Unleashing the Power of Social Enterprise*

THE RIGHT HONOURABLE PAUL MARTIN, P.C., M.P.

Over the last 150 years, there has been a never-ending debate between those who espouse the free market on the one hand and socialism on the other. It is clear now that the free market has won out—because, at its core, it gives full flower to individual ambition and entrepreneurship and, because of this, it delivers best.

That being said, let there be no illusion. It is not the free market in pure form that has emerged triumphant. We do not live in a Darwinian economy, and no one with any sense would recommend that we do so.

The fact is that all developed countries depend heavily in one way or another on government for the delivery of public goods: universal primary and secondary school education, and public infrastructure, to cite only two examples.

Thus, few would deny today the importance of the state in providing the social inputs that enable the modern economy to grow. What is less well recognized, however, is the contribution made by another building block in our social and economic structure—the charitable sector, which plays an essential role in dealing with the unacceptable gaps in equality that arise from an intrinsic disadvantage or often from the fall-out of the free market.

Indeed, the importance of the charitable, the nonprofit, and the voluntary sectors appears to be Canada's secret, a hidden truth as it were. Yet taken together, as a percentage of the population, they constitute the second largest sector in the world. They are also a *huge* employer, with more than two million paid workers in Canada. This is almost as many Canadians as the *entire* manufacturing sector and two-and-a-half times the number of workers in the construction industry. They contribute almost eight per cent of Canada's GDP—this is more than the retail industry, and more than mining and oil and gas *together*.

They represent as well, in so many ways, the social conscience of the country. For all of these reasons, let there be no doubt that without the work of Canada's charities and nonprofits we would be a much poorer society morally and economically. The need they fill will continue to grow and so must our support for them.

That being said, however, I believe we have barely scratched the surface of the full potential of the charitable sector in all its permutations and combinations and what it could mean to Canada's evolving society. More specifically, I think that there is much potential to be tapped by social enterprise organizations that borrow from the objectives of traditional charities on the one hand and the management principles of the private sector on the other including, in certain cases,

* This article is adapted from a speech delivered on November 8, 2007, by the Rt. Hon. Paul Martin at the Munk Centre for International Studies at the University of Toronto.

the need to ensure growth by showing profits and the possibility of providing a financial return on investment.

"Social enterprises" are like businesses in that they trade goods and services and make money doing so. However, the latter is not their primary objective. Making money is a means to a greater end. Their major return on investment is calculated by their social or environmental return, based on a double and, in the best of cases, a triple bottom line. It is this emphasis on the deeper return that distinguishes them from the many corporations whose activities may include a social or environmental return but whose principal objective is profit.

Wherein lies the problem, you ask? It lies in the rules and regulations that govern the charitable sector. For example, simplifying its complexities somewhat, the *Tax Act* sets out rules for three categories of endeavor: first, taxpaying corporations and individuals; second, nonprofits, which do not pay taxes; and, third, conventional charities, which do not pay taxes and have the added benefit of being able to distribute charitable tax receipts to donors. These categories have played an important role in the growth of Canadian charitable giving. That being said, however, there is now a problem with the historic boundaries they set out in that they have not kept pace with the evolution of the social domain they seek to serve.

In broad terms, as we seek new ways of serving public needs, the traditional limits are a barrier to innovation. More specifically in the case of social enterprise, they do not take into account its potential to attract new forms of capital that would not otherwise be available.

Let me give you two examples of what I mean.

Not long ago, I visited Eva's Phoenix Print Shop in Toronto. It is not a big place, and, frankly, there is nothing about it that makes it stand out from any other small print shop, except for one thing. To get there, you walk through Eva's Phoenix, a centre that people as young as sixteen call home. Many of them have suffered family breakdowns and physical or sexual abuse; many have addiction problems; some are young offenders. When they land at Eva's Phoenix, they are desperate.

But once there, they are offered hope, shelter, and support. And the print shop gives even more: intensive on-the-job training in a field that needs workers. Once the young people have finished the training program, some are hired to work on site; others find jobs in other shops. Others still go on to college or university, most with a scholarship from Eva's.

The problem is that, as in so many cases, the print shop is now ready to expand its ability to help more young people but needs additional capital to do so. Under the current system, its only option is to boost its fundraising efforts. But a different model, one that permitted Eva's Print Shop to leverage its base by seeking investors to lend it money or even buy equity shares, would provide a much more sustainable way of raising the needed expansion funds and would still allow fundraised dollars to go to functions that are not part of its business model. If such a system were in place, Eva's could quickly be in a position to help many more young people and realize its ambition to replicate its model in different cities across the country.

The second example is one of a different magnitude, in a different part of the country, and with an entirely different focus from the Phoenix Print Shop. The Great Bear Rainforest of British Columbia is the largest intact temperate rainforest left on Earth. Its territory contains more than eight million hectares, that is, one and a half times the size of Nova Scotia.

Last year, a landmark 120-million-dollar deal was struck to save the rainforest. Funding came from private philanthropists and from the provincial and federal governments. But the deal does not simply fence off this magnificent piece of land. The money raised will be spent on conservation management and in developing ecologically sustainable businesses run by Aboriginal Canadians. This project has an environmental objective, a social objective, *and* a business objective. The architects of the Great Bear Rainforest project have designed a made-in Canada model of sustainability, that is worthy of—and has captured—international recognition and support.

The problem is, it is not easy to raise money for Great Bear businesses. First, they are not dissimilar to venture capital investments, yet, unlike venture capital, the investments are not likely to offer a high financial return, especially since at the same time there is the added need to develop a stable and qualified First Nation's workforce.

The original intention had been to raise a complementary private sector fund to invest in the companies that would flow from the economic development package. Unfortunately, while the overall project is a go, that aspect of the initiative, the social enterprise aspect that would create a multiplier effect in jobs, has been put on hold because the tax and other incentives needed to bridge the risk-reward gap are not there.

At this point, some of you are probably thinking, 'Wait a minute, this guy may make sense, but why is he lecturing us? He was the Minister of Finance and Prime Minister. Why didn't he act?' And the answer is—I did, but I did not go far enough.

As we cleaned up the national balance sheet, we enhanced tax support for conventional charitable activities, including the capital gains tax exemption, and began to fund the social economy, which I had been introduced to years earlier by Nancy Neamtam, one of its pioneers in Quebec. When I became Prime Minister, we set aside a further 132 million dollars for the social economy and gave a leading Parliamentary Secretary, Eleni Bakopanos, the nod to push the envelope as far as she could.

What I missed, however, was that there was still a major gap in the way government was responding to the real world evolution of the social economy, that of social enterprise in its fullest sense.

This I realized only after I left government and began seeking ways of fostering a sense of economic independence among Aboriginal Canadians. I felt and continue to believe that this can best be done by supporting and mentoring Aboriginal entrepreneurs, through investments in companies which might provide only a below market return but a high social return—a social return which equates to furthering a culture of entrepreneurship and economic self-sufficiency. Most people I approached supported the concept enthusiastically, but some had difficulty categorizing the nature of the proposal. They would say, if it is investment, why is the return below market, or if it is charity, where is the charitable tax deduction: to which the only thing I could respond was, it is a hybrid with which the policy makers have not yet caught up.

The fundamental problem is that, in Canada, there is very clear division between charitable giving including nonprofits on the one hand and private sector investment on the other, and never, it would appear, should the twain meet.

If you want to create employment for people in difficult circumstances and you want to do it solely as a charity or a nonprofit, that works; nonprofit disability workshops are an example we are all familiar with. But if you want to raise money from investors to create those jobs and in so doing provide a return on investment consisting of a high social return and a below market financial return, then, in terms of tax incentives, you are out of luck.

Clearly the rigid line of demarcation between charitable giving and social enterprise operates to the detriment of Canada's social goals, because it severely narrows the pool of capital from which social entrepreneurs can raise financing.

Why do I think this is important? It goes back to my opening statement. The market economy has demonstrated that there is more innovation and more economic growth coming from a system built on the initiatives of individual entrepreneurs than there is in any form of state capitalism.

We recognize that business entrepreneurs are those whose original ideas spark new trends, create new jobs, and create the wealth we redistribute. They are those altogether too rare individuals with the drive, energy, and passion that are needed to make the economy come alive.

Well, social entrepreneurs come from the same stock. They see problems and they dream about answers.

Like business entrepreneurs, social entrepreneurs run on vision, energy, and passion. Like business entrepreneurs, they come up with solutions that seem perfectly obvious—but only *after* they have been created.

I have tremendous respect for the public service, but there is no way in heaven, because of the structure of government, that a bureaucracy or any one else for that matter can match the obsession of someone with an original idea driven to make it happen.

What is the problem? The problem is that business entrepreneurs can tap capital markets to support their ideas but social entrepreneurs, in most cases, cannot because their return on investment is primarily a social good. If they provide a financial return, it is by definition secondary and, in all likelihood, below market. Otherwise they would be no different than conventional businesses.

So what is the answer? It is that despite the current problems in capital markets, there is a financial liquidity out there that dwarfs the potential for funding to be found in government and while most of that money seeks quite naturally the highest return possible, a not insignificant percentage will target social goods, if the right incentives are provided. What we have to do is create those incentives. What we have to do is make it possible for social entrepreneurs to tap capital markets the same way their business counterparts can do.

If more money was flowing to Eva's Phoenix Print Shop, it could grow its business. It could buy new printing equipment, which means it would employ more homeless young people, teach more of them a trade, and help them get off the streets. It would also create a pool of talent that other print shops could employ, one currently not available. Clearly, that would be of benefit to *all* of us.

The same is true of Great Bear. If they were available today, incentives to offset lower financial returns and greater risk would help fund new business opportunities right now that could generate as many as 1,400 new jobs, most of them for Aboriginal Canadians.

And the same is true also of the Aboriginal issue that opened my eyes to social enterprise in its fullest sense. Economic growth may not be a sufficient condition for the elimination of Aboriginal poverty, but it certainly is a necessary condition. To that end, if you are going to create an entrepreneurial class in an economy where one exists but barely, there is only one way to do it. That is to support the ambitions and the initiatives of those who seek to be entrepreneurs. That backing, by definition, cannot be charitable, but neither will it be the product of laissez-faire inertia. The status quo in most Aboriginal communities is proof of this. What is required is a leg up, a helping hand, all within the context of the free market.

The question is, what should that leg up be? It is here that we begin to enter the area of greatest debate. Clearly an investment that provides a lower than market return, but a return nonetheless, should receive a smaller incentive than a straight-out gift to a charity.

But because that return is below market, in many cases it still requires an incentive and the question is: What should it be? The good news is we do not have to re-invent the wheel. There is considerable international experience in the field.

For instance, unlike Canada, the U.S. now allows a foundation to make investments in social enterprises out of both its endowment funds and its grant-making activities and earn income without affecting the foundation's charitable status. These Program Related Investments—or PRIs –are permitted as long as the primary goal is a social return.

Nor is this the end of the PRI evolution in the U.S. The states of North Carolina and Vermont may be on the threshold of adopting a proposal by the Mannweiler Foundation to create social enterprise companies with PRI-eligible characteristics but open to regular investors as well as to foundations.

The U.S. has also created the New Market Tax Credit, which provides up to 15 billion dollars worth of credits for community investments over a five-year period. These credits are available through competition and could easily be adapted to the concept that I am describing.

In the UK, new legislation has created Community Interest Companies (CICs), which, incidentally, are the first new form of business created there in more than 100 years. These "kicks," as they are called, are organizations that conduct a business with the purpose of benefiting the community rather than purely for private gain.

The development of the rules around CICs is an ongoing process. Certain tax incentives are provided and consideration is being given to the kinds of further incentives required to accelerate investment. That being said, the new business model has proven very popular—it was introduced only two years ago, and already, more than 1,200 CICs have been created.

Having cited American and British examples, the fact is that we do not have to look offshore to find models that would enable us to fund Canadian sociall entrepreneurs! We can look to the tax incentives that support Canadian business entrepreneurs.

For example: labour-sponsored funds or the Canadian Film and Video Production Tax Credit Program, which offers federal incentives for Canadian productions.

Yet a third example would be flow-through shares that encourage investment in resource-based exploration.

The question I would put to you is quite simple: If we in Canada are prepared to use these kinds of incentives to enable business entrepreneurs to tap capital markets for the betterment of the economy, why would we not provide similar incentives to social entrepreneurs as they seek to tap capital markets for the betterment of society?

In conclusion then, let me say the following. The generation of leaders who came into office in Canada at the end of the Second World War was dramatically influenced and affected by the Great Depression. As a result, they created the social safety net that we now take for granted but that in their time took great imagination and vision. We must be no less innovative.

Charity has changed. Andrew Carnegie made his money but waited to give it away until his final years. Today, philanthropists are much more active and much more involved during their lifetimes. Bill Gates and Warren Buffett are far from their end, and they are giving away sums that were unheard of in the past, as are many wealthy Canadians.

And there are many more people who may not have such enormous sums at hand but who still have considerable disposable income or assets. There are also others of lesser or indeed of little wealth, but who want to make a difference and who want to do so during their lifetimes.

In short, there are many investors who would put their money into social enterprise if the vehicles and incentives were there. What we need to do is to develop the right mix of risk and reward so that social enterprise becomes attractive to mainstream capital.

Financial experts ought to be developing new cutting edge instruments to make funding available to social entrepreneurs.

Tax experts ought to be thinking about mechanisms that can support social enterprise in a meaningful way.

Legislators should encourage an environment that allows foundations to become more imaginative in support of social enterprise.

And all the rest of us need to raise the profile of the issue and to push for change.

What we need in addition to conventional charitable giving is a new way to think about philanthropy and the achievement of social goals. We are at a point in our nation's history where we can do this. All the elements are there. We have a history of progressive social policy. We have social entrepreneurs who are already running successful operations. We have a charitable and voluntary sector that is the *second largest in the world*.

We have had tremendous success in Canada in unleashing business to create wealth. We have learned that entrepreneurship is an unbeatable force. Government unleashed the power of business entrepreneurs when it provided them with the wherewithal to succeed—with needed public goods and functioning capital markets. What I would now ask is that government unleash the power of social entrepreneurs as well by providing them with the wherewithal to succeed.

We must understand that the social entrepreneur is every bit as much a part of the free market as is the business entrepreneur.

The business entrepreneur improves our quality of life by creating wealth and economic growth. The social entrepreneur improves our quality of life by confronting the inequality that is often the collateral occurrence of free markets. Both kinds of entrepreneurs are necessary. Let us give them both the chance to succeed.