

Commission on Poverty (CoP)

“From Welfare to Self-Reliance” -

Social Enterprise Development – An Update

PURPOSE

This paper updates Members on the initiatives to further encourage the development of social enterprises (SEs) in Hong Kong, including training and business support, as well as efforts to creating an enabling environment for SEs.

BACKGROUND

2. At the Commission meeting on 12 September 2005, Members supported the direction to further encourage the development of SEs to facilitate work integration of the unemployed through providing them with a real work environment to acquire the necessary skills and work habits. A number of initiatives have been launched to further promote SE development in the past year –

- (a) establishing the value and gaining public acceptance (through conferences and seminars, publicity and researches);
- (b) providing facilitation and support measures (including start-up funding, training and business support); and
- (c) creating an enabling environment (exploring a more SE-friendly public procurement regime, and relevant regulatory framework).

3. Members were updated at the last meeting on 20 November 2006¹ on the start-up funding provided through the Enhancing Self-Reliance Through District Partnership Programme under the Home Affairs Department. This paper will update Members on training and business support, as well as efforts to creating an enabling environment for SEs.

¹ CoP Paper 21/2006 refers.

SE TRAINING AND BUSINESS SUPPORT

4. Recognising the lack of personnel with business mindset and experience as well as social purposes to run SEs, the CoP Ad Hoc Group on SE Training has held a number of informal brainstorming sessions with the universities/skills training institutes/private sector and non-governmental organisations to explore the training needs in Hong Kong. As a start, the Hong Kong Council of Social Services (HKCSS) in collaboration with a number of tertiary institutes with expertise on business management and social entrepreneurship has undertaken to develop a training programme that caters for the training needs of middle to senior management mid-careers from the NGO or private sector. The curriculum, which includes drawing up business case studies on the factors leading to the success and failure of social business, is being developed. The programme will be launched in the first half of 2007. Suitable accreditation will be issued to the participants who complete the programme.

5. The SE training programme should help equip SE practitioners and those interested to start a SE, including applicants of the Enhancing Self-Reliance Through District Partnership Programme, with essential business knowledge and operational skills. The programme will be complemented by business mentorship. Existing support to small and medium sized enterprises (SMEs) available under the Trade and Industry Department and its SME Committee (business advisory service; business information and other activities for SMEs) is also available to the potential social entrepreneurs.

6. Besides more practical SE training programme and business support for SE practitioners and mid-careers, it is equally important to promote the concept of SEs in the universities which can act as an important bridge between the social sector and the private sector, by promoting the concept of corporate social responsibility and social entrepreneurship among students who may work with SE/NGOs or businesses willing to partner with SEs in the future. In this regard, the tertiary institutes would be invited to consider adapting the SE training programme as part of their business study modules in future. Separately, the tertiary institutes will jointly hold a Hong Kong Social Enterprise Challenge in the first half of 2007 to encourage students to partner with SEs or NGOs in drawing up viable SE business plans, and to educate them on the needs of the community and the potential benefits of SEs.

FACILITATING SE IN THE PUBLIC PROCUREMENT PROCESS

7. In the 2006/07 Budget, the Administration has undertaken to facilitate the participation of SE in public procurement, subject to the principles of transparency, fairness and value for money. In the case of SEs employing people with disabilities, procuring departments would consider giving them preferential treatment through the use of restricted tender or the award of additional weighting in open tender exercises. Such preferential treatment however should not apply to the case of SEs employing the able-bodied unemployed in order to avoid displacement of SMEs. This is also in line with the policy to regard such SEs as competitive businesses instead of welfare operations.

8. That said, it is possible to facilitate SEs employing the able-bodied unemployed to participate in public procurement through taking into account the additional benefits they can bring, e.g. in terms of facilitating training and work integration of the unemployed alongside mainstream service delivery. We have drawn references to overseas practices and explored with relevant bureaux and departments on possible models to operationalise this objective. We are working on a pilot operational model which requires successful bidders to employ a certain percentage of the unemployed persons who have completed a relevant retraining programme offered by the Employees' Retraining Board (ERB). The tendering process is non-discriminatory - SEs and for-profit enterprises can bid for the contracts so long as they can deliver the required outcomes (e.g. quality of mainstream service, plus engaging a number of trainees from relevant training schemes). There is however a need to modify the procurement requirements and to work out a cost-effective method to manage such contracts. Our aim is to identify some pilot contracts for the purpose of testing out this operational model in the first half of 2007. More details are available at *Annex A*.

9. In facilitating SEs to participate in the public procurement process, we are weary that most of the SEs are relatively small-scale operations at the moment and there are limitations to the size and type of contracts they can bid. In addition, most of the outsourced social and personal services are currently provided by NGOs. Nevertheless, taking into account the additional community benefits brought by SEs in the procurement process is a small but important step. At the same time, we would continue to promote the products and services of SEs to those responsible for public procurement at both the central and district level, and we encourage the same among NGOs and the private sector.

REGULATORY FRAMEWORK

10. SEs may take different legal forms (companies, subsidiaries of charities, co-operatives, etc.) appropriate to the background and the needs of the particular operations. With voluntary membership structure and democratic member control, co-operatives are often used for groups of people to form self-help organisations to meet their specific needs in a collective manner. In terms of economic activities, some co-operatives provide goods and services to their member-owners e.g. the more traditional type of co-operatives among the agriculture and fisheries sector or for building civil servants' flats. In recent years, there have been more co-operatives of an SE nature and operate more like small enterprises such as tuck shops and domestic cleansings.

11. At present, co-operatives are registered with the Agriculture, Fisheries and Conservation Department (AFCD) under the Co-operative Societies Ordinance (Cap.33). Some have proposed that the Administration should review the Co-operative Societies Ordinance to facilitate the formation of co-operatives. Specifically, it has been suggested that the requirement to have a minimum number of 10 members and to re-invest 25% of their net profits into the co-operatives for further development should be relaxed.

12. The Administration is aware of the need to keep our regulatory framework relevant to the changing environment. In considering whether and how our regulatory framework can be improved to support SE/co-operative development, we need to consider the suitable regulatory framework for co-operatives which are both voluntary associations and business enterprises. The challenge is to have adequate protection of the interests of co-operative members and third parties, yet be flexible enough to accommodate the rapid changes in the society -

- (a) *Checks and balances*: The present regulatory framework for co-operatives adopts a "light touch" approach and relies on the self-regulation among member-owners and the check and balances within the co-operatives to protect the interests of its members, instead of adapting the regulatory requirements for companies. Relaxation of the membership and profit allocation requirements of co-operatives would affect this regulatory balance and may require new additional safeguard measures against possible abuses.

- (b) *Nature of regulatory framework:* The SE-type co-operatives operate more like business operations compared to the more traditional form of co-operatives. The question becomes whether a separate regulatory regime should be put in place for SE-type co-operatives, and if so, the suitable regulatory framework for such operations, taking into account the need to avoid unfair regulatory advantage over SMEs.
- (c) *Alternative regulatory framework:* Some co-operatives of a more enterprising nature may register as companies under the company law. Separately, a new form of companies, the Community Interest Companies (CICs), have recently been introduced in the U.K. which cater for the special needs of SEs. Some information on CICs is at **Annex B**. We need to consider the need to have a more modern legal vehicle to promote SE development in Hong Kong.

13. Given the above, it is uncertain whether moving piecemeal relaxation of the co-operatives requirements under the Co-operative Societies Ordinance (Cap.33) at present is the best way forward to facilitate SE development. We will conduct a technical examination with the relevant bureaux and departments on the issue, including assessing the impact of the relaxation of the existing co-operatives requirements on the regulatory environment for all types of co-operatives, the appropriate regulatory framework which can cater for the needs of SE-type co-operatives as well as SEs, as well as the applicability of the latest development overseas to Hong Kong. We will include the findings on the suitable legal framework to facilitate the operation of SEs in Hong Kong in the future in the report of the Commission due April/May 2007.

14. Separately, the HWFB has met some co-operatives to better understand their concerns, and understands that the main difficulties they face at present relate to business and financial viability, the need for training, business support and start-up assistance. The supporting initiatives (paragraphs 4 – 9 above) hopefully can address the concerns of the co-operatives.

ADVICE SOUGHT

15. Members are invited to note the progress of the initiatives to further encourage the development of SEs in Hong Kong, including -

- (a) training and business support (paragraphs 4 – 6 above);
- (b) facilitating SEs in the public procurement process (paragraphs 7 – 9 above);
and
- (c) exploring the suitable legal framework to facilitate the operation of SEs in Hong Kong in the future (paragraphs 10 – 14 above).

Commission Secretariat
January 2007

Facilitating Social Enterprises in the Public Procurement Process

PURPOSE

This note sets out the efforts of the Administration to facilitate the participation of social enterprises (SEs) in the public procurement process.

OBJECTIVE

2. The primary objective of public procurement is to secure, under a transparent and fair system, the delivery of goods and services with the best value for money which serve the needs of the community. The ultimate test is whether the bidders, be they SEs or for-profit enterprises, can deliver the types and quality of services required by the procuring agencies.

3. SEs which employ people from disadvantaged background have the potentials to bring additional benefits to the community through their participation in the public procurement process. Given their social objectives, SEs could help the Government meet more than one objective with roughly the same expenditure, i.e. training or work integration for the disadvantaged groups and the delivery of the required mainstream service at the same time.

APPROACHES

4. In facilitating SEs to participate in the public procurement process, we have adopted different approaches in handling SEs employing people with disabilities (“PWDSEs”), and those SEs which facilitate the work integration of “able-bodied” unemployed (“WISEs”) (paragraphs 5 - 9 below).

SEs Employing People With Disabilities (“PWDSEs”)

5. In the case of PWDSEs, procuring departments may give preferential treatment through the use of restricted tender or the award of additional weighting in open tender exercises. This is clearly permissible under the World Trade Organization Agreement on Government Procurement (WTOGPA)¹.

¹ Exceptions relating to the products or services of handicapped persons under Article XXIII of WTOGPA.

6. A number of non-government organisations (NGOs) have set up PWDSEs in recent years to create employment for people with disabilities through innovative business operation. The Social Welfare Department has relaxed the required ratio of disabled employees of the “Enhancing Employment of People with Disabilities Through Small Enterprise” Project (3E’s Project) from 60% to 50%. In addition, the 3E’s Project is extending the funding period from one to two years. These new measures will widen the scope of business types that PWDSEs can run, enhance their flexibility and sustainability, thereby creating more employment opportunities for people with disabilities.

7. Procuring departments may consider giving appropriate preferential treatment to PWDSEs which employ more than 50% of PWDs. Some public bodies have also given enhanced weighting to the employment of disabled persons when awarding contracts. For instance, the Hospital Authority (HA) has increased the weighting of the employment of disabled persons in awarding contracts from 5% to 10% of the total score since November 2005.

8. The Government would continue its efforts in enhancing the employability of PWDs and in facilitating PWDSEs to bid for public contracts by encouraging procuring departments and public bodies to make use of the restrictive tender mechanism, or to give them additional weighting in open tender exercises. PWDSEs will also be encouraged to take on PWDs as trainees in providing them with vocational training in real work settings, thereby enhancing their opportunities of seeking employment in the open market.

SEs Facilitating Work Integration of “Able-bodied” Unemployed (“WISEs”)

9. Unlike PWDSEs, our approach in facilitating the development of WISEs is not, and should not be viewed as a welfare policy initiative as this may be counter-productive in fostering its growth as a viable business option, and may cause unfair competition to small and medium sized enterprises. WISEs should not receive any special preference in the procurement process. The key is to provide a level playing field for SEs to compete and grow. This is also in line with the practice in the European Union and our obligations under the WTOGPA.

10. That said, we could encourage the development of WISEs through examining the way we commission public services, in recognition of the additional benefits such

SEs could bring to the community. Combining mainstream service delivery with training for disadvantaged groups requires innovative lateral thinking and joined-up approach in the public procurement process. As a first step, we propose to explore how we can better recognise the additional benefits WISEs can bring in terms of facilitating training and work integration of the unemployed alongside mainstream service delivery (paragraphs 11 – 13 below).

OPERATIONAL MODEL – FACILITATING WORK INTEGRATION

11. Helping the able-bodied unemployed to enhance their employability and to find employment is the ultimate way to help them move out of poverty. In this regard, the Government invests a lot of resources in the various vocational training and retraining programmes (\$4,721 million in 2004²). Studies have shown that training complemented by suitable placement opportunities would be more effective in helping the unemployed gain more work experience, and for those long-term unemployed, to adjust to the requirements of the mainstream labour market.

12. Other than providing subsidies for work trials in the private sector and offering placement opportunities in the public service, the Government may also explore achieving the training objective through the Government procurement process to facilitate the work integration of the unemployed. One possible operational model is for the Government to identify some contracts suitable for work integration of the able-bodied unemployed, and to require successful bidders to employ a certain percentage of the unemployed persons who have completed a relevant retraining programme offered by the Employees' Retraining Board (ERB). The tendering process is non-discriminatory - SEs and for-profit enterprises can bid for the contracts so long as they can deliver the required outcomes (e.g. quality of mainstream service, plus the number of trainees from recognised training schemes).

13. We are working with the ERB and relevant departments on a sample tender specification to facilitate cost-effective contract management. We will identify some small pilot contracts for the purpose of testing out the operational model in the first half of 2007. We also need to avoid selecting contracts which are more suitable to help enhance employability of the PWDs, and instead identify contracts which require a skill level commensurate with that of a semi-skilled able-bodied trainee.

² Detailed breakdown is at Annex F to CoP Paper 19/2005 "Assisting the Unemployed : Welfare-to-Work" for the meeting on 28 June 2005.

WAY FORWARD

14. The Administration would continue to promote a SE-friendly public procurement regime through the following direction -

- (a) continue to facilitate bidding by SEs employing PWDs (paragraph 5 – 8 above);
- (b) test out the operational model through pilot contracts in accordance with the approach set out in paragraphs 9 – 13 above; and
- (c) continue to promote the concept of SEs among those responsible for public procurement at both the central and district level, and remove any barriers and obstacles unique to SEs.

15. Besides the public sector, the NGO sector and the private sector also offer many procurement opportunities suitable for SEs. We should encourage such “caring procurement” among the NGO and private sectors which are potentially important partners of SEs. For instance, the Education and Manpower Bureau (EMB) has encouraged schools to procure services provided by SEs employing PWDs and those from disadvantaged backgrounds as and when opportunities arise. Given the relatively small-scale of SEs in Hong Kong at the moment, a fraction of the opportunities from the different sectors would greatly enhance the potential market and business viabilities of SEs.

16. Social and personal services are some of the areas where SEs may bring additional benefits to the community. However, we are mindful that most of such services are provided by NGOs. There may be little room left for adopting the proposed model under current funding/subvention arrangements

Community Interest Companies (CICS)

Social enterprises (SEs) can operate in different legal forms, as registered charities, in the form of companies, or as co-operatives. The U.K. introduced in 2005 a new type of companies, called the Community Interest Companies (CICs) (社會公益公司), designed specifically for those wishing to operate for the benefit of the community rather than for the benefit of the owners of the company. This provides a unique type of companies to facilitate SE development.

Background

2. The CIC concept was first raised in the U.K. in 2002. CICs are companies which are limited either by shares or by guarantee or limited by guarantee and having a share capital. They are subject to Part 2 of the Companies (Audit, Investigations and Community Enterprise) Act 2004 (which is a free-standing item of primary legislation quite separate from the Companies Act) and the Community Interest Company Regulations 2005, in addition to the general requirements applicable to ordinary companies under the U.K. Companies Act. In this respect, companies already formed and registered under the Companies Act as well as completely new companies can apply to become CICs. However, once they have been formed and registered as CICs, they are subject to the additional statutory requirements set out in the 2004 Act and the Community Interest Company Regulations 2005 as well as their existing statutory obligations under the Companies Act.

Special Features

3. The special features of CICs include a "community interest test" and an "asset lock", which ensure that the CICs are established for community purposes and the assets and profits are dedicated to these purposes.

4. The "community interest test", in gist, is whether a reasonable person might consider that the company's activities (or proposed activities) will be carried on for the benefit of the community. The criteria used are broader and more flexible than those used in the public interest test for "charities". In line with regulation of charities, a CIC cannot be formed to support political activities.

5. Limited companies that do not have charitable status may find it difficult to ensure that their assets are dedicated to public benefit. The statutory “asset lock” ensures that the assets and profits of a CIC are either retained within the CIC and used solely for the community purposes for which it was formed, or transferred to another asset-locked organisation such as another CIC or charity. The “asset lock” however does not prevent a CIC from using its assets for normal business activities, meeting its financial obligations or paying allowable dividends.

6. CICs limited by shares can pay dividends to individual shareholders, subject to a cap, but stakeholders in CICs will still have the assurance of community benefit provided by the asset lock.

7. CICs do not enjoy any special tax advantage over other companies by virtue of its legal form. However, they may benefit from other programmes for particular activities or regions. For instance, the Community Investment Tax Relief (“CITR”) gives tax relief to individuals and corporate bodies investing in Community Development Finance Institutions (CDFIs). These CDFIs then provide finance to qualifying profit-distributing enterprises, social enterprises or community projects in disadvantaged communities that are excluded from mainstream sources of finance.

Regulation

8. Registration of a company as a CIC has to be approved by an independent regulator (i.e. not the UK Companies House) appointed by the U.K. Secretary of State for Trade and Industry, who also has a continuing monitoring and enforcement role. The Government expects the Regulator to be a “light touch regulator” who will encourage the development of the CIC brand and provide guidance and assistance on matters relating to CICs.

9. The accounting requirements for a CIC is the same as those of other companies, but CICs have an additional obligation to prepare an annual community interest report to be filed with their accounts in order to enhance transparency of their activities.

Benefits

10. CICs offers an additional legal form for SEs to operate in - a non-charitable company form to conduct activities and operate more “commercially”, but with a clear

assurance of not-for-profit distribution status. The new and unique status also helps raise the profile of SEs. Nevertheless, SEs may choose to use other legal forms that suits the needs of their organisations best, and some may view the additional benefits from the legal form may not outweigh the additional complexity and regulatory requirements.

11. More information about CICs is available at <http://www.cicregulator.gov.uk> and <http://www.nearbuyou.co.uk/>.

Commission Secretariat
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