Can social finance improve the outcomes of employment and training programs?

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with research assistance from Ryan Nichols

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Introduction

Paper purpose

The purpose of this paper is to map out the 'social finance landscape' as it relates to employment and training programs and assess the extent to which social finance approaches can play a role in improving outcomes in this important policy domain.

Recently, the concept of social finance has captured the attention of Canadian and international jurisdictions alike. This concept includes a wide variety of approaches ranging from *Social Impact Bonds* that mobilize private capital to invest in preventive interventions to *social investment funds* that support enterprises with double or triple bottom line business models. What these approaches have in common is that they aim to *mobilize private capital to attract new investments that deliver social benefits, and in most cases, at least a nominal financial return*.

According to the Canadian Task Force on Social Finance (2010), the promise of these approaches is that they offer an unprecedented opportunity for non-profits to open up new sources of financing at a time when many are trapped in a cycle of short-term funding that diverts attention from their mission. Proponents of social finance point to the role private capital can play in stimulating innovation and improving outcomes for individuals and families who depend on services. Despite this growing interest, there has been little, if any, systematic analysis of the extent to which social finance approaches have delivered on this promise in a particular policy domain. This is in part because these approaches are relatively new and it takes time to understand how a particular approach or set of approaches adds value. It is also in part because social finance approaches tend to be studied from a broad lens of social innovation in general rather than from an outcomes lens in any particular policy area.

This paper aims to contribute to our knowledge base by examining the potential of social finance in the domain of employment and training programs. Together the federal government and Canadian provinces and territories currently spend over $3 billion in this area, yet programs are often criticized as not meeting the needs of job seekers or employers (Mowat Centre, 2012). To what extent do social finance approaches hold promise to improve outcomes? And importantly, are there risks associated with increased reliance on these approaches? Limited by a lack of rigorous evidence in this area, our analysis is necessarily preliminary. We rely largely on the results of an environmental scan of selected jurisdictions and expert consultations in the province of Manitoba. Manitoba was selected because the province is currently in the midst of transforming its employment and training system and expressed a strong interest in engaging in discussions about the potential role of social finance in this transformation.[1]

1 While we were only able to consult with one province within the constraints of this project, further research should explore other Canadian jurisdictions where social finance approaches are more well-established such as British Columbia and Quebec.

What is social finance?

According to the MaRS Centre for Social Impact, social finance is a way of managing/acquiring capital that connects investors and entrepreneurs interested in *both* making money and promoting positive social/environmental impact. For investors, social finance is an approach to managing money that aims to deliver social and/or environmental benefits, and in most cases, a financial return. For entrepreneurs, social finance lies somewhere between a charitable donation and a loan, and is used to further a social mission to create impact at a scale that complements traditional philanthropic support or government contributions (MaRS Centre for Impact Investing, 2010).

The paper proceeds in four sections:

- First, we begin by briefly describing the current policy context related to employment and training programs and highlighting the role that social finance could potentially play in helping governments achieve their policy objectives. In this section we draw attention to the long standing challenge of how to make the shift from a system that is fundamentally 'supply-side' driven to one that is more responsive to labour market demands and thus more effective in matching the target population to sustainable employment.
- Second, we set the stage for a discussion of social finance models by providing a high level overview of the Canadian social finance marketplace. In this section, we draw on the conceptual framework developed by the MaRS Centre for Impact Investing to highlight the key actors and the drivers underlying this emerging marketplace. For a more theoretical discussion of social finance concepts and definitions see Kerlin (2006).
- Third, we map out the 'social finance landscape' as it relates to employment and training programs. We draw on the Canadian and international context to provide examples of various social finance approaches in action. We emphasize the *needs of actors who use social finance* (rather than social finance instruments themselves) because the major objective of this paper is to explore the extent to which social finance approaches can be harnessed to achieve policy objectives. To achieve this objective we need a better understanding of what actors are using social finance and what problems it is solving.
- Fourth, given the findings of our scan as well as consultations with policymakers and service delivery providers in one Canadian jurisdiction (Manitoba), we analyze the extent to which social finance approaches may play a role in helping governments meet their policy objectives in the domain of employment and training programs.

The major finding of our paper is that while various social finance approaches have different strengths and limitations, taken together they have the potential to improve the effectiveness of employment and training programs by fostering a more demand-led system that meaningfully engages employers. By definition, social finance approaches engage private capital and use market discipline to align needs and incentives so that all parties benefit (see Section 2). From this standpoint, the real promise of social finance may be in its ability to align incentives in a system where incentives are often misaligned so that employers, providers, governments and jobs seekers all benefit. Indeed we identify five distinct models that are already being used in the employment and training domain to align the needs of these four actors to drive innovation and improve employment outcomes.

However, our analysis also suggests that these approaches are not without their own challenges. Social finance approaches are far from a panacea and indeed they raise new risks. Our analysis suggests three important caveats:

- First, social finance approaches should not be seen as a substitute for government funding but rather as a complement. For example, while social finance approaches like social impact bonds may rely on private investors to finance the delivery of a given social program, if the program meets its pre-agreed upon targets, governments must not only pay the full cost of the intervention but also a financial return to the private investors who provided the upfront capital. In terms of other approaches such as social enterprises, as we show in section four, even the largest, most successful social enterprises still tend to rely on government support. Thus, while social finance approaches may open up new opportunities they do not enable government retreat from a policy domain.
- Second, social finance approaches should not be seen as synonymous with privatization of social services. While definitions differ across countries and context, it is generally accepted that social enterprises must have a social mission at the core of their operations. Indeed, our analysis indicates that most social enterprises are non-profit organizations. Those that are for-profit organizations usually seek means to ensure their *directors consider the interests of all stakeholders, not just shareholders, when making decisions*. This protection is essential to ensuring that financial goals do not overtake social goals. Thus, social enterprises should be distinguished from more traditional for-profit organizations that compete for government contracts to deliver social services but do not have a structure that allows them to have a social mission at the core of their operations.
- Third, from a more tactical standpoint, social finance approaches are not simple to mount. The legal complexities and time-intensive requirements associated with developing a social impact bond are now well-documented (Aiken, 2007; Loxley, 2013). The challenges associated with social enterprises are of a different nature but no less significant in kind. The process of building a social enterprise is similar to starting any kind of enterprise and having a social mission is no guarantee of success. Indeed a dual bottom line may only make the challenges more significant. Like any entrepreneurial approach, the learning curve is steep and the risk of failure is high.

With these caveats in mind, it is unlikely that social finance approaches would play a predominant role in the near or medium term in the social services landscape of any policy domain. But while social finance approaches are far from a panacea, their focus on mobilizing private capital and aligning incentives suggests the potential for them to play a promising role in creating more effective employment and training programs.

Scope and methodology

To better understand the social finance marketplace, we began with a review of the social finance literature. Next we conducted an environmental scan to identify organizations that use social finance to foster innovation and improve returns for employment and training programs. We focused on four jurisdictions: Canada, the United States, the United Kingdom, and Australia. We used various social enterprise directories to identify organizations that met two criteria: first, the organization delivers employment related training programs; second, the organization uses some form of social finance.

We analyzed this list of organizations to determine whether we could identify distinct models or approaches to using alternative financing to deliver employment-related training programs. Finding that distinct models exist, we present a scheme that first differentiates models according to type of entity and then further differentiates them by the type of business model and financing scheme. To provide a more comprehensive scan of the Canadian context, we used this framework to determine the extent to which different models are currently in use in Canada.

Next we analyzed what is known about the effectiveness of each of the models identified in our scan. Finally, we conducted a more detailed examination of the potential of social finance in one Canadian jurisdiction – Manitoba. Our consultations included two roundtables, the first with senior government officials and the second with executive directors of both employment and training organizations. In addition we conducted one-on-one follow up interviews with selected government officials, service providers, and social finance experts. See Appendix A for a list of all consultation participants.

1. Employment and training policy context

1.1 Context and challenges

Understanding the potential of social finance in the domain of employment and training programs requires a basic understanding of the policy context in this area. This section presents a brief overview of how employment and training policy is framed in Canada and highlights some of the pervasive and longstanding challenges in this domain.

Training policy in Canada is framed and financed through inter-governmental relations and has undergone considerable reform in the past fifteen years (Wood and Klassen, 2011). Labour Market Development Agreements (LMDAs) and Labour Market Agreements (LMAs) are the key intergovernmental agreements that set out responsibility in this domain. LMDAs set out responsibility for Employment Insurance (EI) clients including a set of programs known as the Employment Benefits and Support Measures (EBSMs). In the mid-1990s, the federal government began a process of negotiating the LMDAs to enable provinces and territories to better integrate EBSMs with their own labour market investments. As the negotiations of the LMDAs progressed, a major issue emerged around how to expand access to training for individuals who were not eligible for Employment Insurance. In 2007, the federal government proposed to address this problem by investing an additional $500 million annually through a new set of agreements called the *Labour Market Agreements.* Today, LMAs continue to provide funding for low skilled individuals who need assistance with skills development but are not covered by EI. There are also a number of new agreements that target specific vulnerable groups such as Aboriginals and persons with disabilities.

When they were launched, the new agreements were billed as a 'new training architecture' but in practice, funds have been used in a rather ad hoc way. As Wood and Klassen (2011) point out, there is concern over the extent to which vulnerable groups actually benefit from these new agreements. Moreover, service delivery integration – part of the original impetus for the negotiation – has been slow. Several provinces are only just beginning the process now.

Even in provinces that began this process in the previous decade, progress has been uneven. For example, Myers et al. (2011) identify several sticky challenges, perhaps the most fundamental of which is how to better engage local employers and ensure that job seekers are being prepared for jobs that are in-demand in the local labour market. As they note in their report, there is widespread consensus among expert practitioners that employers should be more deeply engaged and that this consensus is consistent with the international literature. Indeed, several reports have recently concluded that the most effective employment and training programs not only deliver services to job seekers but also develop connections to the employers who ultimately hire them (Leitch, 2006; Palameta et al., 2011; Meadows, 2006; Freeman & Taylor, 2002). For example, in an authoritative review of Britain's skills needs, Leitch (2006) concludes that conventional approaches to delivering skills have been too 'supply driven' and that improving outcomes would require a demand-led system to better meet the needs of individuals and employers. According to this literature a demand-led orientation would include working with employers to identify jobs, identify desired skills, help design training curricula, offer on-the-job training and internships to trainees, and ultimately offer jobs to individuals who complete employment and training programs (Palameta et al., 2011; Social Capital Partners, 2012).

While the Myers et al. (2011) report indicated that there was considerable agreement on the degree of challenges involved in creating a more demand-focused system, there were also some counter-examples of promising models that had successfully engaged employers. According to the report, when asked what it would take to replicate these program models on a larger scale, some experts suggested that new, more flexible funding approaches that both removed barriers and provided incentives for collaboration and innovation would be required. There was general agreement that existing funding arrangements often acted as constraints rather than enablers of innovation.

1.2 Potential role of social finance approaches

To what extent can social finance play a role in shifting employment and training programs to a more demand-focused approach and improving outcomes for both job seekers and employers? While we did not identify any studies that addressed this question directly, our review of the literature identified several potential benefits that social finance approaches may bring to government in general.

The first and foremost benefit cited in the literature is improved outcomes driven by stronger incentives to innovate. Despite substantial investments, there is a general consensus that governments have not been particularly successful in solving deeply rooted social problems. This is in part due to a government tendency to fund remedial rather than preventive interventions, and in part due to a desire to avoid the risk associated with innovative ideas (Warner, 2012; Social Finance Inc., 2012). At best, governments are likely to fund incremental innovations, thus reducing the uncertainty associated with any innovation (Antadze & Westley, 2010). Proponents of social finance assert that social finance approaches can stimulate innovation by bringing new actors to the table and attracting new investments that harness the discipline of the market and align incentives by paying for outcomes rather than activities and outputs. This is in contrast to the traditional approach whereby governments hold providers accountable for how programs are delivered instead of whether they produce results. Thus, instead of providers being constrained to pursue only activities that are allowable under often rigid program parameters that may be driven by longstanding funding silos, social finance approaches may provide both the motivation and the means to enable providers to design innovative interventions that better respond to the needs of their target populations. In the domain of employment and training programs, this is an area of potential opportunity given that in many Canadian jurisdictions providers are typically paid for activities and outputs and in many cases long-term outcome data is not even systematically collected (Palameta, Myers, & Conte, 2013).

Of course the risk or potential downside associated with an increased emphasis on outcomes is well-documented. Although we are not aware of any rigorous evaluations of the effectiveness of ‘paying for success’ in the context of programs with a social finance component, there are numerous studies on the effectiveness of ‘paying for success’ in the context of existing government funding streams. As Palameta, Myers, and Conte (2013) conclude, pay for performance systems are often associated with increased gaming behaviour and thus need to include a commitment to continuous improvement to correct for unintended consequences and ensure that intended benefits are realized. Thus, given the well-documented challenges associated with pay for performance models used with *existing* government funding streams, whether the 'pay for success' elements of social finance approaches are ultimately associated with improved outcomes is a question that can only be answered as these approaches are tried and rigorously evaluated.

A second purported benefit is that social finance approaches enable governments to share the risks associated with innovation with private actors. This is important because while governments may recognize the benefits of innovative programs, fiscal constraints may prevent investment in innovation and prevention since funds are usually already committed to high-cost remediation programs. If the innovation fails, governments risk having to pay for both it and existing programs (Social Finance Inc., 2012). Social finance approaches mitigate this risk because the private market covers part or in some cases all of the costs associated with the innovation. While risk sharing is an attractive feature for governments, it is worth noting that it is unclear to what extent investors and service providers will be willing and able to embrace this risk. Risk-sharing is a feature of social finance approaches that has raised particular concerns in Canada (for example, see Loxley, 2013).

Finally, social finance approaches may help governments improve outcomes by aligning interests so that capital is channeled toward the most effective interventions. This alignment arises because social finance creates a market for social outcomes with private investment, and the incentives within this market encourage various stakeholders to seek to achieve common objectives (Jagelewski, 2011). The potential of social finance to create incentives for increased alignment may be the most significant benefit that social finance approaches can bring. As we discuss above, while numerous reports have identified employment and training systems as being overly-supply focused, in other words focused on 'fixing job seekers,' it has proven difficult for jurisdictions to reform their systems to better align with the needs of employers (Social Capital Partners, 2012). Indeed, as we discuss in the final section of this paper, this is the potential benefit that most strongly piqued the interest of both government officials and service providers during the Manitoba Roundtables.

Thus, from a government standpoint, the promise of social finance may be its potential to align interests in systems where interests are often misaligned and where resources are sometimes channeled to activities that do not drive desired outcomes. In the specific context of employment, market discipline may bring the additional benefit of infusing the system with incentives to engage employers and shift towards a demand focus. By tying incentives to the achievement of employment outcomes, social finance may facilitate a shift in focus among service delivery agencies toward meeting employers' needs – the gateway to improved outcomes for job seekers.

In the countries included in our environmental scan (Canada, United States, United Kingdom, and Australia), there are a wide range of actors using social finance approaches in the context of employment and training programs. The next section provides an overview of what this emerging new landscape looks like in general and more specifically the context of employment and training programs.

2. Understanding the social finance landscape

2.1 The Canadian social finance marketplace

Like any financial marketplace, the field of social finance is made up of demand-side actors who need social finance and supply-side actors who exist to meet this need. Intermediaries exist to connect these two types of actors. Figure 1 provides a high-level overview of the Canadian social finance marketplace as mapped out by the MaRS Centre for Impact Investing.

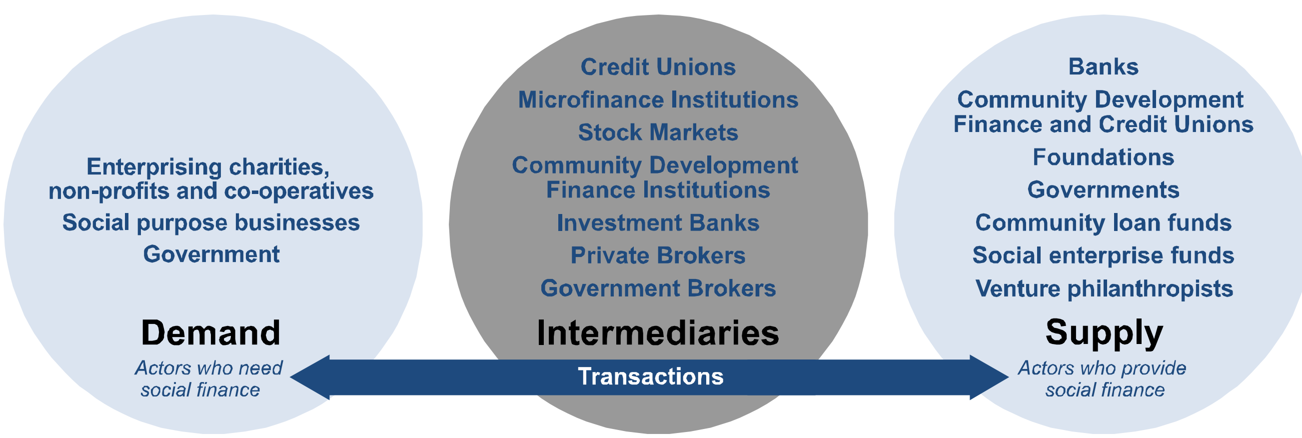
As Figure 1 illustrates, the demand side is comprised of a wide range of actors who 'need' social finance instruments. As a recent progress report issued by the Canadian Social Finance Task Force (2011) concludes, in Canada the number of actors on the demand side is increasing. A growing number of enterprising charities and non-profits, social purpose businesses – and more recently governments – are using social finance approaches and adopting innovative business models to mobilize private capital and increase their impact.

The supply side of the marketplace is compromised of actors who provide social finance. Responding to increased demand, an increasing number of socially responsible private actors are finding new ways to channel capital in pursuit of social impact in addition to growing their bottom line (Canadian Task Force on Social Finance, 2011; Harji & Jackson, 2012).

In addition, there are a growing number of intermediaries that connect social actors who need additional capital with private actors who can supply capital. Note that governments can be actors on both the supply and demand side of the social finance marketplace.

Our environmental scan suggests that the landscape is roughly similar across the Anglo-nations of the UK, US, Australia and Canada in the sense of the range of demand and supply side actors. However, there are important differences. First, the UK and the US are much further ahead in creating the policy and legal environment to encourage new actors on the demand side (Bridge & Corriveau, 2009; Bridge, 2010; Markey et al., 2011). Second, the UK and the US have a wider range of enablers, funders, and intermediaries in the social finance marketplace (Causeway, 2009).

Figure 1 Overview of the social finance marketplace



Adapted from MaRS Centre for Impact Investing, 2010.

Western European approaches

Although outside the scope of this paper, it is worth noting that the institutional environments for social finance and social enterprise differ widely across regions. As Kerlin (2006) points out, social enterprises in Europe tend to be viewed as belonging to the 'social economy' where social benefit is the main driving force. This is also the case in Quebec. In contrast, in the US, the UK, Australia, and most parts of Canada, the concept of a social economy does not tend to be used and non-profit social enterprises are often discussed as operating in the market economy.[2] (For a fuller discussion of these differences see Kerlin, 2006, 2007; Nyssens et al., 2012.)

Also in Western European countries the social enterprise landscape is heavily focused on a specific type of social enterprise – work integration social enterprises (WISEs) – that employ individuals from the target populations they serve in the enterprise. This focus on work integration has often enabled more stable access to public subsidies. However, as Nyssens and Kerlin (2009) point out, subsidies are usually only temporary and granted to start the initiative and to make up for the productivity gaps of individuals from the target populations that are employed in the enterprises. In contrast, in the US, social enterprises have access to larger amounts of capital and innovative financial products (Mendell & Nogales, 2009). The US has also introduced legislation that requires financial institutions to invest in underserved markets. This legislation, in part, provided the impetus for Goldman Sachs to investment in the US's first social impact bond that is currently underway in New York City (see below).

What drives the social finance marketplace?

Economic, social, environmental and demographic challenges continue to exert fiscal pressure on governments, institutions and communities (Task Force on Social Finance, 2011). To increase their resiliency in the wake of such challenges, a growing number of non-profits are seeking to diversify their revenue sources, generate increased revenues and maximize their social impact through operating as social enterprises (Canadian Task Force on Social Finance, 2010; Hebb, 2012). According to Emerson et al. (2007), social enterprises are creating new and exciting solutions to society's problems, but despite their emerging successes, most face a common problem: an inability to secure growth capital. Specifically, there is a lack of risk-taking capital. The result is that even proven social enterprises are unable to access the capital required to scale up their enterprise and increase their social impact. However, there is also a growing number of investors looking for opportunities to affect social impact in ways that go beyond traditional grants and into the realm of debt and equity (Emerson et al., 2007), often referred to in the literature as 'impact investing.' It is these two forces – non-profits that wish to scale up their enterprises to achieve greater social impact but have limited access to traditional financing, and philanthropically minded investors who are willing to consider new models of risk and return – that drive the social finance marketplace.

Indeed, an increasing number of social entrepreneurs and investors are realizing that social enterprises can generate financial returns that may attract the right investors (Bugg-Levin, Kogut, & Kulatilaka, 2012). Connected to this is the realization that instead of delivering a blended return for all investors

[2] We are grateful to internal reviewers who brought these distinctions to our attention.

that is attractive to only a few, enterprises can offer different risks and returns to different types of investors (Bugg-Levin, Kogut, & Kulatilaka, 2012). For example, by raising a portion of capital from grants, enterprising non-profits will be more attractive to debt investors who seek higher, more predictable returns.

Who supplies social finance?

From a global standpoint, there has been a marked increase in the past five years in the number of players on the supply side of the market. As Harji and Jackson (2012) put it, "the quantum of capital has risen steadily, key intermediaries have emerged, and there has been significant growth in innovative products and platforms for investors" (2012; xii). In Canada, the Canadian Task Force on Social Finance reports that, "a suite of new impact investment funds, products and services are being launched into the marketplace, offering a spectrum of opportunities for engaged investors," a movement being led largely by the foundation sector (2011). In 2011 alone, foundations contributed $50.25 million in new investments in Canada (Task Force on Social Finance, 2011). There are also a growing number of impact investing funds (for example, the Community Forward Fund in Ontario, and Vancity Resilient Capital Program in BC). The Task Force is calling on the Canadian and provincial governments to establish their own investment funds, with the purpose of supporting existing regional funds to reach scale, and to facilitate the creation of new funds (Task Force on Social Finance, 2011). Despite this growth led by the foundation sector, is it important to note that in Canada, governments (federal and provincial) have been, and are still, the principal source of funding for social enterprises through grants and subsidies. Indeed as the Task Force points out, Quebec has long been a leader through various government programs, dedicated financing vehicles, capital pools and enabling regulatory change.

In Canada, credit unions have long played a role in social finance and continue to be a major source of capital. For example, Caisses Desjardins du Québec is a founding leader in developing the Quebec social economy. In Ontario, the Caisses populaires de l'Ontario provides community based organizations with mortgages, operating lines of credit, and bridge financing. In British Columbia, Vancity, Canada's largest credit union, has $14.5 billion in assets and has taken a leadership role in exploring new vehicles to complement foundation funding efforts.

Figure 2 takes a closer look at the major types of actors on the supply side of the social finance marketplace. As the figure shows, the supply side is comprised of a wide range of actors, from government, credit unions, banks, foundations and venture philanthropists. Governments may provide social finance, such as small business loans, either directly or through an intermediary.

How does social finance work?

Social finance requires a new set of expectations between entrepreneurs and investors for repayment of principal and/or returns, and perhaps a degree of patience and forgiveness on the part of the investor (Emerson et al., 2007). In the social finance marketplace, traditional financing instruments have been adapted to reflect these needs. New instruments are also being developed and tested.

Our scan identified a number of sources that attempt to categorize and describe the various social finance tools (Shortall & Alter, 2009; Emerson et al., 2007; Hebb, 2012; Mendell & Nogales, 2011; Bugg-Levin, Kogut, & Kulatilaka, 2012; Joy, de Las Casas, & Rickey, 2011). These sources vary in terms of their organizing frameworks and whether they approach the topic from the perspective of investors or social entrepreneurs. In their guide to social investment for social entrepreneurs and practitioners, Shortall and Alter (2009) provide a useful and a widely cited typology of social finance instruments. Figure 3, which is adapted from their guide, provides a high level overview of the broad categories of social finance instruments currently in play. As the figure shows, social finance instruments range in terms of their degree of risk and potential to generate a financial return.

Figure 2 Actors on the supply side of the social finance marketplace

Investors

Banks
Investment bankers, wealth advisors, and fund managers provide impact-focused products (e.g. with non-financial, ethical objectives, and negatively screening public equity funds to avoid the support of damaging activities) for consumers that want to engage in impact investing (investing for financial plus social or environmental returns, or all three)."

Foundations
Engage in mission-related investments (MRIs) through a variety of investment vehicles (e.g. debt, venture capital, private equity). In contrast to a grant, the mission-related investment is repayable, with no or low interest.

Community loan funds
Micro-loans are directed to an underserved population of a community (entrepreneurs, small and medium enterprise, etc.) with the intention of contributing to the wider prosperity of the geographical region.

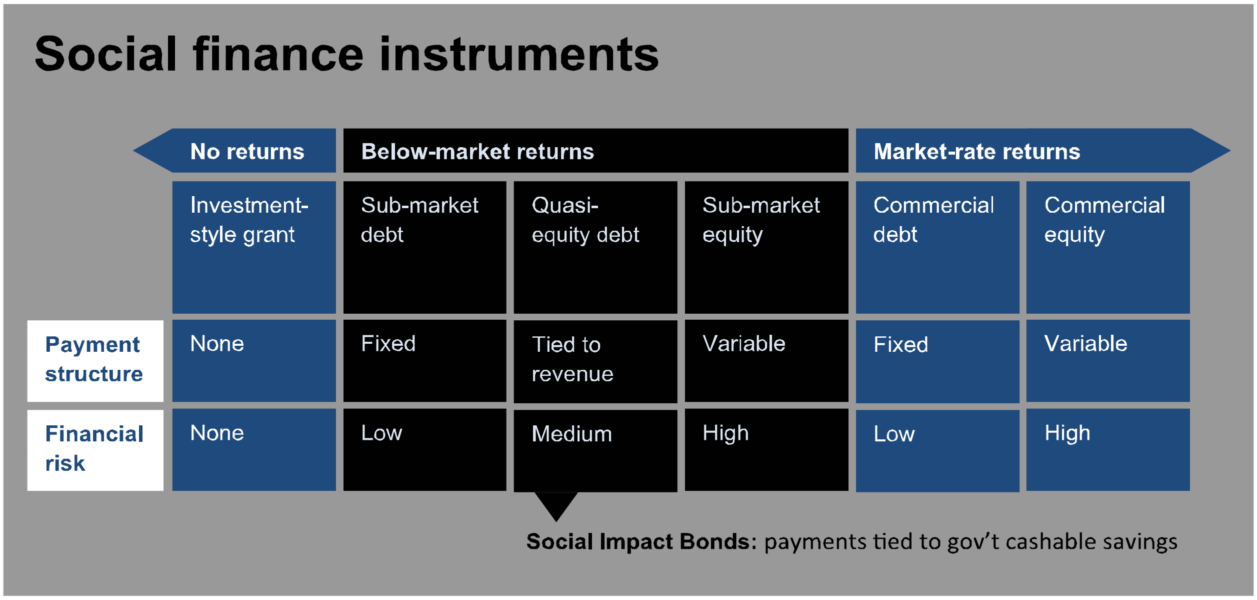
Community development finance and credit unions
Finance community economic development (CED) and social economy initiatives in a variety of ways (e.g. lines of credit, loans, start-up and growth financing.

Government
Provides direct access to capital (usually loans) for community investment and the social economy, or indirectly through financial intermediaries.

Social enterprise funds
Grants, loans and/or equity are provided to social enterprises to support development.

Venture philanthropists
Non-profits make long-term funding pledges to social enterprises, closely monitoring performance goals through pre-agreed assessment tools, and solve problems jointly with the enterprise in order to build capacity, produce deliverables, and create social return.

Figure 3 Types of social finance instruments



Source: Adapted from Shortall and Alter (2009) and Bugg-Levine, Kogut, and Kulatilaka (2012).

No returns – Investment style grants

According to Shortall and Alter (2009), investors typically offer a range of investment vehicles so that they can better tailor their financing to the needs of the social enterprise. At one end of the spectrum are investment-style grants. Investors provide grants to non-profits without the expectation of repayment or a financial return, although there is an expectation of a social return. Investors who make 'investment-style' grants are similar to venture capital investors. Like a venture capitalist, the social investor – commonly referred to in the literature as a 'venture philanthropist' – takes a highly engaged, long-term stake in the success of the organization, and invests in the organization's capacity and growth, rather than any specific program. Some venture philanthropists employ debt and equity along with grants (Shortall & Alter, 2009).

Below market returns – 'Patient Capital'

The rest of the spectrum is comprised of social financing instruments that require a financial return. Shortall and Alter (2009) maintain that, increasingly, social investors expect a financial return on their investment. According to the authors, the motivations for this vary. Some investors are simply hoping to make money while achieving social outcomes. However, other reasons may be more principle based. For example, investors may believe that debt repayment requirements introduce market discipline into a social enterprise, and/or that if a social enterprise is capable of providing financial returns, it should do so to allow capital to be recycled to other social enterprises (Shortall & Alter, 2009).

In the middle of the spectrum are instruments that yield below-market returns, sometimes referred to in the literature as 'patient capital.' These instruments may take the form of debt, equity, or quasi-equity debt, and are often characterized by a willingness to forgo maximum financial returns for social impact; greater tolerance for risk than traditional investment capital, longer time horizons for return of capital, and/or intensive support of management as they grow their enterprise (Evenett & Richter, 2011). Debt is simply an amount of money borrowed by one party from another that is to be repaid by the borrower, typically with interest. Sub-market debt requires a below-market rate of return to be paid by the borrower. Social investors may offer several concessions to a social enterprise, including longer repayment periods, lower interest rates, and interest holidays (the debt service is delayed until growth milestones are reached) (Shortall & Alter, 2009). Community bonds, which are securities issued by non-profits to raise debt-financing, are a type of sub-market debt. The Centre for Social Innovation in Toronto was able to raise $6.5 million to purchase real estate by issuing a 5-year, 4 per cent mortgage backed community bond (Mendell & Nogales, 2011).

Equity is defined by Shortall and Alter as the ownership of shares in a company, which are sold to investors in order to provide funds for growth of the enterprise. Investors receive a return once the company can pay dividends or is sold (2009). Sub-market equity is ownership of shares in a company that are not expected to provide market rates of returns to social investors (Shortall & Alter, 2009). Lower returns may be due to the social enterprise reinvesting most of its profits back into its social mission, or to the higher costs associated with working with specific target populations and/or testing out new models in hard-to-reach communities. The Canada Revenue Agency stipulates that only for-profit enterprises may receive equity investments.

Quasi-equity debt combines the properties of equity and debt, although it is usually structured as a sub-market loan (Shortall & Alter, 2009). Quasi-equity instruments are particularly useful for enterprises that are legally structured as non-profits and therefore cannot obtain equity capital (Bugg-Levin, Kogut, & Kulatilaka, 2012). Although technically a form of debt, it resembles equity financing in that its returns are indexed to the organization's financial performance, and the terms and conditions of the loan are carefully designed to promote the efficient operation of the organization. Because this type of financing performs the function of equity, it enables social enterprises to offer banks and other profit-seeking lenders a competitive investment opportunity (Bugg-Levine, Kogut, & Kulatilaka, 2012). Social Impact Bonds, a new type of financing that is being applied to pay for performance projects, are akin to quasi-equity instruments. Under a Social Impact Bond scheme, the government, in partnership with an intermediary, sells Social Impact Bonds to private investors, which covers the cost of the intervention. Investors get their principal investment back if the intervention meets a specific minimum target. For example, in the Peterborough Prison Pilot, investors are only repaid if recidivism decreases by 7.5 per cent. Anything above the minimum benchmark will give investors a return. The size of the return depends on the extent to which the target is exceeded (up to a specific limit). Thus, similar to quasi-equity tools, Social Impact Bonds are a form of debt with repayment and returns tied to the performance of service delivery organizations. (See Section 3 for a more in-depth discussion of Social Impact Bonds.)

Market rate returns – commercial debt and equity vehicles

At the far end of the spectrum are instruments requiring market-rate returns, such as commercial debt and equity vehicles. Commercial debt may come in the form of a loan or bond and requires full repayment plus market-rate interest. Some social investors may offer debt financing at commercial rates to social enterprises whose cash flow can sustain it. Commercial equity instruments are typically applied to social enterprises in cases when the enterprise is expected to be highly commercial and return market-rate returns to investors, while also making social impact (Shortall & Alter, 2009).

Another instrument not included in Figure 3 is a loan guarantee. The OECD defines a loan guarantee as "a legally binding agreement under which the (loan) guarantor agrees to pay any or all of the amount due on a loan … in the event of nonpayment by the borrower" (OECD, 2003). According to Shortall and Alter (2009), this type of agreement can give a social enterprise access to commercial debt that it might otherwise not have. For example, New York City is piloting a Social Impact Bond with a program to reduce recidivism rates, with the bond backed by a private investor. In this model, Goldman Sachs is contributing $9.6M to cover the cost of the intervention upfront, with a guarantee of $7.2M from Bloomberg Philanthropies. If the program is unable to achieve the minimum outcome target of reducing recidivism by 10 per cent, Goldman Sachs will only lose a small portion of its total investment ($2.4M) as Bloomberg Philanthropies is backing most of the loan (Deprez & Kaske, 2012).

Social enterprises require various types of social finance instruments depending on their needs and the lifecycle of the organization. For instance, a non-profit enterprise in the start-up or scaling-up phase may require investment-style grants to build organizational capacity along with sub-market debt financing to finance growth, while a for-profit social purpose business may seek any of the above, and/or commercial debt or equity financing. Enterprises may also seek sub-market or commercial debt financing as a source of working capital at any time in their organizational development.

A key finding of a recent Rockefeller Foundation report (2012) is that the social finance industry has focused primarily on its supply-side efforts to mobilize and place capital. As a result, there are still too few investment-ready projects and enterprises to facilitate the optimum allocation of this new capital (Harji & Jackson, 2012). As stated in the Rockefeller report, an important task moving forward will be to find scalable business models that are attractive to impact investors and ready to receive investment (Harji & Jackson, 2012). The remainder of this report aims to illuminate the various model options that may be effective in mobilizing social finance, and to explore the opportunities, key considerations and challenges that may exist for their application in a Canadian context.

3. A closer look at actors that use social finance

3.1 Three types of actors that use social finance

The social finance literature typically points to two broad categories of actors on the demand side of the social finance marketplace: enterprising non-profits, charities and co-operatives; and social purpose businesses (MaRS Centre for Impact Investing, 2010; Emerson et al., 2007; Hebb, 2012). However, given the recent attention paid by governments to innovative financing mechanisms such as Social Impact Bonds, we argue that governments are now also actors that may have a demand for social finance. The remainder of this report focuses on these three broad categories of actors; however, we narrow our scope slightly to include only organizational entities that have the potential to offer investors blended returns (financial and social returns). Therefore in terms of non-profits, charities and co-operatives, we consider only those engaged in enterprising activities that have the potential to generate at least some revenue.

Enterprising charities are registered charities that run a 'related business,' which according to the Canada Revenue Agency is a business activity that is either substantially staffed by volunteers or it is linked to a charity's purpose and subordinate to that purpose (Bridge & Corriveau, 2009). A *co-operative* is a special-purpose organization owned by members that use its services. It is operated with or without share capital. The members share equally in the governance of the organization, and any surplus funds (profits) are generally distributed among members or can be donated for community welfare or used to improve services (Task Force on Social Finance, 2010). *Enterprising non-profits* are non-profit organizations (without charitable status) that generate revenue but do not seek a profit. Any surplus revenues are unintentional and must be reinvested back into the organization's social goals.

Social purpose businesses are commercial, for-profit entities created to address social issues, with the core of their operations directed toward maintaining their social purpose, while operating in the market economy (Task Force on Social Finance, 2010). A social purpose business focuses on both its social and financial bottom line, but in recognition that without profits, it may not survive to meet its social goals (MaRS Centre for Impact Investing, 2010).

Governments may also require private capital to finance pay for success funding systems, such as Social Impact Bonds. In this context, the government creates a synthetic market for social service delivery, and acts as a catalyst that brings together key players – investors, service providers, external evaluators, and a financial intermediary. The government, through a financial intermediary, attracts private investment to fund service delivery. If providers achieve social outcomes that exceed a minimum outcome threshold, the cashable savings generated from these outcomes are used to pay back investors their principal plus a return. Providers are also provided a financial reward.

3.2 Six models in context of employment and training programs

The results of our scan indicate that all three of the above demand-side actors are currently operating in the domain of employment and training programs. Our scan also suggests that the models that these actors use can be differentiated according to type of business model and financing scheme. Enterprising charities and non-profits tend to be operating under one of three distinct business models.

Employment model – The first and most common model in use is what is termed in the literature as the 'employment model.' Under this model, the organization trains and hires its target population to sell goods or services to the public in a business related to the social mission, which generates revenues for the organization. These revenues are then reinvested back into the organization's social mission. Goodwill is an example of an organization using this model. Another example is Stella Burry Community Services. Stella Burry provides training to adults with mental health issues, and hires them to work in one of its three enterprises: a café, a construction business, and an office cleaning service.

Fee-for-service model – The second model that we identified in the non-profit employment and training sector is a 'fee-for-service' model whereby an organization commercializes its social services and sells them on the market. An example of an organization using this approach is EMBERS Staffing Solutions. EMBERS is a social staffing organization that provides employment opportunities to individuals facing employment barriers. It generates revenue by charging employers a fee for finding employees in construction, warehouse, administrative and other sectors, while serving its target population by providing training and fair wages.

Financial incentives – The third model we identified is what we refer to as the 'financial incentive employment model,' which was developed by the non-profit organization Social Capital Partners. This model differs from the first two models in that it was developed by one specific organization and, based on the findings of our scan, has not been replicated. In this approach, the organization acts as a labour market intermediary that offers prospective employers attractive debt financing conditional on their commitment to hire individuals with employment barriers in the local community into entry-level jobs.

Social purpose businesses – We identified only two examples of for-profit social purpose businesses in the employment and training field. One organization is Advanced Learning Interactive System Online (ALISON). ALISON provides online learning opportunities to anyone seeking to acquire workplace skills. ALISON is able to offer learners free training by offering publishers advertising space on its website. Revenues are also generated by charging nominal fees to trainers and humans resources managers who wish to track the progress of students. The other organization is TurnAround Couriers, which provides employment for at-risk youth to work in its back office or provide bicycle courier services in the Toronto and Greater Toronto Area.

Pay for success financing – Pay for success financing models involve private investors paying for upfront program costs, with the promise of a return on investment if program outcomes are above a specific threshold. Typically, providers are paid for achieving performance targets. Pay for success financing allows governments to mobilize private capital to invest in preventive solutions that have the potential to improve outcomes and generate cashable savings, while reducing or eliminating government risk. While our scan identified five variants of this model, so far only two variants – Social Impact Bonds and Human Capital Performance Bonds – are being applied in the domain of employment and training programs.

Public-private partnership – In addition, we identified a sixth model that is currently being proposed by the non-profit organization Social Capital Partners in Ontario. The proposed model is a public-private partnership approach that focuses on effecting systemic change by shifting employment and training systems to be demand-driven. The model involves an intermediary working with key stakeholders in the employment field (employers, community employment and training agencies, staffing firms, and governments) with the dual goal of making the system more responsive to employer and industry needs, and achieving improved longer-term employment and retention outcomes for job seekers with employment barriers.

Figure 4 provides an overview of the six major types of models that we identified in our scan. The next section provides a more detailed description of each of the six models.

Figure 4 Business models used by demand side actors in the employment and training domain

Enterprising charities and non-profits

Employment Model

Enterprise trains and hires target population to produce goods or deliver services. Must strike a balance between dual goals of offering employment experience to target populations and competing in the marketplace. *Note: extent to which model generates enough revenue to subsidize other services varies significantly by enterprise and over time.*

Examples: Stella Bury Community Service, Pioneer Human Services, Goodwill, Inner City Renovations

Fee-for-Service Model

Commercializes social services and sells them directly to target populations or "clients," individuals, firms, communities, or to a third party payer.

Examples: EMBERS Staffing Solutions, SkillPlan, Douglas College

Financial Incentive Employment Model

Investor leverages capital to change behavior in order to produce a desirable social outcome. For example an investor works with an intermediary to provide small business owners with attractive debt financing conditional on their commitment to fill entry-level positions with people from the community.

Examples: Social Capital Partners' Social Finance Fund

Social purpose businesses

For Profit Model

The business combines commercial and social goals with equal emphasis and generates a financial return to owners/shareholders.

Examples: ALISON, TurnAround Couriers

Government

Public-Private Partnership Model

Government partners with an intermediary that engages employers, investors, service providers and other experts to ensure incentives are aligned to optimize outcomes for the target population and deliver value for all stakeholders. Governments may need to re-align existing public investments, but benefit from cashable savings and improved outcomes for society. Employers contribute by providing opportunities to the target population in exchange for indirect financial returns, such as reduced costs and productivity gains.

Examples: Social Capital Partners' proposed employment pilots

Social Impact Bond Model

Government partners with private actors to share/transfer risk associated with scaling up promising preventive interventions. Private investors to cover the full up-front cost of intervention. Government, in partnership with intermediary, sells bonds (akin to quasi-equity debt) to private investors; which covers the cost of the intervention. If outcome targets achieved, government returns the principle and shares a portion of the cashable savings by paying investors a return. A portion of payments to providers is contingent on meeting performance targets.

Examples: Minnesota's Human Capital Performance Bonds

Note: examples from other policy domains include: Peterborough Prison Pilot; Goldman Sachs Jail Program

3.3 Enterprising charities, non-profits, and co-operatives

Employment model

The distinguishing feature of the employment model is that the target population is employed by the enterprise. This model appears to be the most common approach adopted by social enterprises in the employment and training field, perhaps because it directly serves the stated need of the target population, i.e., a meaningful employment opportunity. The results of our scan suggest that enterprises vary quite substantially however, in terms of the proportion of their workforce that is from the target population, and the extent to which competing in the marketplace is a goal.

This model is deeply rooted in the history of social enterprise. Indeed, it was used by Goodwill Industries as early as 1895 (Institute for Social Entrepreneurs, 2008). This model is currently used by organizations serving a wide range of target groups such as disabled persons, immigrants, youth at risk, former prisoners, Aboriginals, women, and individuals living in poverty. This model is roughly equivalent to the Work Integration Support Enterprises (WISEs) found in Western Europe.

Typically, the objective is to ladder individuals to sustainable employment in the competitive market. However, this process may use considerable time and resources and may require the provision of comprehensive employment readiness services and supports. The cost of providing these services cannot usually be passed on to the consumer (doing so would make the product/service too expensive to compete in the marketplace) (Corriveau, 2008). Consequently, enterprises may face pressure to hire more individuals who are closer to being employment-ready (Corriveau, 2008). Thus, in order to balance social and financial goals, most enterprises rely on a mix of government grants and earned revenue.

In most of the Canadian examples we identified, enterprises rely on public funding as a core element of their business model. For example, Stella's Circle is a Newfoundland organization that employs individuals with complex needs and barriers to employment in three enterprises: a cafe, a cleaning service and a trades-related service. Stella's Circle provides meaningful work opportunities to individuals with complex needs, in part, by relying on both government contracts and agreements that allow individuals to maintain existing sources of income assistance while they are employed in Stella's various enterprises. Indeed, even large and successful social enterprises in the US often rely on public funding. For example, Pioneer Human Services, a non-profit organization that operates in Washington State, employs ex-prisoners and recovering addicts in several profitable enterprises (Pioneer Human Services, 2011).[3] While Pioneer's various enterprises generate relatively large revenue streams, they continue to rely on government funding for counselling and other wraparound supports.

We did identify a small number of enterprises that are financially independent such as Manitoba social enterprise, Inner City Renovations. This enterprise hires a high proportion of its employees (more than two-thirds) from its target population of inner-city Aboriginals and, after five years, now generates a profit (Social Capital Partners, 2011). It is worth noting, however, that Inner City renovations benefited

3 In the United States, non-profits can engage in revenue-generating activities that result in annual surpluses or profits; however, unlike for-profits, non-profits must reinvest surpluses back into the organization and its tax-exempt purpose (See http://www.irs.gov/pub/irs-pdf/p4220.pdf).

from a substantial investment from a venture philanthropist and needed to make several adjustments to its model before it achieved sustainability. *Thus, for the most part, our environmental scan suggests that in order to maintain a balance of social and financial goals most enterprises integrate a mix of revenue sources rather than aim for complete financial self-sufficiency. (See Aiken, 2007, for further discussion of this point.)*

Fee-for-service model – Alternative staffing organizations and training enterprises

Most of the employment and training organizations that use a fee-for-service model are staffing agencies that broker jobs for hard-to-employ individuals. These organizations are often referred to as 'alternative staffing organizations,' or ASOs. ASOs range in terms of organizational form, scale, and type of client served. Most are organized as subsidiaries of non-profit parent organizations. Similar to conventional staffing agencies, ASOs charge employers a fee for finding candidates to staff their job openings, and the worker is on the payroll of the ASO. This market-based approach leverages either public and/or philanthropic support with fees-for-service charged to employers, making it a highly cost-effective and sustainable workforce development strategy. In the United States, fee revenues generally cover at least 75 per cent of an ASO's operating costs, which allows it to leverage grant investments. Fee revenues lower the average cost per job seeker served compared with other transitional employment models (Alternative Staffing Alliance, n.d.).

ASOs are distinguished by a 'dual customer approach.' While conventional staffing agencies tend to focus on the employer as the key customer, and publicly funded employment services tend to focus on the job seeker as the key customer, ASOs seek to build strong relationships with *both* job seekers and employers (Carré et al., 2009). In the United States, ASOs often focus on particular groups of job seekers who have barriers to employment. For example, ASOs may focus on brokering jobs for individuals residing in an economically distressed neighborhood, job seekers with previous criminal convictions, or job seekers who have disabilities (Holgate et al., 2012).

The innovation of alternative staffing agencies is that they tap a very large market that is dominated by for-profit staffing agencies that have little incentive to engage individuals with employment barriers. This is an important market to tap, given that some large Canadian companies rely on private agencies exclusively for the hiring of front line employees.

ASOs vary in the ways they connect individuals to training opportunities. Some provide limited connections to training, while others run in-house training programs or partner with training organizations. For example, Triada is an alternative staffing operation developed and run by Wisconsin Regional Training Partnership (WRTP)/Big Step. WRTP serves individuals with employment barriers, through its training programs in construction and manufacturing. WRTP is well-known for its deep relationships with employers and labour management partnerships.

EMBERS Staffing Solutions is the first ASO in Canada and operates as the enterprising arm of EMBERS, an economic development charity. The enterprise was created to establish a sustainable revenue source for EMBERS' microenterprise and small business incubator operations.[4] EMBERS credits its

[4] In this case staffing services provided to the target population is intended to generate the revenues to subsidize the other social activities of the organization.

success to several factors. First, because the enterprise is related to its mission, it is allowed to operate as a division of the charity and benefit from tax-free status, rather than as a separate taxable corporation. Second, EMBERS was able to gain a competitive advantage over existing for-profit staffing agencies by offering higher rates of compensation and training opportunities to job candidates. Third, since the social enterprise model of non-profit ASOs had already been tested in the US, EMBERS was launched with a solid business model. Fourth, EMBERS was able to attract financial support for development and ongoing working capital requirements through the Vancouver Foundation and VanCity Credit Union. Finally, EMBERS is able to capitalize on synergies between its charitable and social enterprise components, such as its existing relationships with employers and contractors (Sinopoli, 2012).

Training providers

Another type of social enterprise that may operate under a fee-for-service model is training providers. For instance, SkillPlan, a non-profit enterprise operating in British Columbia, charges a fee-for-service for some of the basic skills training it provides. Although service fees make up only a portion of total revenues (other sources include union dues and government contracts), the portion of revenue from fees has grown over the past several years as SkillPlan pursues more fee-for-service contracts to serve greater numbers of workers with lower skills and to meet growing demand from industry. Some Canadian provincial sector councils such as the Ontario Tourism Human Resource Council also rely on a hybrid model of government contracts and fee-for-service activity.

Financial incentive employment model

This model was developed by Social Capital Partners in 2006 and is used in its Social Finance Fund program (see profile on page 12). It provides small business owners with attractive debt financing conditional on their commitment to fill entry-level positions with job seekers who have overcome employment barriers. The model directly ties financial incentives to employment outcomes by linking the interest rate on the loan to the number of individuals hired through community employment agencies – for every new community hire, the interest rate declines. The organization partners with non-profit community employment agencies, such as the YMCA, to source and pre-screen job candidates based on the fit and skills required by its clients. The business owner thus benefits not only from a reduced interest rate, but also from cost and time savings associated with the recruitment process. Employers are evaluated on a number of social criteria including labour intensity, job quality and career progress opportunities (Social Capital Partners, n.d.). This model is significant to the extent to which it taps into the mainstream private sector, using financing as a lever to change the human resource behaviour of small businesses. However, we are not aware of other Canadian or international examples of this model.

Examples of enterprising charities and non-profits

Stella Burry Community Services

NEWFOUNDLAND | is a charity that provides support to adults who have suffered mental health issues. The agency provides customized training and employment opportunities to its target population through three enterprises: a café; a construction business, and an office cleaning service. Clients receive training and support while they gain work experience.

Goodwill

INTERNATIONAL | is a charity that supports individuals facing employment barriers. The organization runs several enterprises including thrift shops that employ members of its target population. In 2011, more than 189,000 people obtained meaningful employment through their participation in Goodwill programs. Goodwill's enterprises generate substantial revenues; a portion of which is used to subsidize the training and wraparound services it provides to clients.

EMBERS Staffing Solutions

BRITISH COLUMBIA | is Canada's first socially responsible non-profit temporary staffing agency. A division of the economic development charity, EMBERS, the staffing agency was created in response to both a market-driven social need, as well as the charity's own need to diversify its revenue base. The agency generates revenue by charging employers a fee for finding workers in construction, warehouse, administrative and other sectors on a monthly, weekly or daily basis. And the agency serves the target population by providing training and fair wages ($16/hour) to individuals facing employment barriers. As the agency continues to grow and become more profitable, excess funds will be directed toward EMBERS Ventures, helping to decrease dependency on external funders and increase the resilience of the overall organization.

Pioneer Human Services

WASHINGTON STATE | is a nonprofit organization that supports individuals overcoming mental illness, addictions, and persons re-entering society from prison. The agency provides customized training and employment opportunities to its target population through numerous enterprises such as construction, food services, manufacturing and pest detection. Combined these enterprises generate over 25 million in revenue; a portion of which is used to subsidize the training and wraparound support services it provides to clients

Inner City Renovations

MANITOBA | is a non-profit enterprise that provides employment for inner city low-income residents through general contracting services for infrastructure projects in Winnipeg's inner city. Inner City Renovations recruits at least 60% of employees from low-income, inner city neighbourhoods.

Social Capital Partners' Social Finance Fund

CANADA |Social Capital Partners is a non-profit organization that aims to align the interests of employers, governments, community agencies and jobseekers so that everyone benefits. Through its Social Finance Fund, Social Capital Partners provides small business owners with attractive debt financing conditional on their commitment to fill entry-level positions with people facing employment barriers from community employment agencies. . Clients have the opportunity to decrease the interest rate on their loan based on their success hiring from local community employment agencies.

3.4 Social purpose businesses

Another type of actor that uses social finance is what the MaRS Centre for Impact Investing calls a *social purpose business*. Social purpose businesses are for-profit organizations but differ from traditional businesses that engage in social activities primarily to fulfill corporate responsibility mandates. Instead, *social purpose businesses pursue social and financial goals with equal emphasis* (for a more formal discussion of social purpose businesses, see Dees & Anderson, 2003).

Our scan identified one example of a social purpose business that provides employment-related training. The Advanced Learning Interactive System Online (ALISON) is an innovative business that reaches thousands of individuals around the world whose job prospects are constrained by their skill levels and who lack the resources to upgrade them through conventional training. In 2011, ALISON received an award from UNESCO for innovation in online workplace education and has been recognized by Ashoka as a social entrepreneur (Bornstein, 2012).

From the standpoint of investors, this model is attractive because it offers the potential of a financial as well as social return. However, it is unclear the extent to which this model has applicability in the context of a policy area that targets individuals with complex needs and barriers. Recent developments with ALISON provide some insight here. In the United States, ALISON is now offered through government workplace centres in 18 states. That said, however, the general concept of a social purpose business may not translate that well to target populations that would require intensive services to overcome multiple employment barriers, since these services would likely be priced above what the market would be willing to pay.

Examples of social purpose businesses

The Advanced Learning Interactive System Online (ALISON)

IRELAND | is a for-profit social purpose business that provides learning opportunities to anyone seeking to acquire workplace skills. In 2012, ALISON offered over 400 courses and diplomas spanning topics from health studies to graphic design. What distinguishes ALISON from other for-profit providers is that all of its programs are free. Publishers agree to work with ALISON because they receive advertising space on the website. In addition to the sale of advertising, the model is sustained by nominal fees to trainers and human resources managers who wish to track the progress of their students. ALISON also relies on organizations to provide educational content without the expectation of a financial return. ALISON operates on every continent, and has over 1 million registered users worldwide. In 2011 alone, over 50,000 users earned certificates or diplomas.

TurnAround Couriers

TORONTO |TurnAround Couriers is a for-profit social purpose business that offers couriers services in Toronto and the Greater Toronto Area. Launched in 2002, TurnAround Couriers recruits only at-risk young adults for all of its bicycle and back office staff. In addition to providing work experience for its employees, TurnAround Couriers also encourages its staff to pursue further education during their tenure and the company and will assist in funding the educational expenses.

3.5 Governments

Pay for success financing model

Pay for success financing provides a means for governments to mobilize private capital to invest in preventative solutions that have the potential to improve outcomes and generate cashable savings, while reducing or eliminating government risk. All pay for success models involve private investors paying for upfront program costs, with the promise of a return on investment if outcomes are above a specific threshold, and providers are paid for achieving performance targets. There are several variants of pay for success financing including two that have been applied in the domain of employment and training: Minnesota's Human Capital Performance Bonds and UK's New Horizons Social Impact Bond.

Social Impact Bond (SIB)

The most well-known 'pay for success' model is the Social Impact Bond that is currently being tested in the UK through the Peterborough Prison Pilot. Launched in 2010, the government, in partnership with an intermediary, sold a 'bond' (akin to quasi-equity debt) to private investors, which covered the cost of the intervention. Investors get their principal investment back if the intervention meets a specific minimum target. For example, in the Peterborough Prison Pilot, investors are only repaid if recidivism decreases by 7.5 per cent. Anything above the minimum benchmark will give investors a return. The size of the return depends on the extent to which the target is exceeded up to a specific limit. The rate of return is set based on some portion of the total cashable savings that the government expects to receive as a direct result of reduced recidivism. Therefore if an intervention is successful in exceeding the minimum benchmark, the government pays out more than the actual cost of the program, but less than the total savings that the government expects to receive. Service providers also receive payments for meeting specific performance targets through a performance-based funding mechanism to ensure that providers are incentivized to achieve outcomes.

The UK also recently launched the New Horizons Social Impact Bond, one of six projects funded by the UK government's Innovation Fund. The Fund has commissioned Triodos Bank to manage the project. Triodos has partnered with Greater Merseyside Connexions Partnership and other local charitable providers in the Merseyside area to deliver the New Horizons program. The program will provide intensive support to 3,900 young people, including those who are currently in the care system, young offenders and young people with learning difficulties. Investors will be repaid by the Department of Work and Pensions. Investors will receive payment of up to 12 per cent annually if the project achieves a number of outcomes, including encouraging young people to remain in education, placing young people in training courses and placing them in jobs for 26 weeks. If the charities fail to hit outcome targets, the investors will absorb a loss (Ainsworth, 2012).

This approach offers the potential of enabling governments to both generate cashable savings as well as bring promising solutions to scale. For example, in the domain of employment and training programs, making an investment in high quality skills upgrading combined with comprehensive wrap-around supports may result in significant cashable savings in the form of reduced income assistance payments as well as increased tax revenues. From the standpoint of governments, the most significant benefit of this approach is that risk is transferred from the government to private investors, since the government pays nothing if the intervention is not successful.

SIB with full/partial guarantee

A social impact bond has been launched in the United States with a similar funding structure, with the notable exception that the model includes a partial guarantee, which means that risk is shared between private investors and a private guarantor. In the recently launched, NYC Prison Social Impact Bond pilot, the private investor, Goldman Sachs, is contributing $9.6M to cover the cost of the intervention upfront, with a partial guarantee of $7.2M from Bloomberg Philanthropies. If the program is able to reduce recidivism by at least 10 per cent, Goldman Sachs will receive its principal investment plus a return of up to $2.1M. If the program is unable to reduce recidivism by 10 per cent, Goldman Sachs will only lose a small portion of its total investment ($2.4M) as Bloomberg Philanthropies is backing most of the loan (Deprez & Kaske, 2012).

Human Capital Performance Bonds (HUCAP)

The state of Minnesota recently launched what it calls Human Capital Performance Bonds (HUCAP). The government of Minnesota is raising funds by issuing annual appropriation bonds and directing those funds to non-profits that have demonstrated the potential to generate positive social outcomes and create government savings. It then plans to use the cash unlocked by those savings to repay the bondholders. The $10 million designated toward Human Capital Performance Bonds in Minnesota's 2011 budget made Minnesota the first, and so far the only state to pass legislation on pay for success contracts (Belinsky, 2012). It is expected that the bond will be 10 years in length, with sufficient principal to provide between 20-30 per cent additional funds over the provider's current state allocation for a period of three to four years (Invest in Outcomes, 2011).

Under this structure, the government sells bonds and holds investor funds until payout terms are met by a certified pool of high-performing providers whose previous outcomes have exceeded the minimum threshold required to service state debt (Invest in Outcomes, 2011). Certified providers may request a working capital loan from a capital pool. Providers receive payments if they successfully perform. The size of the payment would be directly related to the size of the incremental economic value the government receives from increased tax collections, lower public subsidies and lower prison costs. The government would never pay more than it expects to get back on a present value basis (Rebeck, 2012). The government establishes the economic value equation for service providers (i.e., a share of the incremental value created). If performance targets are met, the government receives a high return on investment which generates cash flow to fund interest and principal repayment to investors. The government retains residual cash returns to lower the cost to the government. If performance targets are not met, the government has use of the funds for principal repayment, interest, or other purposes until the bond period terminates, since providers are paid only when they meet performance targets (Rothschild, 2010). If no provider meets their targets, no payments are made to providers and the government may call the bond early. The government's cost would be one year interest payment to the investors (at 4 per cent in Minnesota HUCAP), plus some administrative expense less the amount it can earn on investing the bond proceeds (at 1 per cent in Minnesota HUCAP) (Invest in Outcomes, 2011).

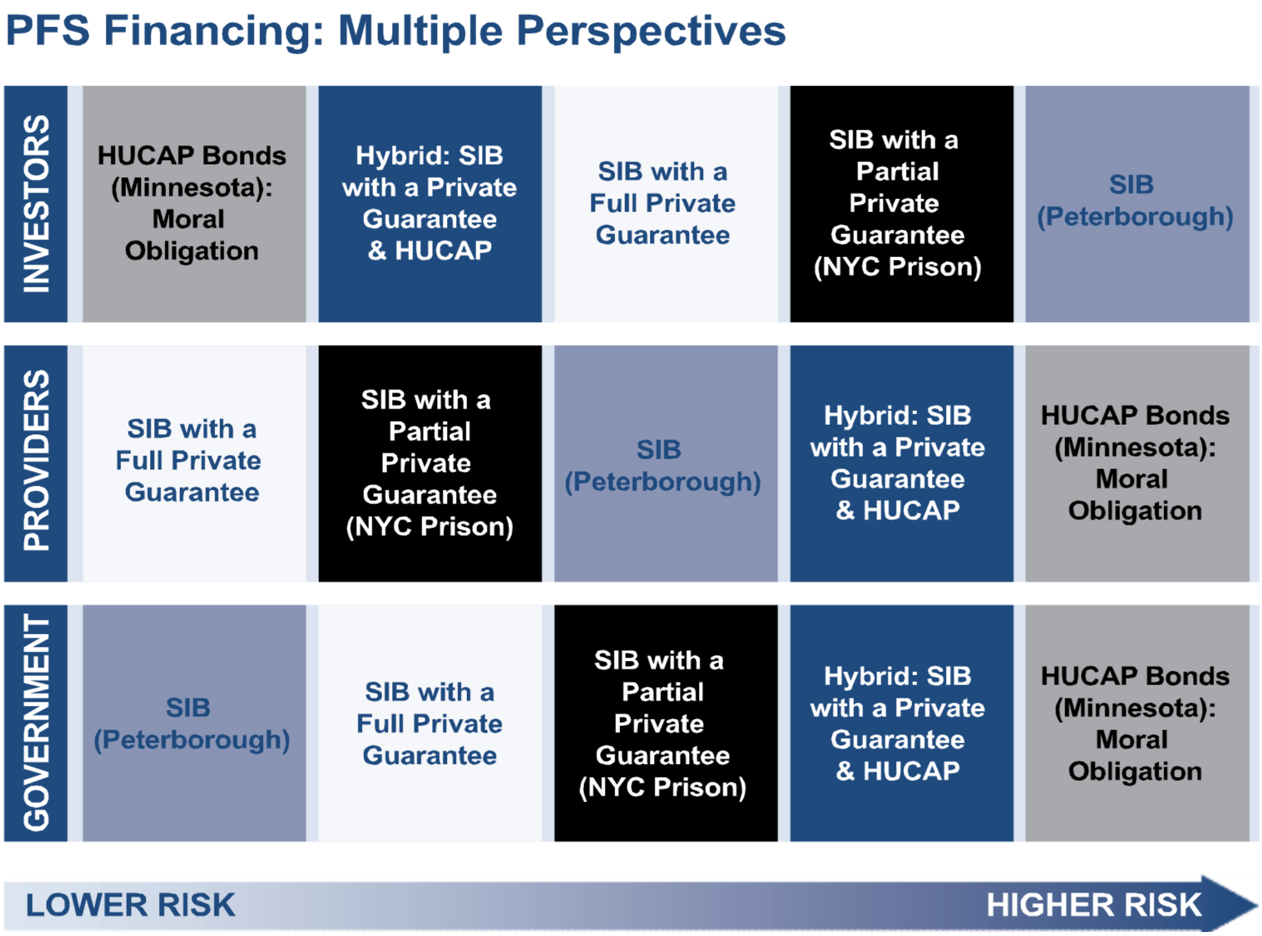
Investors face the same risk that all AA-rated appropriation bondholders face.[5] A variant on this model would be to backstop loans to providers with a private guarantee (Nonprofit Finance Fund, 2011a).

Comparing pay for success financing structures

Each approach to pay for success financing offers participating stakeholders various degrees of risk and so may cause different stakeholders to have different perspectives on which structure suits their respective needs. Figure 5 below illustrates the risk trade-off continuum for each of the three main stakeholders in a PFS financing scheme: government, providers, and investors. As the figure shows, investors who are more averse to financial risk are more likely to prefer the HUCAP model because the financial instrument is a true bond and the likelihood of the government failing to pay out on the bonds is slim, whereas they are likely to shy away from SIB schemes in which repayment is dependent on service provider performance. However, almost the opposite is likely to be true of service providers. Providers are likely to opt for SIB models because they can access working capital provided by private investors at no cost, as opposed to the HUCAP model in which providers must borrow funds for working capital from a loan pool and thereby shoulder all of the financial risk for outcome performance. Although all pay for success financing models aim to significantly reduce government risk, governments may prefer one model over another for different reasons. Governments focused primarily on reducing financial risk may opt for the Peterborough Prison SIB model as all risk is transferred to private investors. However, while the HUCAP model poses a small financial risk to government, associated with negative arbitrage (due to drop in interest rates after the bonds are sold), it may be easier to implement since it uses familiar, pre-existing financial instruments (annual appropriation bonds).

5 Annual appropriation bonds are not backed by the government's full faith and credit. The obligation of government to pay debt service is contingent upon inclusion of the debt service payment in the government's adopted budget.

Figure 5 Pay for success financing risk tradeoff continua for stakeholders



Source: Adapted from Nonprofit Fund, 2011.

Public-private partnership model

The government is also a lead actor in the public-private partnership or ‘P3’ model that is currently being pitched by an organization called Social Capital Partners.

The proposed P3 model involves an intermediary that serves as a catalyst working with the major actors in this system: governments, employers, community service agencies, staffing agencies and other stakeholders, with the dual goal of making the system more responsive to employers’ needs, and achieving improved longer-term employment outcomes for target populations.

This model does not use a social finance approach per se, but we include it because it emerged directly out of Social Capital Partner’s early experimentation with various social finance approaches, which includes every model discussed above with the exception of social impact bonds. While most of these enterprises are still successfully in operation, Social Capital Partner’s leadership team has become increasingly interested in generating opportunities to impact change at a more systemic level. At the same time, they are also becoming increasingly aware of the relatively high resource intensity associated with the social finance approaches in which they had been involved. As a result of these two factors, they were becoming increasingly interested in more resource-efficient approaches to innovation with the ultimate goal of improving outcomes for as wide a number of job seekers as possible.

According to Social Capital Partners, an opportunity arose when they realized that the franchise owners they were engaging with through their Financial Incentives program did not actually require the ‘carrot’ of attractive debt financing to participate as long as the services that they received from participating employment agencies were high quality and responsive to their needs. This was one of the insights that led Social Capital Partners to believe that the key to improving employment and training systems was to create opportunities to better align the needs of actors in the system. While they continue to believe that social finance approaches are one mechanism to achieve this alignment, they have become increasingly interested in opportunities to make better use of existing government funding streams.

Social Capital Partners’ P3 approach would involve creating a formal channel for collaboration through the creation of ‘employer councils,’ which would bring together CEOs and other groups, such as community agencies, vocational trainers, sector councils, trade unions and industry associations, as appropriate, for five-year terms. The point of the council would be to collaborate for the purposes of designing the service delivery system that will prepare disadvantaged job seekers for employment in their respective businesses/industries, including testing and revising different training and employment preparation models (e.g., sector specific) through pilot projects. Councils could be created based on geography, industry, and/or employer size (Social Capital Partners, 2012).

As we discuss in the next section, this model was particularly well-received by both government officials and service delivery providers in the Manitoba Roundtables. Indeed, shortly after the roundtable event, the Manitoba government formally agreed to pilot-test this model and at the time of writing, design work has already begun.

Examples of government approaches

Public-private partnership model

Social Capital Partners

CANADA | This is an approach currently being proposed by Social Capital Partners. This proposed approach focuses on effecting large-scale, systemic change by addressing what SCP calls the supply-demand interface. The model involves an intermediary that serves as a catalyst working with the major actors in this system: employers, community service agencies, governments at all levels, staffing agencies and other stakeholders, with the dual goal of making the system more responsive to employers' needs, and achieving improved longer term employment outcomes for target populations. The model is premised on the assumption that all partners contribute and all partners benefit.

Social Impact Bond

Human Capital Performance Bonds

MINNESOTA | Human Capital Performance Bonds is a Social Impact Bond pilot program that officially recognizes that non-profit organizations create financial value that can be captured and used to fund services. The state of Minnesota would enter into a contract with a service provider (based on projected social and financial benefits) once certain performance measures have been met. Services would focus on workforce training, as well as mental and physical treatment to generate human capital. Bonds would be sold to private investors creating a pool of funds to pay service providers. Once the state begins to receive financial returns, these financial returns are set aside to pay back the investor with interest. At present, the state has authorized US$10 million of appropriation bonds for the pilot.

Prison Social Impact Bond

NEW YORK CITY | Goldman Sachs, a for-profit banking firm, is investing US$9.6 million aimed at reducing recidivism rates in New York jails. Goldman's funds, which serve as a Social Impact Bond, will be geared toward outcomes. The money from Goldman Sachs will be used to pay MDRC, a social services provider, to design and oversee the program. If the program reduces recidivism by 10 percent, Goldman would be repaid the full $9.6 million; if recidivism drops more, Goldman could make as much as $2.1 million in profit; if recidivism does not drop by at least 10 percent, Goldman would lose as much as $2.4 million. The potential loss is capped at $2.4 million because the charitable foundation Bloomberg Philanthropies has insured the loan up to $7.2 million. If the program fails, the foundation gets stuck with the bigger portion of the cost.The program represents the first attempt by a municipal government in the United States to leverage private capital through a Social Impact Bond toward a social investment.

Peterborough Prison Pilot

UNITED KINGDOM | Social Finance Ltd. launched the world's first Social Impact Bond in September 2010. The UK-based organization raised £5 million from 17 investors to fund a comprehensive re-entry program (the One*Service) for short-sentenced prisoners leaving Peterborough prison over a six-year period. The SIB contracts organizations to provide tailored wrap-around services to 3,000 prisoners before and after their release to facilitate successful re-entry into the community. The Ministry of Justice and the Big lottery Fund have agreed to repay these investors if one-year post-release reconvictions decrease by at least 7.5 percent, relative to a comparison group. Returns are commensurate with social outcomes and will range between 2.5 percent and 13 percent.

4. Analysis and discussion

In this section, we draw on the literature as well as the findings of our consultations with policymakers and service delivery providers in Manitoba to analyze the extent to which these various social finance approaches may play a role in helping governments meet their policy objectives.

4.1 Employment model

The employment model has several strengths. First, and perhaps most obviously, under this model, there is a direct opportunity to align the needs of providers, employers and job seekers because the provider and the employer are in fact one and the same. Second, because this model aims to generate at least some revenue, it may open up opportunities for innovation by generating a revenue stream with fewer constraints than are typically found with government funding streams. These two benefits taken together may provide both the incentive and means for experimenting with new approaches to serving the target population. Given the resource-intensive nature of this model, successes will likely be small scale. The most promising innovations, however, could potentially be scaled-up and integrated into a more system-wide approach. Thus, this model can potentially serve as an 'innovation pipeline.' A further benefit is that the model may be particularly well-suited for people who are not ready for employment in the competitive labour market. Because the enterprise is both the provider and the employer, this model tends to be a more supportive environment for individuals with complex barriers.

Both the Manitoba government officials and service provider roundtable participants were particularly interested in the employment model's potential to align stakeholder interests, while providing the freedom and flexibility to find innovative solutions to local problems. Participants acknowledged that the risks of starting a social enterprise are equal to, if not greater than, the risks of starting any business and thus did not see this model as one with widespread applicability; however, they argued that this model may have an employment role to play in the employment and training services landscape. They identified the model used by Inner City Renovations as a particularly compelling approach and one with which many roundtable participants were familiar (see profile on page 22).[6]

As discussed above, the key challenge associated with this model is the need to continually balance social and financial goals (Shamash, 2010). From the standpoint of the social mission, the purpose of the employment model is to hire job seekers who need extra support and training in order to become effective employees. However, this may be at the expense of the financial goals since poor performance may lead to weaker business results (Social Capital Partners, 2009). Thus, successful social enterprises need to develop cost-effective strategies like providing new recruits with customized training. However, even the most effective employment enterprises tend to rely on government funding as well as earned income.

[6] Inner City Renovations employs local low-income residents in the construction of local infrastructure in Winnipeg's inner city. During the roundtable, Bill Young, the major investor in Inner City Renovations made the point that prior to its launch, many downtown development sites were often quickly vandalized. Once Inner City Renovations was launched, because it employed local residents, they became vested in the preservation of the property. This vested interest appears to have contributed to considerably fewer incidences of property damage.

4.2 Fee-for-service model – Alternative staffing organizations

The experience of alternative staffing organizations (ASOs) in the United States demonstrates that this approach has the potential to reach relatively large numbers of job seekers. Several ASOs in the US place over 1000 workers annually (Carré et al., 2009).

There is some evidence to suggest that alternative staffing organizations (ASOs) may represent an opportunity to connect job seekers from disadvantaged backgrounds to expanded economic opportunity in the communities in which they live. Indeed, as many large companies are increasingly relying on staffing agencies to fill their entry level recruiting needs, ASOs may represent a critical pathway to a 'hidden' job market (Grant, 2012; ACSESS, 2012). In addition, as Holgate and his colleagues (2012) point out, job candidates with employment barriers do not tend to fare well in a marketplace where job application procedures have become 'tighter' and more formalized, with greater reliance on online applications that filter out those whose background does not meet the job specifications. More fundamentally, ASOs provide job matching and placement services to job seekers that often do not exist or can be difficult to access through traditional employment agencies.

Summarizing the results of several early research studies, Holgate and his colleagues (2012) report that the demand-side orientation of ASOs is often appreciated by workers, who state that the advantage of an ASO over another workforce development or training program was that *the ASO placed them in a job*. For many job seekers, this was a distinct improvement over just receiving assistance or guidance in their job search process, which they were accustomed to getting from employment programs.

Roundtable participants who were service providers expressed cautious interest in this approach. On one hand they saw this model as providing an opportunity to more deeply engage employers as a customer. By requiring employers to contribute to the cost, it could encourage employers to have a more vested interest in the success of individual job seekers. And by more clearly positioning the employer as a customer, providers may be better positioned to achieve longer-term employment and retention outcomes for the target population. As such, this model has the potential to align the incentives of all key stakeholders – government, providers, employers, and the target population – toward the achievement of longer-term employment outcomes.

Both government officials and service providers also pointed out that a 'fee-for-service' model would be a departure from the current system where *employers are sometimes paid to hire job seekers through tax credits and wage subsidies.* Participants pointed out that wage subsidies tend to inadvertently stigmatize the employee by sending a signal that the client is not of similar quality as employees hired through more conventional channels. By charging employers a fee, not only would this provide a new stream of revenue, but it would signal to employers that the service being provided to them is of both social *and financial* value.

But service providers also raised questions about how this model could work in the context of existing service delivery networks and funding mechanisms. Given the different legal and institutional environment in Canada versus the United States, the American experience does not provide readily transferable answers.

More specifically, service providers expressed concern about whether in practice this model would be able to provide a true alternative to for-profit staffing agencies which they perceived as being focused primarily on meeting the needs of employers and not on providing opportunities for job seekers to obtain sustainable employment.

In terms of training enterprises that use fee-for-service models, participants noted that Workplace Education Manitoba already applies a hybrid government funded and fee-for-service model to the provision of workplace Essential Skills training. This model could be tested in other jurisdictions. Given that both federal and provincial governments have already made significant investments in the research and development of high quality sectoral curricula, the enterprise could lever these investments to offer high quality curricula at a relatively low cost.

4.3 Financial incentive employment model

The financial incentive model provides small business owners with attractive debt financing conditional on their commitment to fill entry-level positions with job seekers who have overcome employment barriers. Government and non-profit roundtable participants alike were intrigued by this model. They expressed enthusiasm for the ingenuity of offering employers something that they need – debt financing – in exchange for employers hiring clients from community employment agencies. Mostly, however, they found the role of the intermediary to be the attractive component of this model, and even non-profit providers indicated that they would appreciate the service of an intermediary like Social Capital Partners that could better interface with employers. Both government and providers noted several challenges in working more closely with employers including current funding restrictions, as well as the skills and experience of agency staff.

This model has several strengths including the fact that it does not involve any start-up risks on the part of the social investor, and the probability of success is much higher because it invests in businesses that have already proven their business concept and possess well-defined operating models. This makes the business easier to run while simultaneously allowing the social mission to be introduced (Social Capital Partners, 2006). The key challenge with this approach is identifying franchises that can provide entry level jobs but also offer opportunities for wage progression and career advancement. This a key challenge given that many franchises often operate in sectors that do not emphasize sustainable employment opportunities, where remuneration is generally low, and where ideal employment and career progression opportunities are few and far between (Social Capital Partners, 2006).

Like all of the models presented so far, the balancing of financial and social goals is a challenge. The experiences of Social Capital Partners suggest that a business owner that is financed by an intermediary may face mixed incentives. On one hand, the owner will demand business performance in line with other business units while on the other hand the intermediary will put pressure on the owner to execute effectively on the social mission. To mitigate this potential conflict, intermediaries in cooperation with community service agencies may need to provide support for business owners, such as providing assistance around hiring and training their target employees (Social Capital Partners, 2006).

4.4 Pay for success financing model

Although still in its infancy and far from proven, pay for success financing may be a promising approach to mobilizing private capital for solving social problems and determining which social programs are successful and worthy of government investment. Pay for success models are a clear catalyst bringing together and aligning the interests of the public and private sector and, if successful, have the potential to affect large-scale, systemic change. Because providers are paid for performance, this may infuse a market-like discipline into service provision, creating incentives to find new and innovative approaches that can result in better outcomes for clients and in turn, increased savings for government.

The Young Foundation identifies several factors that are likely to be critical to the success of pay for success financing models. Key factors include the preventive nature of the intervention, its potential to improve wellbeing in an area of high social need, and the extent to which it is supported by evidence of its efficacy and impact. In addition, impact should be relatively easy to measure and closely related to the savings of a specific government stakeholder. Savings should be relatively immediate and much greater than the cost of the intervention and transaction costs (Young Foundation, 2011). Based on these criteria, employment and training systems may be particularly suitable for pay for success financing models for several reasons. First, employment and training programs, if effective, can prevent recurring unemployment and reverting back onto employment insurance or social assistance. Second, long-term unemployment is a significant issue among specific population segments and thus is an area of high social need. Third, there are numerous examples of interventions in Canada and the US that show promise for improving employment and retention outcomes and so may be attractive to social investors. Fourth, it would be relatively straightforward to measure employment and retention outcomes, as well as to determine the cashable savings that could result from a reduction in clients that revert back to social assistance. Making an investment in high quality skills upgrading combined with comprehensive wrap-around supports may result in significant cashable savings in the form of reduced EI and social assistance payments as well as increased tax revenues. Finally, evidence from Ontario shows that roughly half of individuals that move from social assistance to employment cycle back into social assistance within the first year (Brighter Futures Report, 2012) therefore, there may be an opportunity to realize cashable savings in a relatively short time period.

Service providers were particularly interested in the ‘pay for success’ model in that they felt it presented an opportunity to shift funds from remedial to more holistic and preventative programs. Service providers also expressed interest in the opportunity to demonstrate a track record of success in achieving their mission goals. Government officials were tentatively interested in this model but expressed concern about measurement issues and the likely need to track potentially hard to measure outcomes and cost savings across multiple ministries. Government officials also raised this issue of added complexity around contracting issues.

4.5 Public-private partnership model

While the previous models may have potential to offer providers more flexible financing and align stakeholders’ interests, they likely do not have the capacity to produce large-scale social impact. Nor do they appear to address other system-wide problems, namely the highly fragmented employment services landscape of many provinces. The P3 model proposed by Social Capital Partners aims to address this confusion and, by partnering directly with government, may have the potential to produce social impact on a larger scale.

There was strong consensus among Manitoba Roundtable participants that this model has the strongest appeal. Participants saw significant promise with this approach since, in Manitoba, the context of low unemployment rates amid looming labour shortages is perceived to present a ripe opportunity for private and public sectors to collaborate to employ more marginalized groups. In particular, participants were particularly interested in the value added that could be brought by an intermediary who has expertise in dealing with both social service providers and employers, and thus can effectively work with both parties to ensure that the needs of all the key stakeholders are met. Government officials in particular recognized that this model has the potential to achieve impact on a greater scale because it has the capacity to put greater numbers of clients into employment at a faster rate, and it is not confined to serving franchises alone, which often may not present clients with opportunities for career progression.

The notion of 'employer councils' that would be comprised of regional employers, industry groups and other stakeholders was also very appealing to both government and non-profit participants. Generally speaking, participants recognized that improving the outcomes of clients would require better meeting the needs of the private sector, and that establishing formal mechanisms for private sector input and collaboration is likely a key component of a more demand-led approach to employment and training systems. Manitoba is perceived to be in a favourable position to establish councils given the already existing high capacity of its sector councils and industry associations.

More than any other model, this model has the potential to have system-wide implications for funding and delivery of employment and training programs. Given the uniqueness and scale of this model, further research is needed to provide a careful analysis of opportunities, challenges and implications.

Conclusion

This paper identifies several distinct models that apply a social finance approach to the provision of employment and training services. The three approaches used by enterprising non-profits (employment model, fee-for-service model, and financial incentives model) are clear examples of social innovation. For instance, while the employment model is time and resource intensive, and requires careful development and business expertise, when successful it offers multi-barriered clients an opportunity that they are not likely to receive anywhere else – namely, a meaningful entry-level position in an enterprise with a social mission, and a work environment that is accommodating to clients' barriers. These types of enterprises also create a breeding ground for innovation, and lessons learned from such enterprises can inform future programs that can be designed to have a larger-scale impact. Fee-for-service models and financial incentive employment models are also promising in that they call for a more demand-led approach to service delivery, which may translate to better employment and retention outcomes for clients. The key challenge associated with all of these models is the need to balance social and financial goals and manage this tradeoff effectively. In two of the three models – employment and fee-for-service – active government support appears to be a critical success factor.

Government-led approaches may be better positioned to achieve large-scale social impact. For instance, the public-private partnership model is promising to the extent to which it offers potential to unite a multitude of public and private stakeholders around common needs and interests and provide formal collaboration mechanisms to find solutions to these common needs. Meanwhile, pay for success models appear to have the potential to pool risk while mobilizing enough private capital to fund the scaling up of effective employment and training interventions. These models may also be more resilient in the face of typical bureaucratic hurdles and changes in government leadership.

What all of these models have in common is that they all aim to align needs among key players in the employment and training system: employers, providers, governments and job seekers. All models, albeit in different ways and to different degrees, have the potential to contribute to a shift to a more demand-led approach to employment and training that involves building relationships with employers in an effort to better meet their needs, with the ultimate goal of improving the client's employment and retention outcomes.

Thus, the major finding of this paper is that, taken together, various social finance approaches have the potential to play a significant role in addressing one of the most pressing challenges in the domain of employment and training programs, which is how to foster a more demand-led system that engages local employers and ensures that the target population is well-trained for jobs that actually exist in local labour markets. The real promise of social finance approaches is in their ability to align needs and infuse a market discipline that better motivates and enables providers to engage employers and thus stimulates the transition to a demand-led system.

That said, our analysis suggests that social finance approaches are not without their own challenges: the learning curve is steep and transaction costs are high. But while social finance approaches are far from a panacea, their focus on mobilizing capital and aligning needs almost by definition positions them to play a role in creating a more effective employment and training system.

What would governments need to do to encourage the proliferation of these models? Given the complexity of existing funding arrangements, further research is needed to determine how these arrangements would need to be adapted to encourage the implementation of any of these models. Indeed most roundtable participants indicated that they had difficulty seeing how any of these models were even possible under existing federal, provincial and territorial funding arrangements. A better understanding of the regulatory environment is also required. (While a discussion of the regulatory environment is outside the scope of this paper, see Appendix B for a brief discussion.)

From a more immediate and practical standpoint, governments can also lay the groundwork by shifting toward a focus on programs that actually demonstrate the achievement of outcomes that will result in cashable savings to the public purse. Social finance approaches may only be successful if they are designed to finance *what works,* as the private sector will not be willing to shoulder undue risk for programs that have demonstrated less than positive success. Thus, if a social finance approach to employment and training service provision is desired, governments may need to: (1) revise funding mechanisms so that funding and social finance is channeled toward achieving outcomes rather than outputs, and (2) revise monitoring and evaluation functions accordingly to collect greater intelligence on which programs are associated with improved outcomes for job seekers and their families and ultimately net benefits to society.

Appendix A: List of consultation participants

Bill Young – President, Social Capital Partners

Jan Forster – Assistant Deputy Minister, Labour Market Skills and Employment Income Assistance

Paul Holden – Senior Executive Director, Labour Market Skills Division

Dave Fisher – Senior Executive Director, Employment Income Assistance Division

Kimberley Puhach – Senior Executive Coordinator, Labour Market Skills Division

Tim Jones – Executive Director, Division Support

Peter Szewchuk – Director, Finance

Lynn Houghton – Executive Director, Industry Workforce Development

Jacqueline Ratte-Kohut – Executive Director, Apprenticeship

Crystal Chercoe – Director Policy, Employment Manitoba

Phillip Evans – Manager Winnipeg Division, Employment Manitoba

Sandi Howell – Director – Sector Councils, Essential Skills and RPL, Industry Workforce Development

Bev Stewart – Executive Coordinator, Minister’s Advisory Council on Workforce Development

Bruce Clark – (ret) VP Shuman Resources Standard Aero and board member, Minister's Advisory Council on Workforce Development

Ron Koslowski – VP Manitoba Division Canadian Manufacturers and Exporters and board member, Minister's Advisory Council on Workforce Development

Sarah Staziak – Executive Director Manitoba Music (sector council) and board member, Minister's Advisory Council on Workforce Development

Wendy Bulloch – Executive Director, Literacy Partners of Manitoba

Jeremy Johnson – Program Coordinator, Literacy Partners of Manitoba

Katherine Green – Literacy Partners of Manitoba

Cheryl Barsalou – CEO, Manitoba Customer Contact Association

Lisa Dabrowski – Manager, Training and Development, Manitoba Customer Contact Association

Thom Sparling – Executive Director, Arts & Cultural Industries Association of Manitoba

Carol Findlay – Director, Education and Training Development, Arts and Cultural Industries

Kara Wright – Operations Manager, Workplace Education Manitoba

Sheila Kingswell – Project Office, Workplace Education Manitoba

Jonathan Cote – Communications Coordinator, Workplace Education Manitoba

Rosemary Deans – Education and Training Coordinator, Manitoba Environmental Industries Association

Deb Tardiff – Education and Training Coordinator, Manitoba Environmental Industries Association

Anthony Augustine – Manitoba Workplace Integration of Newcomers

Dave Shambrock – Executive Director, Manitoba Food Processors Association

Fatima Soares – Executive Director, Manitoba START

Debbie Donato – Team Leader - Career Coaches/Facilitators, Manitoba START

Jonathan Bauer – Workshop Facilitator and Career Coach, Manitoba START

Shannon Fontaine – Manitoba Tourism Education Council

Neila Benson – Executive Director, Manitoba Film

Barbara Bowen – Manager of Special Programs, Manitoba Aerospace Human Resources Association

Darrell Cole – CEO, Career Trek

Shawn Mahoney – Executive Director, Opportunities for Employment

Appendix B: FAQ on legal issues and key developments

1. From a legal standpoint, how can a charity generate its own revenue?

- A **charity** can generate revenue through a related enterprise. The CRA defines a 'related business' as

  a) A business that is run substantially by volunteers (90 per cent);

  b) A business that is linked or subordinated to the charity's main purpose.

2. What happens if a non-profit organization or a charity makes a profit? What are the challenges faced by these organizations in this area?

- A **non-profit** can only make a profit unintentionally. A non-profit might budget with the intention of not earning a profit, but ultimately find itself with a profit because of expenses that were less than anticipated or that were reasonably expected but not actually incurred.
- It is generally acceptable for non-profits to make a profit so long as the original budget was reasonable, the profit earned would not, in and of itself, cause the organization to cease to be a non-profit entity as defined by the Canada Revenue Agency, and as long as it is not recurring. However if an organization intentionally earns a profit, it will lose its tax exemption status.
- A **charity** can generate profits from a related business (as defined by the Canada Revenue Agency), so long as profits are reinvested back into the organization to fund the organization's programs.

Challenges:

- Non-profits are not able to actively pursue profits, even if the purpose of profit generation is to reinvest back into the organization to fund the organization's programs. This may create a lack of financial stability and may make annual budgeting more challenging.
- For national organizations, the relevant legislation and regulatory systems can vary from province to province, making legislative compliance challenging for organizations.

3. What type of social financing is available to charities and non-profits?

- Non-profits and charities can access social finance in the form of debt financing such as mortgages, lines of credit, operating lines of credit, and quasi-equity investments.
- Unlike Low-Profit Limited Liability Companies (L3Cs) in the US and Community Interest Companies (CICs) in the UK, charities and non-profits in Canada cannot directly raise equity capital.

4. What are recent developments in Canada and the US related to social finance and social enterprise?

New guidance from Canada Revenue Agency gives social enterprises more flexibility around revenue generation and introducing more sources of private capital

- On July 26, 2012, the CRA released new guidance that, according to an analysis by the BC Centre for Social Enterprise, relaxes language related to profit generation such that enterprising not-for-profits and charities are not prohibited from making a profit, so long as profit generation is not the focus. Onus is on the organization to demonstrate that any profits realized were indeed not the main focus. The implications of this are that organizations no longer need to needlessly rack up expenses in order to meet the previous breakeven requirement, or have to hive the enterprise off into a taxable corporation.
- Moreover, social enterprises can now raise capital from private foundations' Program Related Investments (PRIs). PRIs are repayable investments made by charitable foundations out of their grant funds and count toward their disbursement quota. Foundations' PRIs can now be directed not only to qualified donees (registered charities) but also to non-qualified donees such as simple non-profits and for-profit businesses.

New legal changes in US allow more opportunity to mobilize private capital for social goals

- In 2008, Vermont passed legislation that enables the creation of new legal entities called Low-Profit Limited Liability Companies, or L3Cs. L3Cs are not subject to federal income tax, and importantly, are able to attract private capital for their works through the sale of shares and other securities, various forms of loans, or other commercial financial arrangements.
- A key feature of the L3C innovation is the ability that they provide to American charitable foundations to make Program Related Investments in these new legal entities. This substantial pool of investment capital enables L3Cs to leverage other capital (from pension funds, institutional and individual investors, banks, insurance companies, etc.) to undertake community projects.
- The L3C has been passed into law in Vermont, Michigan, Utah, Wyoming, Illinois, New York, North Carolina, Maine, and Louisiana. Legislation is being reviewed in Colorado, Georgia, Oregon, North Dakota, Tennessee, Arkansas, and Arizona.
- In 2010, Maryland passed legislation enabling and legitimizing 'Benefit Corporations.' Vermont followed in September. Key features of the new law are:
  - Explicit recognition that public benefit purposes (e.g., positive environmental or community impacts) may be adopted by corporations
  - An obligation on directors to pursue those purposes and consider the interests of stakeholders (employees, community, etc.)
  - Confirmation that the maximization of shareholder value is not the dominant duty of directors, and legal protection for directors who pursue public benefits

- A requirement that Benefit Corporations publish annual Benefit Reports that document performance in achieving their public benefit purposes
- A 2/3 shareholder vote requirement for changes to the control, purpose, or structure of a Benefit Corporation

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