

# Financing Successful Social Enterprises: CDCs and Franchising

CDCs and their unique access to financing resources that could benefit the franchisor are well worth the effort.

By C. Everett Wallace



With each passing day, the number of non-profit organizations increases in this country. Their growth in the last two decades has been nothing short of phenomenal. At the same time, the sources of capital to support these charitable efforts have grown at a steady, but slower pace. In many instances, these nonprofit organizations, new and old alike, are turning to “social enterprises” as a means of diversifying their streams of revenue and to lessen their dependence on some sources that have begun to prove less reliable in today’s market.

## Blurring of the Line

This notion of developing social enterprises or “social entrepreneurship” by non-profit entities as a means of gaining earned income is not new. Andy Robinson, in his book *Selling Social Change (Without Selling Out)*, pointed out that “[t]he Girl Scouts have created perhaps the best-known example of nonprofit commerce. In 2000, Girl Scout volunteers (both children and adults) sold an estimated 250 million boxes of cookies. In terms of sales volume, Girl Scout cookies, taken as a single product, are reputed to be the number two cookie in America—and they are only available six weeks a year.”

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Robinson goes on to point out that over the years there has been a “blurring” of that bright line that used to separate non-profit from for-profit activities. Increasingly there are for-profit entities that have entered into the traditional domain of the not-for-profit sector. In numerous fields—health care, childcare, job training, education and so on—the

landscape has been dominated by for-profit service providers. These companies, with their attention to marketing, promotion and the bottom line have caused many non-profits to rethink their approach to service delivery and customer satisfaction. As a result, these groups are attempting to meet “a double bottom line” of both social mission and profitability. Many are responding to this “invasion” by becoming more business like in their operations and more entrepreneurial in their thinking.

On the other hand, more and more businesses are beginning to embrace the concept of the “double bottom line” as a driver for their operations and relationships. Groups such as the Body Shop and Newman’s Own have developed business models that not only achieve this double bottom line, but they have made this one of the central themes. The marketing, advertising, operations, customer and employee relations are all constructed on this premise. They all publicly proclaim the virtue of “profit with a purpose.”

As more non-profits have come to embrace the burgeoning field of earned income from social enterprises, the field has taken on a life of its own. The result has been a concatenation of organizations, consultants and institutes designed to assist these non-profits in determining the appropriate approach to this market. In fact, an increasing number of business schools have begun to offer certificates, and in some cases degrees, in the field of social enterprise.

Business consultants and social enterprises proponents Jerr Boschee and Jim McClurg, assert that “[a] social entrepreneur is any person, in any sector, who uses earned income strategies to pursue a social objective....” They go on to point out, “The culture of a traditional nonprofit, no matter how innovative, is vastly different from the culture of an entrepreneurial nonprofit. Entrepreneurs have a higher tolerance for risk, a greater appreciation of margins, and an eagerness to compete. Traditional

nonprofits distrust the capital markets, prefer collaboration to competition, and underestimate the productive capabilities of their disadvantaged employees. They watch other nonprofits become increasingly sustainable or self-sufficient, but are unwilling to emulate their practices.”

### Social Entrepreneurial Candidates

One group of nonprofits that are prime candidates for social entrepreneurship is community development corporations, or as they are more commonly known, CDCs. The National Congress for Community Economic Development is the national trade association for the 30,000 plus CDCs operating in the United States. The expressed purpose of these charitable organizations is to provide for economic development in some of the most economically-neglected areas of this nation. Innovation, creative thinking and risk-taking are the hallmark of these organizations. CDCs operate in a wide variety of communities—urban, suburban and rural. They are, by design, creatures of the communities they serve, with board members, staff and volunteers who are residents of these communities. They are uniquely positioned to work both for and with the residents’ and business interests located in their service areas.

## The CDC can be very instrumental in land assembly and site preparation.

Within the nonprofit community, CDCs are especially suited to embrace this growing field of earned income from social enterprises. In a previous article in this publication I discussed the synergy that created an opportunity for CDCs and franchisors in this field. Of critical concern is the ability of the nonprofit to identify, capitalize, manage and support a business venture. This has often proven to be a daunting task when a non-profit (or for-profit) is attempting to create a business on its own.

In a study prepared by the IFA Educational Foundation and Community Wealth Ventures, Inc. titled “Nonprofit-Owned Franchises: A Strategic Business Approach,” authors’ state:

“Franchising can represent an effective approach to mastering the complexities

of a small business. Franchise products and services frequently have been painstakingly developed and improved by the franchisor, and in most cases, they have succeeded in the marketplace. In addition, these businesses usually have developed an operating system that is clearly defined, carefully researched, and universally applicable. More importantly, franchisors often provide training and management assistance to their franchisees to help address common business problems that all small businesses encounter. As a result, franchising offers entrepreneurs tools that increase their likelihood of success.”

### Roles for CDCs

For many CDCs the role they can play in assisting in the recruitment and placement of a franchise in the neighborhoods they serve may vary. One area where CDCs can be especially useful partners is in accessing capital for franchise developments in their communities. Depending on the types of activities the CDC engages in their service area, they can provide support in a number of different areas.

The CDC can be very instrumental in land assembly and site preparation. The CDC may be able to work with its local unit of government to identify, purchase and improve a specific site that would be extremely beneficial to a given franchisor or to a prospective franchisee. In some instances this process may result in the land being offered to the CDC for a below-market price or for as little as \$1. The CDC can, in turn, convey the property to the franchisor or franchisee at a reduced price or, simply, work with the franchisor or franchisee to ensure that the business provides employment opportunities for residents of the neighborhood. This is that double bottom line referenced earlier.

Another way in which CDCs can play a role is as the developer of the property that will house the franchise business. In this instance, the CDC will serve as the landlord to the business and will receive ongoing payments in the form of rent.

The CDC could also provide training and or employees for the business and could perform this service as a fee-generating arrangement with the franchisor or franchisee. In some cases, the CDC may

be receiving funds from a federal, state or local program designed to provide employment for the hard to employ or other community residents who are in need of employment assistance. In many communities, the government agencies will contract with the CDC to provide training or will provide funds directly to the business for providing training and employment for these individuals.

Many CDCs can also provide access to below-market debt financing or subordinated debt from various governmental programs, foundations or private-sector financial institutions. These are usually dollars that are only available to non-profit entities such as CDCs that are engaged in community economic development projects. Often these funds are restricted to certain designated communities and require that a certain number of jobs be created in proportion to the number of dollars that are being used to assist the project. These funds can often turn a marginal project in an untested area into a strong candidate for the franchise.

The source of these funds varies from  
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### WHAT THE MEDIA IS SAYING

*Inc/Candee Wilde*

#### Are there special opportunities for U.S. veterans in the franchising business?

**As a matter of fact, there are.**

And these opportunities are easy for veterans to find through a special program called the Veterans transition Franchise Initiative, or VetFran, which was launched by the International Franchise Association (IFA) during the Gulf War.

To express their gratitude to those who serve in the armed forces, more than 100 IFA franchisor members agreed to create special financial incentives to help veterans invest in a franchise. The VetFran program allows veterans to acquire a franchise with a down payment of 10 percent or less of the initial franchise cost, which typically ranges from \$45,000 to \$150,000. The franchising companies absorb the difference. Nearly 150 franchisors are participating in the VetFran program today. ■

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community to community. Not all CDCs are eligible for these funds in their respective communities. The dollars are usually made available to the CDCs in one of two forms—grants and loans.

Grants dollars are usually made available from the following sources:

- Community Development Block Grants Program—Department of Housing and Urban Development
- Economic Development Initiative—Department of Housing and Urban Development
- Office of Community Service—Department of Health and Human Services
- Economic Development Administration—Department of Commerce
- Rural Community Enterprise Grants—Department of Agriculture
- Rural Community Development Initiative—Department of Agriculture

While many of these programs provide direct assistance from the federal agencies, several provided funding for state and local governments and they, in turn, will create programs that will regrant these funds to CDCs. (As this issue went to press, several of these programs were slated to be eliminated or consoli-

dated into a new program entitled “Strengthening America’s Communities Initiative.”)

## CDCs and franchisors have a symbiotic relationship.

On the other side of the ledger are loans, subordinated debt and equity programs that are available to CDCs. Some of the loan programs are made available through the grants that are provided to the cities and states under the Community Development Block Grant and other federal “entitlement” programs. But the CDC industry also has access to:

- Revolving Loans
- SBA 504 loans
- SBA 7(a) loans
- New Market Tax Credits
- Micro-loans Funds
- Capital Access Program
- Social Venture Equity Funds
- Quasi-Equity Funds (Franchisors United for Neighborhood Development (FUND))

### A Word of Caution

In the February 2005 edition of the Harvard Law Review, authors William Foster and Jeffery Bradach pointed out the following:

“Promoted in books and articles, conferences and courses, earned-income initiatives are becoming accepted—even expected—throughout the nonprofit world. In a 2003, Bridgespan Group survey of U.S. nonprofits’ executives, half of the respondents said they believed earned income would play an important or extremely important role in bolstering their organization’s revenue in the future.... Our analysis revealed that the relative contribution of program service revenue had actually declined by three percentage points over the ten-year period [1991-2001] and that such revenue remains heavily concentrated in health care and education. Outside those domains, earned income’s contribution grew substantially only among employment and community-improvement organizations. In environment and youth-development, it showed a marginal gain, while in arts, education, housing, recreation, and human services, it declined slightly.”

For franchisors, selecting the right partner in a social enterprise—like selecting the proper person as a franchisee can make all of the difference in the world. CDCs and franchisors have a symbiotic relationship. They both are interested in creating successful businesses that will improve the neighborhoods they are located in. They both are interested in a return on investment and on revenue generation. This is not to say that there are not differences in each organization’s approach to addressing the importance of achieving the double bottom line; rather, it is to say that they each have access to tools that can prove extremely useful in achieving their common goals. CDCs and their unique access to financing resources that could benefit the franchisor are well worth the effort. ■

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