SOCIAL STOCK EXCHANGE – RAISING PRIVATE CAPITAL FOR SOCIAL WELFARE

Abstract

On December 12, 2023, India witnessed its first ever listing of a Non-Profit Organization on the social stock exchange segment of the nation's two largest stock exchanges, National Stock Exchange of India Ltd. and the BSE Limited.[1] It was an unprecedented event in the history of capital market of India, which marked the beginning of development of a transparent and structured ecosystem which aims to bridge the gap between social sector finance and private capital.

CS Priya Iyer
Independent Researcher
Thane
cspriya.iyer@gmail.com

CS Aboli Pitre
Independent Researcher
Pune
aboligpitre@gmail.com

I. BACKGROUND

The idea of introduction of Social Stock Exchange ('SSE') in India was proposed by Honorable Minister of Finance and Corporate Affairs, Smt. Nirmala Sitharaman, while presenting Union Budget 2019-2020. While making the proposal she said, "*It is time to take our capital markets closer to the masses and meet various social welfare objectives related to inclusive growth and financial inclusion. I propose to initiate steps towards creating an electronic fund-raising platform – a Social Stock Exchange - under the regulatory ambit of Securities and Exchange Board of India (SEBI) for listing Social Enterprises and voluntary organizations working for the realization of a social welfare objective so that they can raise capital as equity, debt or as units like a mutual fund.*"

Consequently, in June 2020, SEBI published its recommendations and established vision of India's Social Stock Exchange. In September 2020, a Technical Group was constituted to further develop the framework for working of Social Stock Exchange, which proposed the criteria for listing of organisations, prescribed disclosure, reporting requirements and established the norms for reporting of social impact and social auditing. Based onpublic comments thereon, SEBI introduced the regulatory framework for 'Social Stock Exchange' in Indian capital markets, on July 25, 2022 by making amendments to three regulations, viz. Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2018 [SEBI (ICDR) Regulations], Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015 [SEBI (LODR) Regulations] and Securities and Exchange Board of India (Alternative Investment Funds) Regulations, 2012 [SEBI (AIF) Regulations]. Subsequently, National Stock Exchange of India Ltd. and the BSE Limited came up with a separate segment of Social Stock Exchange, namely NSE SSE and BSE SSE respectively.

II. WHO CAN GET ONBOARDED ON SOCIAL STOCK EXCHANGE?

Social Stock Exchange permits securities issued by 'Social Entities' to be onboarded, provided they establish primacy of social intent.However, corporate foundations, political or religious organizations or activities, professional or trade associations, infrastructure and housing companies,

[1] '*New Listing: India sees 1st ever Social Stock Exchange listing with debutant SGBS Unnati'*, (December 13, 2023 04:36 PM IST) , https://economictimes.indiatimes.com/markets/stocks/news/new-listing-india-sees-1st-ever-social-stock-exchange-listing-with-debutant-sgbs-unnati/articleshow/105962778.cms?from=mdr

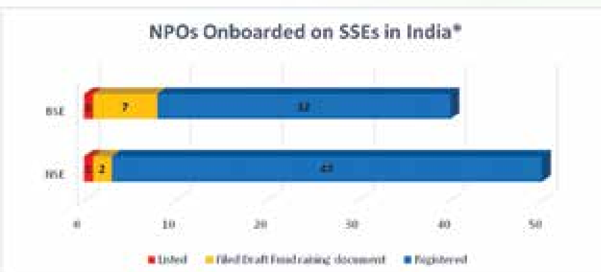
except affordable housing are not eligible to be onboarded on Social Stock Exchange. This is because SSE aims to provide access to public funds to create desired social impact and entities like corporate foundations already have a constant source of funding.

'Social Entities' can be of two types 'Not for Profit Organisations' (NPO) and 'For-Profit Organisations' (FPO).

As FPOs are essentially profit-making Companies, the set of laws applicable to them and securities which can be listed by them are same as any other Company getting listed on stock exchange, whereas for NPOs, the set of rules has been specified separately in relevant SEBI Regulations.

NPOs have an option to either simplyget 'registered' on SSE or to get registered as well as list on SSE by raising funds. Getting registered with SSE requires them to inter-alia comply with disclosure requirement of annual impact assessment report, thusensuring transparency and better governance standards, which ultimatelyresults in increased credibility of the organisation.

This article focusses on the aspects relating to onboarding of NPOs on SSE.



**As on January 25, 2024*

Source:
Websites of National Stock Exchange of India Ltd. and BSE Limited

Note – SGBS Unnati Foundation got listed on both the Exchanges and raised the sum of Rs. 1.80 Crores from issue of ZCZP for training of up to 10,000 graduating youth from government colleges to assist in employment placement.

III. SECURITIES WHICH CAN BE LISTED ON SSE

NPOs can raise funds through issuance of 'Zero Coupon Zero Principle' Instruments (ZCZP) to its investors. ZCZPs have been notified by SEBI as *'securities'* under Securities Contract Regulations Act, 1956. As the name suggests, these instruments neither carry any interest nor isthe principle amount returned to investorsonmaturity, thus making it another form of donation.

SEBI (ICDR) Regulations further allows raising of funds through Mutual Fund Schemes for social welfare. Currently, HDFC Asset Management Co. Ltd has launched HDFC Charity Fund for Cancer Cure which has social impact as one of its objects *i.e.,* it invests money in underlying instruments and generates dividends, which are meant for charity. It has a tie-up with the Indian Cancer Society. The aim is to donate the dividends declared to the NGO; however, at the end of the scheme's tenure, the investor gets the capital back. Going forward, with the introduction of SSE, we can look forward to more of such mutual funds being floated, which are designed for achieving social objectives and listing on the SSE.

SEBI has not specified any additional means of fundraising as on date. However, theTechnical Group constituted by SEBI has suggested various instruments such as equity shares for a Section 8 company, Development Impact Bonds (DIBs), Social Impact Funds (SIFs) etc. as eligiblemodes of fundraising by SEs.Till now, in India, the NPOs have raised or propose to raise funds through ZCZPs. The methods of fund raising through other instruments like mutual funds, social impact funds, development impact bonds are expected to shape up in near future.

IV. WHO CAN INVEST?

Initially, at the time of introduction, SSE was accessible to institutional investors and non-institutional investors *i.e.,* only institutional investors and high net worth individuals could invest in an NPO through SSE.To promote the platform and to allow more people to participate in this newly developed ecosystem, SEBI has now amended the regulations to allow retail investors also invest in securities, thus opening the avenue for retail or general public participationand bringing the masses closer to realising social objectives. This was done by bringing the minimum subscription amount by the investors in an issue from Rs. 2 lakhs to Rs. 10 thousand.

V. LEGAL PROVISIONS GOVERNING SSEs IN INDIA

NPOs are either incorporated as Section 25/8 Company under the Companies Act 1956/2013 respectively or a public charitable trust or a society under Indian Trusts Act, 1882, Public Trusts Acts of various states in India, The Societies Registration Act, 1860. Accordingly, they are required to comply with these applicable regulations also including Income Tax Act, 1961, Foreign Contribution (Regulation) Act, 2010, etc.

Besides these applicable legislations, onboarding or listing of ZCZPs on SSE requires the social entities to comply with various securities laws such as-

a. Chapter X-A of SEBI ICDR Regulations, which governs the onboarding of and listing of securities issued by social entities on SSE platform. It provides the eligibility criteria to be met by the Not-for-Profit Organization or a For Profit Social Enterprise, to be identified as a social enterprise.

b. Chapter IX-A of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 201, which lays down the provisions to be complied by NPOs on an on-going basis once they have been registered / listed on SSE.

c. SEBI Circular on 'Framework on Social Stock Exchange'dated September 19, 2022, amended vide SEBI Circular dated December 28, 2023

   The aforesaid Circulars provide some additional minimum requirement criteria to be met by NPO for registration with SSE. In addition, the circular also lays down the process of fund raising by social enterprises, provides for minimum initial disclosure requirement for NPO raising funds through the issuance of ZCZP as well as explains required annual disclosures by NPOs on SSE which have either raised funds through SSE or are registered with SSE.

d. Normsfor listing Social Stock Exchanges-

   SEBI (ICDR) Regulationshas delegated the responsibility to specify the listing norms of ZCZPs in respect of issue procedure including on agreements with depositories, banks, etc., ASBA related matters, duration for public issuance, allocation methodology, etc. to the SSEs. Hence, both the SSEs in India, have issued the listing norms which the social enterprises must abide by while listing the securities on respective SSE platforms.

In addition to the above, both the Exchanges have published a set of 'Frequently Asked Questions (FAQs)' on SSE on their respective websites, which can also be referred to by the NPOs willing to onboard/ list on SSE for better clarity.

VI. SELECT CLARIFICATIONS ON LEGAL PROVISIONS FOR NPOs

Few of the questions in the minds of the NPOs/ professionals with respect to applicability of certain legal provisions are that whether the NPOs are required to appoint qualified company secretaries as compliance officers on whole-time basis, do the NPOs need to comply with stringent Corporate Governance provisions specified under SEBI LODR Regulations such as appointment of independent directors, formation of statutory committees etc.

To answer the above questions, Regulation 3 (1) of SEBI (LODR) Regulations needs to be reviewed which reads as follows -

Unless otherwise provided, these regulations shall apply to a listed entity which has listed any of the following designated securities on recognised stock exchange(s):

a. specified securities listed on main board or SME Exchange or Innovators Growth Platform;
b. non-convertible securities;
c. Indian depository receipts;
d. securitised debt instruments;
da. security receipts;
e. units issued by mutual funds;
f. any other securities as may be specified by the Board.

While the definition of 'listed entity' under SEBI LODR Regulations includes an entity that has listed any of its designated securities, Regulation 3(1) clarifies that the provisions of the SEBI LODR Regulations, with appropriate exceptions, apply only to a listed entity which has listed the designated securities mentioned at (a) to (f) of Regulation 3(1). It may be noted that ZCZP has not specifically been included in Regulation 3(1). Therefore, unless explicitly mentioned, only provisions of Chapter IX-A of the SEBI LODR Regulations are applicable in the case of listing of ZCZPs on SSE by NPOs. Accordingly, as on date, no other provisions of SEBI LODR Regulations other than Chapter IXA are applicable to NPOs listed on SSE.

For NPOs incorporated under Section 25/8 of the Companies Act 1956/2013, the applicable provisions of the Companies Act also needs to be reviewed, which mandated appointment of whole-time company secretaries for companies beyond the prescribed threshold. However, it is pertinent to note that the Ministry of Corporate Affairs ('MCA') vide its notification dated June 5, 2015, exempted Section 8 Companies from complying with certain provisions of the Companies Act, 2013, subject to the condition that the Company will ensure protection of shareholder's interests. As per the said notification, definition of Company Secretary in section 2(24) of the Act is not applicable for Section 8 Companies. Therefore, Section 8 Companies are not required to appoint a whole-time company secretary.

The entities getting onboarded on SSE are social sector entities which have limited resources available to bear the administrative and compliance costs. Also, it is imperative to note that SEBI (LODR) Regulations which are applicable to listed entities are aimed at regulating the profit-making companies, hence making all the provisions of these regulations applicable to social enterprises is not pragmatic. The other compliance requirements of these entities are limited as compared to listed companies and hence, requiring them to appoint a full-time professional to look only after compliance part of the organization may be excessive and unnecessary cost burden on the organisations. Keeping this in mind, the regulators have framed the regulations.

VII. BENEFITS OF SSE TO VARIOUS STAKEHOLDERS

The vital role that SSEs play is to act as a facilitator of social finance and providing common platform for social enterprises, donors and investors. It attempts to match demand and supply of funds for social causes effectively. Simultaneously, it attempts to promise transparency to the investors and donors about the actual social impact caused by the entities.

On the demand side, access to funds remains aconstant challenge for Social Enterprises all over the world. India is home to more than 3 million non-profit organisations who are relentlessly working for betterment of lives of millions of Indians. They contribute efficiently towards nation's economical as well as social empowerment. They represent the new form of enterprises in India where an entrepreneur mainly acts as an agent of positive social impact. In India, around 57% of organisations have claimed that not having easy access to capital as the biggest barrier to growth. Another survey has found that around 50% of non-profits had been unable to access the CSR funding in preceding 3 years. [2]

The Social Stock Exchanges help in addressing these challenges through providing 'CVT' to these entities.

Credibility- Getting registered/listed on SSE as well as getting incubation support from SSE lends credibility to the entities as the Exchange performs due diligence on them before getting them onboarded. It gains confidence of investors and donors.

Visibility- The NPOs are given the choice to merely get registered with SSE and to not raise any funds through listing of securities. One of the major rationales behind the same is to provide visibility to organization's work through the SSE platform. Getting onboarded on SSE through registration helps the NPOs to make their presence and area of work visible to potential donors as well as investors.

Transparency- Social Enterprises in India lack transparency in their operations, compared to other business organisations. The guidelines for NGO funding do not provide for disclosure as to how NGO beneficiary is selected, whether they utilize funds because in most of the cases, there is no fund utilization certificate which is required to be submitted under General Finance Rules, 2017.

The Delhi High Court in 2013 while hearing a petition filed by *Children's Homes Chatravas and Arya orphanage* challenging government's refusal to grant them license under the Women and Children's Institutions (Licensing) Act, 1956 observed that *"Most private run so called philanthropic organizations do not understand their social responsibilities. 99% of the existing NGOs are fraud and simply moneymaking devices. Only one out of every hundred NGOs serves the purpose they are set up for."*[3] Unless the donor has specifically demanded for the same, there is no mechanism currently in place which would make hold these organisations accountable for their actions and results.

This lack of transparency not only acts as a barrier to raise funds and get investments from big donors and corporations, but it is also one of the major challenges faced by investors and donors who are willing to invest in Social Enterprises. 48% of the impact investors have stated that sophisticated impact assessment is one of the most significant challenges faced by them. Indian impact investors reflect the same. 59% of the donors stated that they would be more encouraged to donate if the process was made more convenient. 63% of them noted that lack of reliable information about where and how to give in order to achieve maximum impact through donations is a constant barrier.[4]

SSE aims to enhance the standards of accountability and transparency for Social Enterprises. Every social entity which has raised funds through issue of ZCZP on SSE is required to comply with various continuous and event-based disclosure requirements. Even for the entities which have merely registered themselves on the platform, must comply with requirement of disclosure of annual impact report at the end of each financial year.

It is important to note that World's first ever SSE was instituted in 2003 in Brazil. Since then, many countries including United Kingdom, South Africa, Singapore, Portugal, Canada, and Jamaica have instituted SSEs. Out of the seven SSEs set up across the globe in past, only three of them, *i.e.,* Canada, Singapore and Jamaica are still active. One of the crucial factors for failure of other exchanges was lack of robust business model to make them self-sustainable entities.[5] To avoid the same fate, in India, SSE is housed as an additional platform of existing recognised stock exchanges having nationwide terminals, viz. National Stock Exchange of India Limited and BSE Limited. This allows the platform to grow with the help

[2] Anustree Parekh et al, What do nonprofits think of CSR?, INDIA DEVELOPMENT REVIEW (March 11, 2021), https:// idronline.org/what-do-nonprofits-think-of-csr

[3] Harish V Nair, 99% NGOs are Fraud, money making devices:HC, HINDUSTAN TIMES (March 06, 2013, 1:21 AM), https://www.hindustantimes.com/delhi/99-ngos-are-fraud-money-making-devices-hc/story-2AMyh5VMGA0edUtvtRnAMP.html

[4] Aarati Mohan et al, EVERYDAY GIVING IN INDIA REPORT, 23 (Sattva Consulting 2019), available at: https://www.sattva.co.in/wp-content/uploads/2019/04/Sattva-Everyday-Giving-in-India-Report_Key-Findings.pdf

[5] Amiya Walia, Anushree Parekh,Shivina Jagtiani, *Social Stock Exchange:What India Can Learn From Global Examples*, (March 25,2021),available athttps://idronline.org/social-stock-exchange-what-india-can-learn-from-global-examples/

of parent exchanges' active pool of investors, required infrastructure and good reputation, without worrying about the revenue model of the platform.

Tofurther incentivise investment in SSE, it would also be helpful if the regulators consider appropriate amendments in the Income Tax Act to provide appropriate tax exemptions to the investors/donors in SSE.Donors to NPOs in India have traditionally received tax exemptions under Section 80G of the Income Tax Act. The finance minister, in her February 2020 union budget speech, hinted at removing the provision for exemption altogether. The working group has noted this development and recommended that Section 80G not only be retained but that the extent of exemptions be increased. With the Union Budget for this year to be announced soon, a positive development in this regard is expected. Further, to mobilise more funds through SSEs, there is also a great need for enabling corporates to participate in the SSE as Corporate Social Responsibility (CSR) spenders.To enable the same, the Ministry of Corporate Affairs may be required to tweak the CSR provisions of the Companies Act to include investment in ZCZP as an eligible investment towards CSR provisions.

VIII. SSE- A NEW AVENUE FOR CMAs AND SUCH OTHER PROFESSIONALS

Introduction of Social Stock Exchange in India has presented an avenue in Social Sector to professionals such as CMA, CA and CS by getting themselves registered as Social Impact Assessors.

As per the requirements of SEBI Regulations governing SSE, every social enterprise which is registered on SSE or whose securities are listed on SSE must submit an annual impact report to the SSE which must be assessed by a Social Impact Assessment Firmemploying Social Impact Assessor(s).

The Social Impact Assessmentallows stakeholders to assess the impact made by the Social Enterprise through itsintervention, program or projects and identify the gap between desired object andactual impact made by the Social Enterprise during the reporting period. It also aims to aid regulators for the effective implementation of applicable laws, rules and regulation and also to the general public to take informative decision while making any investment in securities of Social Enterprise.[6]

ICMAI has formed'ICMAI Social Auditors Organisation'for the empanelment, capacity building and regulating the functions of the members who qualify and get registered as Social Auditors under the SEBI-notified framework for social stock exchanges. ICMAI has also published Social Audit Standards for their members to standardize the process of assessment. The sister institutes *viz,* ICAI and ICSI have also formed similar institutions and notified social audit standards.

In addition to the above, CMAs and such other professionals can also inter-alia assist the NPOs in the below manner, thus playing a critical role in the achieving the social objectives –

a. Provide consultation to social enterprises willing to get themselves registered or listed on SSE.
b. Assist in drafting fund-raising document and such other documentation.
c. Provide various third-party confirmations/ certifications about various aspects of NPOs required by the SSEs at the time of registration/listing of NPOs.
d. Assist the NPOs in drafting policy for determination of materiality.
e. Advise/Assist the NPOs in ensuring compliances with requirements of law on on-going basis post registration / listing including preparation of Statement of utilisation of funds.

CONCLUSION

Over the past two decades, the concept of 'business financing' has evolved drastically. The businesses are no longer evaluated solely based on their profitability; their contributions towards social and environmental development also play a key role in determining their desirability for investors. On the other hand, Social Enterprises which mainly focus on the development of society struggle to raise finance for their projects. India is home to more than 3 million Not for Profit Organisations1 (NPO), *i.e.*, 1 NPO behind every 500 citizens approximately. India is estimated to need 565 billion dollars in investment to meet UN Sustainable Development Goals by 2032.[7]Despite that it records the lowest public education expenditure and health expenditure figures as percentage of Gross Domestic Product.[8] This gap of expenditure for development can be filled to considerable extent by India's social sector if a mechanism is set in place to facilitate the raising of finance by these enterprises. Introduction of SSEs seems to be a promising step to address the issue of raising finance by these Social Enterprises for social development and financial inclusion. Additionally, if the necessary regulatory impetus like tax exemptions, CSR inclusions etc. are provided, SSE has the potential to be not just a step but a leap towards a structured ecosystem for raising private capital for social welfare. MA

[6] Institute of Company Secretary of India, ICSI SOCIAL AUDIT STANDARDS, available at https://www.icsi.edu/media/webmodules/ICSI_Social_Audit_Standards.pdf

[7] STANDARD CHARTERED, OPPORTUNITY 2030 THE STANDARD CHARTERED SDG INVESTMENT MAP at 2-5(2020) https://av.sc.com/corp-en/content/docs/Standard-Chartered-Opportunity-2030.pdf

[8] KPMG, ANALYSING THE CONCEPT OF SOCIAL STOCK EXCHANGE' ININDIA(2020)https://home.kpmg/in/en/home/insights/2020/07/analysing-the-concept-of-socialstock-exchange-in-india.html