NPOs and FPEs remain uncertain and yet to yield real-term benefits. Until these measures are implemented fully and their impacts are observed, the potential benefits for the beneficiaries may remain theoretical, only.

• *Liquidity Crux*

Liquidity issue in relation to the securities is another challenge for the SSEs and which stems from limited investor-base and fewer investment opportunities, resulting into severe hindrances in quick liquidation of such investments on the SSE platforms unlike the traditional stock exchanges.

• *Balancing Profit-motives and Social-intents*

Balancing profit motives with social impact goals presents enormous challenges before the SSEs as investors mostly seek financial returns accompanied with positive societal outcomes. Clear and stringent guidelines and norms must, therefore, be outlined and strictly observed to prevent or restrict such conflicts of interest between the philanthropic investments and the return-oriented investments, for the smooth operation of the SSE framework.

• *Experience from the Global scenario*

Learning from the global SSE failures is must for the SSE ecosystem in India. Addressing challenges faced by the failed SSE concepts in several countries such as improving transparency, accurate reporting and developing modern and scientific impact measurement tools etc. are essential to enhance sustainability and efficacy of the present SSE mechanism in India.

Despite the above mentioned challenges prevailing in the present SSE mechanism in India, it is too early to judge its success or failure, given its recent nascent phase of development. However, with recent developments and initiatives, SSEs in India are expected to find the potential areas to work on and improve upon to prove itself to be a valuable platform for its stakeholders in real terms, aligning their financial viability with positive social intents.

Conclusion

The SSE mechanism in India has thus been able to make a triumphant take-off despite numerous challenges and difficulties. Ongoing research and development efforts are continuously refining and tuning the SSE structure in India to facilitate its successful flight by harmonizing the requirements of both the SEs and investors, and thereby, attempting to achieve India's Sustainable Development Goals (SDGs) in the upcoming times by accelerating social developments in a modernized, structured and transformed way.

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