MERGING THE PROFIT MOTIVE AND MORAL IMPERATIVES: THE RISE OF SOCIAL ENTERPRISE IN THE UNITED STATES

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Federal and state government have been all but irrelevant to the evolution of social enterprise in the United States.

The movement emerged primarily from the private sector, in the 1970s and 1980s. Except for a few courageous entrepreneurs scattered across the country, people in the nonprofit sector did not begin to explore the possibilities until the mid-1990s. Still another decade passed before federal and state governments began to pay serious attention. Even today, efforts by the public sector to support social enterprise are limited to creating modest incentives for social investors and occasionally using the bully pulpit to endorse the efforts of social entrepreneurs.

An explosion of activity took place across the United States during the 1970s and 1980s as entrepreneurs, small businesses and major corporations discovered social markets and started social enterprises. They began to run adult day-care centers; educational programs for small children, high-school dropouts, and adult students; low-cost-housing projects; vocational training and job-placement efforts; home-care services for the disabled and elderly; hospice care; outpatient mental-health and rehabilitation services; prisons; wind farms; psychiatric and substance-abuse centers; and dozens of other businesses that delivered products and services previously provided by nonprofits or government agencies.

How did most people in the nonprofit world react?

They were appalled, affronted by the thought of "making money" while delivering social services and blind to the financial pressures that would gradually erode nonprofit reserves and force them to seek new sources of revenue to finance their programs. For the most part, nonprofits remained frozen for nearly 30 years while businesses cherry-picked the most attractive market opportunities.

How did the public sector react?

It didn't. If anything, it pushed more and more of the responsibility for meeting social needs onto the nonprofit sector and simultaneously slashed federal and state funding for human services by 23 per cent, in real terms, during the 1980s alone.

ORIGINS

Although there had been isolated incidents of private sector companies addressing social needs through their products and services, William C. Norris, founder of Control Data Corporation, codified the principles of social enterprise for the private sector when his Fortune 100 company responded to the torching of American cities during the inner city riots of 1967. Norris immediately built plants in five inner cities and two depressed rural communities -- and then proclaimed his company's new strategy would be "to address the major unmet needs of society as profitable business opportunities." Control Data began to use its expertise in computing services to revitalize urban and rural neighborhoods, incubate small businesses, promote alternative energy sources, create jobs, deliver education, and respond to other social needs.

During the next two decades, Control Data's example prompted other companies to follow its lead, and, in 1982, the management expert Peter Drucker and the economist John Kenneth Galbraith, as well as more than 250 chief executives from around the world, joined Norris at Control Data's headquarters in Minneapolis for an international conference to promote the concept.

Drucker spoke about simultaneously "doing good and doing well," Galbraith debunked the business bromide that "our social responsibility begins and ends at the bottom line," and Norris repeated the message he had been trumpeting for years: The transformative power of business, he told his colleagues, is the ability to merge two often opposing forces -- the profit motive and moral imperatives.

Norris and his admirers were creating something new, something the business world had never seen. Their social enterprises went beyond the traditional concept of corporate social responsibility by *directly confronting social needs through the businesses themselves* in addition to grappling with them indirectly through socially responsible business activities such as corporate philanthropy, paying equitable wages, refusing to manufacture weapons, and using environmentally friendly raw materials.

But it took nearly a generation before most people in the nonprofit arena grasped the power of the social markets. Once they did, in the mid-1990s, nonprofits around the country began to pursue sustainability by adding business activities to their traditional stew of volunteers, charitable donations and government grants. A few have even abandoned dependency on donors and government subsidies entirely, achieving self-sufficiency by focusing exclusively on profits from their businesses.

DRIVING FORCES

So what changed? What prompted nonprofits to re-assess their traditional strategies?

During the past three decades, social innovators in the United States and around the world began to reach a disquieting conclusion: Inspired vision, impassioned leadership, enthusiastic volunteers, government subsidies and a phalanx of donors are not always enough.

They serve admirably while innovators transform their dreams into fledgling programs and steer their organizations through early growing pains. But there comes a time, albeit reluctantly, when most founders and their followers begin to understand that living from year to year does not ensure the future, and that is the moment when they begin migrating from innovation to enterprise. It is one thing to design, develop and carry out a new program, quite another to sustain it. So they begin turning toward commercial markets, gradually exploring the possibilities of *earned* revenue, many for the first time, and often with reluctance given their uneasiness about the profit motive.

The moment of realization comes at different stages and for different reasons. Major funders may be experiencing donor fatigue. The initial band of dedicated volunteers and employees might be burning out. Government support for a project could be waning or the cost of delivering services escalating dramatically. It might even be that the organization is on the threshold of significant growth but cannot proceed without new sources of financing.

In the United States, the moment arrived for most nonprofits in the mid- to late-1990s, although a handful of pioneering social entrepreneurs had been emphasizing earned revenue since the 1960s and 1970s. Around the world, the moment is dawning today for some of the most successful social innovators, and they are slowly moving away from a *dependency* model of financing, the traditional business model for nonprofits in which they depend solely or almost entirely on charitable contributions and public sector subsidies, with earned revenue either non-existent or minimal. The movement takes two forms:

- Some are working toward ***sustainability***, the ability to fund the future of a nonprofit through a *combination* of philanthropy, government subsidies and earned revenue

- Others are seeking ***self-sufficiency***, the ability to fund the future of a nonprofit through earned revenue alone

DEFINITIONS

A social enterprise today is defined as any private sector or nonprofit business that uses earned revenue strategies to pursue a double or triple bottom line, either alone (as a social sector business) or as a significant part of a mixed revenue stream that includes charitable contributions and public sector subsidies.

In the United States today, there are basically three types of nonprofit social enterprises:

- ***CHAMELEONS*** are businesses that begin life as nonprofits and stay that way -- but in every other respect operate as for-profit businesses. They have at least a five-year track record of self-sufficiency, defined as consistently hovering around break-even or achieving profitability through earned revenue alone. Well-known examples include Pioneer Human Services in Seattle, Housing Works in New York, Minnesota Diversified Industries, Delancey Street Foundation in San Francisco, and Gulf Coast Enterprises in Florida.

- ***MIGRATORS*** have at least a five-year track record of *pursuing* self-sufficiency, defined as being fully committed to social enterprise, with earned revenue the driving force for strategic planning, and at least two-thirds of the organization’s operating expenses covered by earned revenue. Prominent examples include Melwood in Maryland, Skookum in Washington, Esperanza Unida in Milwaukee, Rubicon Programs in San Francisco, and Triangle Residential Options for Substance Abusers in North Carolina.

- ***SUSTAINERS*** are not seeking to make a profit from their earned revenue strategies, but use them to reduce dependency on philanthropy and government subsidies. Earned revenue typically covers less than two-thirds of their operating budgets and may or may not be the driver for their strategic planning, but it still plays a significant part in the organization's financial framework.

The types of businesses operated by social enterprises in the United States can be divided into three categories. The first treats the people it serves as potential employees, the second views them as customers – and the third combines the two approaches.

- ***AFFIRMATIVE BUSINESSES*** (known in the U.K. as "social firms") are created specifically to provide four things for people who are mentally, physically, economically or educationally disadvantaged: Permanent jobs, competitive wages, career tracks, and ownership opportunities. It has been estimated that more than two-thirds of all social enterprises created by nonprofits in the United States are affirmative businesses, primarily because one of a nonprofit's greatest assets is an available, untapped labor force (and also because these types of businesses are more difficult to scale and therefore less appealing to the private sector). The businesses themselves are typically straightforward enterprises such as janitorial services, telemarketing, packaging/assembly plants, temporary employment agencies and the like -- their social missions are workforce development, job creation and career development.

- ***CUSTOMER-FOCUSED BUSINESSES*** directly address social needs other than workforce development, job creation and career development. They can be sub-divided into categories such as "human service businesses," "environmental businesses," "educational businesses," and so on. Examples include such enterprises as home care services for people who are frail or elderly, adult day care, assistive devices for people who are physically challenged, management of low-income housing units, employee assistance programs, publishing companies, and dozens of others.

- ***HYBRID BUSINESSES*** simultaneously deliver a product or service that directly addresses a social need *and* employs the members of a target population such as people who are developmentally disabled, men and women on welfare, former prisoners, recovering drug addicts, high school dropouts and others.

Business ventures that generate revenue from a nonprofit's under-utilized assets or as a convenience for clients or patrons (such as space rental, parking lots and cafeterias) are not considered to be social enterprises (unless they qualify as affirmative businesses) because the ventures are not *directly* related to a social mission.

CONTRIBUTING FACTORS

A series of tectonic shifts occurred during the last 30 years of the 20th century in the United States that changed the rules of the game for nonprofits and prompted them to join the private sector in the social enterprise arena:

- Operating costs began to escalate and nonprofit reserves eroded: In 1977, the average nonprofit in the United States had more than three months of operating capital in reserve at any given time – by 1989 it had less than four days, not enough to cover even a single week's payroll

- Annual support from individual, corporate and government sources all declined or flattened

- More nonprofits began to compete for the available charitable funds (there are three times as many nonprofits in the U.S. today than there were 30 years ago)

- More people needed help with the basics of food, clothing and shelter

- Donors and government officials began calling for nonprofits to do more with less, insisting on greater accountability and better results

- Numerous well-publicized scandals embarrassed the nonprofit sector and by the mid-1990s, according to the Gallup Poll, one in three Americans believed the nonprofit sector should be eradicated because it was inefficient, ineffective and unethical

FIGHTING BACK

By the late 1990s, we began to see a response to this pincer movement closing in on the sector, especially a shift in mindset away from viewing service recipients as objects of charity toward one that viewed them as capable individuals who could benefit more from opportunity and empowerment than from handouts. That led to the expectation programs should intervene in people's lives in ways that create growth and independence rather than dependence, and earned revenue initiatives – especially affirmative businesses -- met that expectation perfectly.

The severe cuts in government funding for human services during the Reagan Administration in the 1980s also forced nonprofits to either find new ways of doing business (*e.g.,* leaner, meaner, more self-sufficient) or watch their organizations disintegrate. Simultaneously, at the close of the 1980s, the triumph of capitalism over communism in Eastern Europe ushered in a new respect for the power and legitimacy of the marketplace, even among the liberals who were managing most nonprofits -- and not just as a transactional environment but as a transforming one.

In addition, throughout the latter half of the 20th century, the "entrepreneur" had emerged as the hero of the new economy in the United States, leading to greater tolerance for informed risk-taking and innovations, even among staid nonprofits: In 1967, only eight American universities and colleges were offering even a single course in entrepreneurship; by 1984 there were more than 250, including 212 business schools and 41 engineering schools.

And as we neared the end of the century, volunteers and Board members who came from the business world began importing new philosophies and management theories. Coupled with escalating demands for superior leadership and accountability, these new ways of thinking and behaving led nonprofits inexorably toward strategies for improved performance and sustainability, which in turn pointed toward social enterprise.

Increasingly, then, nonprofit leaders began embracing the concept of social enterprise and started working individually to change their organizations and collectively to create a movement. We began to see the emergence of heroes and role models, authors and activists who paved the way, people who provided the practical models and "proof of concept" that helped push recalcitrant Board and staff members to do what had previously been unthinkable -- endorse earned revenue initiatives.

CURRENT CONDITIONS

Across the globe, social enterprise today has moved into the mainstream and is no longer an isolated experiment. During the spring of 2010, the 11th Social Enterprise Summit, sponsored by the Social Enterprise Alliance, the largest membership organization for social entrepreneurs in North America, is being conducted jointly with the 3rd Social Enterprise World Forum, which is rotating through five continents from 2008 through 2012. Federal and state officials around the world are awakening to the potential of social enterprise, including a few enlightened public servants in the United States. A dozen international conferences each year tout the benefits of social enterprise; for-profit and nonprofit social enterprises are proliferating; academic institutions are offering courses and degree programs; social investors are knocking at the door; the subject appears everywhere in the news media; and a rising generation of young people is energizing the field.

So: We have an emerging lexicon, a rapidly growing community of social enterprise practitioners, an expanding pool of knowledge, new support systems (communications networks, conferences, consultants), a heightened expectation that nonprofits will apply business practices, evidence of more sophisticated business planning, an increasing flow of human and financial capital, and an eroding gulf between nonprofits and for-profits.

What we didn't have in the United States, until very recently, is any significant involvement by the federal or state government, and certainly nothing like the interventions of the British government during the first decade of the 21st century. That is slowly beginning to change. The government has long been a purchaser of products and services produced by nonprofits through such federal set-aside programs as AbilityOne, but today it is also stimulating social investors by creating new legal forms such as low-profit, limited liability corporations (L3Cs) that make it easier for nonprofits to raise money for their social enterprises. As a result, a new breed of social investors is rising that has very different priorities than traditional investors or those who are interested in corporate social responsibility *per se* (see "Investment Priorities Matrix***"©*** on the next page).

For the most part, however, the social enterprise movement in the United States continues to be driven by the private sector and, increasingly, by the nonprofit sector. The social markets began calling 40 years ago. Entrepreneurs, small businesses, and large corporations listened -- and eventually nonprofits joined them. Today the public sector is also beginning to recognize the transforming power of social enterprise – and, at long last, is starting to treat it seriously.

Jerr Boschee has been an advisor to social entrepreneurs in the United States and elsewhere for more than 30 years. To date he has been a keynoter or conducted master classes in 43 states and 15 countries, and has long been recognized as one of the founders of the social enterprise movement worldwide. He has also been a senior marketing executive for a Fortune 100 company, managing editor for a chain of regional newspapers, a Peace Corps Volunteer in India, and a guest lecturer at numerous academic institutions, including Cambridge, Carnegie Mellon, Duke, Georgetown, Harvard, Northwestern, Oxford, Stanford and others. He is the former President and CEO of The National Center for Social Entrepreneurs, is one of the six co-founders of the Social Enterprise Alliance, and was named by The NonProfit Times *to its nonprofit sector "Power & Influence Top 50" lists in 2004, 2005 and 2006. He served from 2001 to 2004 as an advisor to England's Department of Trade and Industry Social Enterprise Unit and is the author or editor of six books, including* Boschee on Marketing, The Social Enterprise Sourcebook*, and the award-winning* Migrating from Innovation to Entrepreneurship: How Nonprofits are Moving toward Sustainability and Self-Sufficiency. *His e-mail address is jerr@orbis.net.*

"INVESTMENT PRIORITIES MATRIX"

	Businesses with a single bottom line *(financial)*	**Business with a single bottom line that practice corporate social responsibility**	**For-profit social enterprises *(double bottom line)***	**Nonprofit social enterprises *(double bottom line)***
TRADITIONAL INVESTORS seeking financial returns	**FIRST PRIORITY**	SECOND PRIORITY	THIRD PRIORITY	NOT A PRIORITY
SOCIALLY RESPONSIBLE INVESTORS seeking both social and financial returns	NOT A PRIORITY	**FIRST PRIORITY**	SECOND PRIORITY	THIRD PRIORITY
SOCIAL INVESTORS seeking both social and financial returns	NOT A PRIORITY	THIRD PRIORITY	**FIRST PRIORITY**	SECOND PRIORITY
SOCIAL INVESTORS primarily seeking social impact	NOT A PRIORITY	THIRD PRIORITY	SECOND PRIORITY	**FIRST PRIORITY**