Social Purpose Capital Markets:
Financial Capital for Social Entrepreneurs in Education

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Introduction

> *"We are not thinking our way into a new way of acting. We are acting our way into a new way of thinking."*
>
> \- Katherine Fulton, Monitor Group

On the outside of nearly every personal computer sold today is a sticker that says "Intel Inside," a reminder from semiconductor giant Intel that the "integrated circuits" its company manufactures are central to that computer's operation. These small silicon chips have tiny electric circuits etched onto their surface, and their existence has in many ways made possible the proliferation of personal computers, which have transformed the way we live and work. But it might not be so if a group of renegade engineers known as the "Fairchild Eight" hadn't jumped ship from their employer in 1957.

Frustrated by the dysfunctional management of Shockley Semiconductor Laboratory, the group met with a young East Coast investment banker by the name of Arthur Rock – who went on to become a successful venture capitalist and helped them raise $1.5 million from a local electronics company. Together with $500 from each of the founders, Fairchild Semiconductor was born, and went on to revolutionize the semiconductor industry. Along the way, Fairchild also helped to spawn a thriving Silicon Valley ecosystem, both as a company and as an incubator for talent. Gordon Moore and Robert Noyce, two of the founding eight team members, went on to create Intel (the source of those stickers on computers), while Eugene Kleiner started the legendary venture capital firm Kleiner, Perkins, Caufield & Byers, which has since provided funding to dozens of successful start-ups including Sun Microsystems, Amazon.com and Google. Before long, other start-ups in what was fast becoming known as "Silicon Valley" began raiding the company for well-trained managers and engineers, pointing the way toward the robust entrepreneurial ecosystem that exists there today.

Like the entrepreneurs who created Fairchild, educational entrepreneurs are in an undeveloped industry, where they must raise financial capital to turn their visions into new enterprises. In industries like technology and medicine, the capital markets available to help entrepreneurs start and grow their businesses have come a long way since the founding of Fairchild, as entrepreneurship has become more accepted and the ecosystem of capital providers has become more sophisticated. The conventional market for private capital is regulated by a number of agencies and operates in ways that have become standard, including a significant amount of uniform and transparent information, and a secure and reliable infrastructure that includes mechanisms like public stock exchanges. These structures and practices have encouraged the development of a wide array of independent intermediary organizations that provide expert analysis, and as a result, a significant and diverse number of capital providers have flourished.

However, for entrepreneurs addressing complex social issues like public education, the availability and structure of investment capital remains an enormous challenge that keeps many entrepreneurs from realizing their true potential and prevents the field from growing. This is particularly true for social entrepreneurs in education – those who are motivated first and foremost by the desire to improve educational access, equity, and outcomes for students who are not adequately served by the current system. These entrepreneurs strike out on their own, unencumbered by the restrictions of the current system, to create new organizations that can both provide students with better educational options and spark disruptive change within existing institutions.

We bring to this subject many years of experience in helping social entrepreneurs create and grow new organizations, most recently at NewSchools Venture Fund, a nonprofit venture philanthropy firm founded in 1998 by Kim Smith in collaboration with noted venture capitalists John Doerr and Brook Byers (of the aforementioned firm Kleiner Perkins Caufield & Byers). The firm's mission is to invest in both nonprofit and for-profit entrepreneurial education organizations and to connect their work to sytematic change in public education. NewSchools does this by aggregating capital from many philanthropic sources, identifying promising entrepreneurial solutions, and providing both significant capital (most investments range between \$1 and \$5 million) and hands-on guidance to a portfolio of organizations. This money and support is generally allocated over the course of several years according to various "milestones" of organizational progress, with senior members of the NewSchools team taking a seat on each investee's board and each bringing to bear many years of experience with entrepreneurial organizations.

Drawing on this experience, as well as our work with and as entrepreneurs in the business world, we will explore in this chapter what we call the "social purpose capital market" – the market of individuals and institutions that provide investment capital to these social entrepreneurs in education. These capital markets are the engines that enable such entrepreneurs to start their new organizations, acquire the necessary equipment, and grow organizations to a scale that begins to address the magnitude of need in public education. We will argue that this social purpose capital market for educational entrepreneurs is lacking many of the elements that make the conventional capital market work for entrepreneurs in other industries. Indeed, we believe that the social entrepreneurs in education who have succeeded to date have done so *in spite* of the current capital markets, rather than because of them. If we can agree that these social entrepreneurs are a potentially valuable mechanism for dramatically improving public education, then we must take action to alter the capital markets that are so vital to their success.

Entrepreneurs In Search of Capital

When a social entrepreneur decides to create a new organization, one of the first questions that he or she faces is whether to adopt a for-profit or nonprofit structure. This is one of the most important decisions a social entrepreneur must make, because most capital providers invest in only one or the other. As one of the few organizations that invest in both for-profit and nonprofit ventures, at NewSchools we have seen this decision-making process play out many times and watched many factors influence this decision, including the organization's business model, its theory of how it will create change, the political context, the status of the capital markets, and often the founder's personal preferences and beliefs.

For instance, Don Shalvey – who founded nonprofit charter management organization Aspire Public Schools in California – knew he wanted Aspire to be a nonprofit institution because he felt most comfortable leading and recruiting teams in the public-benefit sectors, and he believed that this structure would allow Aspire to consistently prioritize social impact without any possible conflicting financial motivations. Conversely, when Linda Chaput created Agile Mind to provide online access to Advanced Placement courses, she sought to create a for-profit company despite her explicit social mission to serve low-income communities. Like Shalvey, she was motivated by her past experience, but also knew that early-stage venture capital funds were available for such businesses and that she would need to offer stock options to recruit software engineers and the other employees necessary to build this Web-based resource.

Even when the entrepreneur is agnostic about corporate structure, the availability of capital, the specific business model or the political context may make the decision clear. For instance, technology-related ventures like Wireless Generation, a provider of innovative handheld assessment tools, that need to raise significant capital to develop their products and entice employees with stock options will often choose to be for-profit so that they can raise money from venture capitalists who understand this need. On the flip side, most for-profit education management organizations have avoided doing business in California because it is nearly impossible to earn a profit on the per-pupil funding the state provides to public schools, except in the rare cases where their work is supplemented by philanthropic funding. And on the political front, organizing by groups such as the Association of Community Organizations for Reform Now (ACORN) has led to broad mistrust of many for-profit providers in education.

Once the organization's corporate structure has been identified, the entrepreneur then turns to that sector's investors for the financial capital and other support needed to start and grow the enterprise.[1] All enterprises need four types of money:

1) *Start-up capital*, which allows the entrepreneur to hire a team, develop products and services, rent an office, buy supplies, and do all the other things that they need to do to get a new organization off the ground;

2) *Operating or working capital*, which begins to flow in once the organization is up and running, and usually comes in the form of revenue;
3) *Capital expenditures*, which are used for purchasing assets that depreciate in value over time, such as real estate or expensive equipment like laboratories; and
4) *Growth capital*, which is used to finance significant expansion of the organization.

The first, third and fourth types can together be referred to as "investment capital" because they come from outside investors or donors, who provide the capital in exchange for the creation of some sort of return (e.g. growth in the business, repayment of a loan, some sort of social impact on society, etc.) However, revenue will not be dealt with in this chapter because it is provided not by investors but more often by customers, or in the case of a publicly regulated industry like education, third-party payers who provide funds on behalf of customers (such as states reimbursements to charter schools for the services that they provide to students).

Investment capital can come from investors in the private, nonprofit, or public sector. When people talk about capital markets, they usually mean the conventional, private for-profit capital markets in which investors provide businesses with capital in the form of either equity (in which investors put their money into a public or privately held company, in exchange for an ownership stake) or debt (in which investors loan money to companies and expect to be repaid). This market is overseen by industry regulators like the Securities and Exchange Commission (SEC), as well as specialized industry groups like the Financial Accounting Standards Board (FASB). As former Federal Reserve chairman Alan Greenspan noted, "Our market system depends critically on trust – trust in the word of our colleagues and trust in the word of those with whom we do business."[2] Recent accounting scandals aside, this industry has a robust system of mostly trustworthy information sources and service providers that help both investors and entrepreneurial enterprises do business.

It is important to recognize that this market is not merely an organic system that naturally evolved into this form, but is rather a publicly regulated market that has been refined over time to increase trustworthiness and efficiency. A full description of the evolution of U.S. capital markets is beyond the scope of this chapter, but there are five elements that we feel make these markets function as well as they do – elements that will be instructive when we consider the challenge of the social purpose capital markets for educational entrepreneurs:

1) General agreement on the *metrics and definitions* of success, including common methods for calculating a business's profits and losses;
2) Transparency, uniformity and availability of *performance data*;
3) A *robust ecosystem of independent intermediary organizations* that provide expert analysis;
4) A *secure and reliable infrastructure* including mechanisms like public stock exchanges, where any investor can buy and sell securities, as well as legal enforcement tools such as contract and property law, the oversight of the SEC, and the criminal and civil court systems; and
5) A *large and diverse supply of capital providers***,** each of whom has a different preference for the amount of investment risk that they are willing to take on, the type of financial return that they seek on their investments, the types of investment tools that they use, and the stages of companies that they will invest in.

The nonprofit capital market operates much differently. Donors – whether foundations or individuals – are given a public subsidy in the form of a tax deduction to encourage them to provide funds to organizations that produce some sort of public value. The vast majority of investment activity takes place in the form of grants. Internal Revenue Service (IRS) regulations dictate that 5 percent of the endowment assets of a foundation must be distributed, whether to grantees or as administrative expenses, each year; the remaining 95 percent of assets are generally invested in the conventional capital markets so as to maximize financial return and keep the foundation going. The philanthropic capital market is loosely regulated and enforced by the IRS and by states' attorneys generals, but most regulations were established primarily to prevent fraud and the misuse of these tax-advantaged philanthropic funds for personal benefit or political advocacy. There have been comparatively few attempts made to put in place the kind of practices, transparency of information, or intermediaries that make the for-profit capital markets so efficient.

Finally, although a significant amount of money does flow through the public sector, little of it takes the form of investment capital. When federal, state, or local governments do provide funds to entrepreneurial organizations, it is less often as direct investments, and more often as investment incentives, such as tax credits, that are designed to motivate investors to take action in an underserved area or industry.

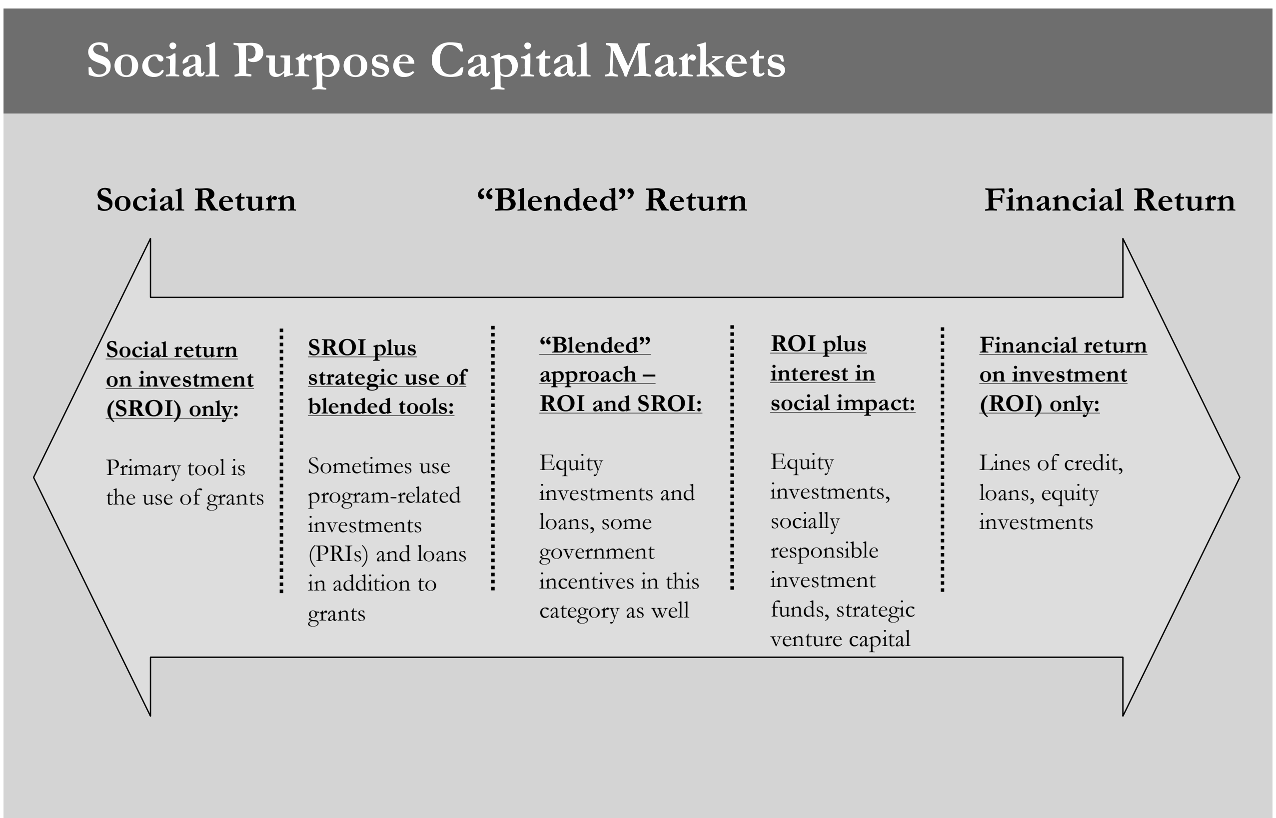
Social Purpose Capital Markets and Education

Since we have limited the focus of this paper to the capital markets for social entrepreneurs in education, it is worth turning our attention to the narrow slice of the capital markets that serve them. We refer to these as the social purpose capital markets, and they include a variety of individual and institutional investors from across the public, private and nonprofit sectors.

Many of these investors have different expectations for the kind of value that their investments will create. One of the most common and straightforward measures is the return on investment

(ROI), in which a financially motivated investor compares the number of dollars spent or contributed with the dollars generated. But many investors who back social entrepreneurs intend to calculate a social return on investment (SROI), which is a far more slippery notion than the counting of dollars and cents that essentially boils down to: "for each dollar invested, what is the resulting benefit to individuals and to society?"[3] For example, the longitudinal High/Scope Perry Preschool Study – which has studied the short-term and long-term benefits of a Michigan preschool program – has found that the program returns to the public roughly $7 for every dollar spent to operate the program, given the higher level of schooling completed by the preschool's attendees, their need for fewer social services, their greater job earnings, and the like.[4]

Figure I: Social Purpose Capital Markets



As Figure I indicates, at one end of the spectrum are investors that are motivated entirely by social impact. These include nearly all conventional endowed foundations that support education, from older foundations like the Hewlett Foundation to newer players like the Bill and Melinda Gates Foundation and the Broad Foundation. University of Arkansas professor Jay Greene has estimated that, in 2002, private philanthropies gave only about $1 to $1.5 billion to K-12 schooling, which was less than .03 percent of the $388 billion spent by taxpayers that year on K-12 education.[5] Of that, it is impossible to calculate just how much went to support educational entrepreneurs – as opposed to school districts or other established entities – but we project that it was a small fraction. The primary nonprofit supporters of social entrepreneurs in education are listed in Figure II.

As noted earlier, individual donors and foundations have a remarkable degree of flexibility in how to use their funds. This is intended to enable philanthropists to take early-stage risks with important innovations that can later be taken up by the public sector, such as the Carnegie Foundation's work with public libraries back in the late nineteenth century or the Walton Family Foundation's early support of charter schools in the early 1990s. However, this flexibility sometimes results in philanthropic funding decisions that are idiosyncratic and ideological. Each nonprofit funder has a distinct organizational personality – often informed by the wealthy individual or family whose money endowed the foundation and how they achieved their success – which affects both *what* they will invest in (such as whether they are for or against school choice), as well as *how* they invest (size of grants, level of engagement with grantees, length of grant cycles, anticipated scale of impact).

Generally, most philanthropic funders prefer to invest in specific programs that nonprofits operate, rather than in the general operating expenses that a nonprofit incurs. "Different funders are interested in different things," explained one entrepreneur. "So, you have to pull your organization apart in various puzzle pieces and then sell each one to the funder who cares about that piece. In the end, you put the puzzle together with a whole variety of different funders, all of whom want something a little different and feel they are supporting something different and important." Foundations also tend to give out a large number of small grants that are short-term in scope, and as a result, spend a great deal of time managing the details of selecting and overseeing grants, rather than deeply engaging with grantees in a long-term way.

Figure II: Nonprofit Providers of Capital in Education

ORGANIZATION	BACKGROUND
National Foundations	
Bill & Melinda Gates Foundation *www.gatesfoundation.org*	**Founded:** 2000 **Structure:** 501(c)(3) private non-operating foundation **Assets:** $30 billion (2005) **Investment Focus:** First wave invested primarily in "inside" systems change, second wave was increasingly co-opetition combining inside and outside change agents. New leadership in August 2007 may affect focus.
The Broad Foundation *www.broadfoundation.org*	**Founded:** 1999 **Structure:** 501(c)(3) private non-operating foundation (spun out operating organizations include The Broad Center for the Management of School Systems). **Assets:** $836 million (2005) **Investment Focus:** Majority of investments are leadership for "inside" change agents, mostly districts. (Some data, competition, and charter CMO grants).
Doris & Donald Fisher Fund *(formerly Pisces Foundation, no website)*	**Founded:** 1998 **Structure:** 501(c)(3) private non-operating foundation **Assets:** unknown **Investment Strategy:** Funds K-12 public education reform efforts with particular emphasis on charter school movement (including schools, human capital and policy/advocacy) and social entrepreneurs, notably the Knowledge is Power Program (KIPP) and Teach For America.
William and Flora Hewlett	**Founded:** 1966

Foundation *www.hewlett.org*	**Structure:** 501(c)(3) private non-operating foundation **Assets:** $7.3 billion (2006) **Investment Focus:** Long term institutional and field development in education reform, improved instruction, and access to technology (large effort in open-source educational content).
Walton Family Foundation *www.waltonfamilyfoundation.org*	**Founded:** 1988 **Structure:** 501(c)(3) private non-operating foundation **Assets:** $1.3 billion (2005) **Investment Focus:** Strong free market theory of change including charter schools and vouchers.
Michael & Susan Dell Foundation *www.msdf.org*	**Founded:** 1999 **Structure:** 501(c)(3) private non-operating foundation **Assets:** $1.2 billion (2005) **Investment Focus:** Data systems, human resources, leadership development and charter school organizations
Tiger Foundation and Robertson Foundation *www.robertsonfoundation.org*	**Founded:** 1996 **Structure:** 501(c)(3) private non-operating foundation **Assets:** $659 million (2005) **Investment Focus:** Entrepreneurial change from within as well as with charter schools, primary focus on New York City.
Regional Foundations	
Hyde Family Foundations *www.hydefamilyfoundations.org*	**Founded:** 1961 **Structure:** 501(c)(3) private non-operating foundation **Assets:** $131 million **Investment Focus:** Revitalization of the city of Memphis, with focus on entrepreneurial human capital and inside change as well as charter schools.
Robin Hood Foundation *www.robinhood.org*	**Founded:** 1988 **Structure:** 501(c)(3) public charity **Assets:** n/a, $83.5 million in grants (2007) **Investment Focus:** Poverty in New York City through four programs, including two related to education (Early Childhood & Youth, Education). Entrepreneurial education grantees include Achievement First, Building Educated Leaders for Life (BELL), Uncommon Schools, Urban Assembly.
Intermediary Financial Organizations	
NewSchools Venture Fund *www.newschools.org*	**Founded:** 1998 **Structure:** 501(c)(3) public charity **Assets:** $100 million raised to date. Current fund roughly $50 million. **Investment Focus:** Highly engaged venture philanthropy; invest only in educational entrepreneurs (both for-profit and nonprofit); large investments in CMOs and entrepreneurs who serve both district and charter systems with human capital programs and data tools.
New Profit, Inc. *www.newprofit.com*	**Founded:** 1998 **Structure:** 501(c)(3) public charity **Assets:** $5.9 million (2005) **Investment Focus:** Social entrepreneurs in the non-profit sector to build scalable organizations that will create a lasting impact on society.
Chicago Public Education Fund	**Founded:** 2000

www.cpef.org	**Structure:** 501(c)(3) public charity, intermediary **Assets:** $8 million (2006) **Investment Focus:** Educational entrepreneurs working in Chicago-area schools, as well as in-district initiatives.
Venture Philanthropy Partners *www.vppartners.org*	**Founded:** 2000 **Structure:** 501(c)(3) public charity, intermediary **Assets:** $17.9 million (2006) **Investment Focus:** Washington, D.C. region.
Charter School Growth Fund *www.chartergrowthfund.org*	**Founded:** 2005 **Structure:** 501(c)(3) public charity, intermediary **Assets:** $35 million (2006) **Investment Focus:** Charter school entrepreneurs growing organizations to large scale.

At the other end of the spectrum are investors whose goal is financial return on investment (ROI) but whose capital is sometimes available to some social entrepreneurs in education. These profit-seekers may be willing to provide funds to for-profit companies or to give out loans or lines of credit for mature charter management organizations. Because of their explicit focus on financial return, these investors consider only an organization's financial viability and potential profitability, rather than its mission or social impact. Traditional lenders like Wells Fargo and Bank of America fall into this category, as do traditional venture capital firms such as Arcadia Partners that seek to make money by investing in start-ups in the education sector.

The size of this financially-motivated market pales in comparison to philanthropic support. For example, in 2005, venture capital investors funneled just $64 million into preK-12 businesses, according to market research firm Eduventures, Inc. That is trivial compared with the $1.5 billion in philanthropic support that flowed into K-12 education that year, not to mention what venture capitalists put into entrepreneurial organizations in healthcare: more than $7.2 billion, according to healthcare market research firm Irving Levin Associates – more than 100 times the amount invested in K-12.

Unlike foundations, the method for selecting for-profit investments is somewhat standardized across venture capital firms and other private investors, regardless of industry. They assess the market, the product or service, the financial model and most importantly, the team, using a relatively standard model of due diligence that they can apply across a wide variety of companies.[6] The investors who support these start-ups also tend to be professional investors whose job it is to serve on their ventures' boards so as to be engaged in helping the companies develop. They often work together to increase the amount of upfront support that the entrepreneurial organization receives while decreasing the burden on the entrepreneur, by combining their efforts as a "syndicate" that provides coordinated funding all at once. According to George Overholser, a founding executive at consumer finance company Capital One who now runs the nonprofit investment firm NFF Capital Partners, "Investing growth capital is a tricky business – it requires a lot of predictions, a lot of judgment and a lot of due diligence. And due diligence is expensive. One of the benefits of writing large checks – and of forming syndicates – is that we can afford to conduct due diligence in an in-depth way."

Because of this high engagement in ventures, venture capitalists tend to invest significant amounts of capital upfront (an average of $3.8 million per early-stage deal[7], compared with an average foundation grant size of $125,000 in 2005[8]). As such, for-profit entrepreneurs are generally able to raise all the initial investment capital that they need from just a handful of investors. These investments are allocated toward general operating purposes of the company, and thus the entrepreneur can use it as he or she sees fit to develop the organization. For example, Aaron Lieberman is an entrepreneur who has raised nearly $2 million in early-stage funds for his for-profit preschool management firm Acelero Learning, all of which has come from just three investors. This compares with at least 20 individual and institutional donors from which he had to raise funds to start Jumpstart, a nonprofit focused on the same market, back in 1993. The flipside to these larger amounts of investment capital is that a typical venture capital investor is often in hot pursuit of the fastest path to "exit" – either an initial public offering (IPO) on the public stock market, or an acquisition or merger with another company – which often leads them to prioritize rapid growth in revenues rather than long-term, sustainable quality. This can be difficult or even disastrous for a social entrepreneur in the public education space, where it takes time and patience to develop a strong company.

Increasingly, the middle of the spectrum is expanding, as more investors choose to include some social preferences in their investment decisions, and some philanthropic organizations are more open to utilizing loans or for-profit tools like equity investments. Some blended value investors[9] focus on generating economic activity in a specific state or region, such as Pacific Community Ventures, which is a development venture capital fund located in northern California that seeks financial returns but invests in businesses that employ low-income workers.[10] Other blended value firms partner with banks to meet federal Community Reinvestment Act requirements that mandate financial institutions to provide a certain level of investment in low- and middle-income communities where they operate businesses.

For example, JPMorgan has spun off the Bay Area Equity Fund, a $75 million venture capital fund raised from traditional sources – major banks and insurance companies, foundations, corporations and private individuals – to invest in "companies that can deliver market-rate venture capital returns while enabling social and environmental improvement in the San Francisco Bay Area's low and moderate income neighborhoods." Within education, the fund has invested (along with NewSchools) in Revolution Foods, a for-profit company that provides healthy meals to local schools at a reasonable cost. NewSchools is also in this blended middle zone, as a philanthropic investor that clearly prioritizes an organization's social mission but makes strategic use of financial instruments like equity investments and loans where appropriate. Figure III shows the small group of relevant investors who support for-profit entrepreneurs in education.

Figure III: Providers of For-Profit Capital for Education

ORGANIZATION	BACKGROUND
Geographically focused firms that have made at least one investment in education	
Bay Area Equity Fund (JPMorgan) *http://www.bayareafamilyoffunds.org/funds/baef.shtml*	**Founded**: 2003 **Assets**: $75 million **Mission**: Double bottom line investor. Invests primarily in technology, health care, consumer products, clean tech. **Education investments**: Revolution Foods, organic healthy food for Bay Area schools.
Boston Community Capital *http://www.bostoncommunitycapital.org*	**Founded**: 1985 **Assets:** $70 million (2006) **Mission**: Social purpose investor; loan fund invests in housing, community facilities, and social services; venture fund invests in product and service companies. **Education investments**: Acelero Learning; management tools for Head Start programs; loan recipients include Jumpstart.
Pennsylvania Early Stage Partners *http://www.paearlystage.com*	**Founded:** 1997 **Assets:** $239 million **Mission:** Prioritizes financial returns, focuses on technology and life sciences companies, some funds required to be invested in Pennsylvania-based companies. **Education investments:** LearnNow, education management organization (sold to Edison Schools).

Financially motivated investors with industry focus on education	
Knowledge Universe *http://www.knowledgeu.com*	**Founded:** 1996 **Assets**: unknown **Mission:** Michael Milken founded to invest in cradle to grave education ventures (not focused on underserved communities or public education). **Education investments:** LearnNow and Charter Schools USA, primarily weighted toward consumer market products like LeapFrog and higher education and training services.
Knowledge Investment Partners *http://www.kiplp.com*	**Founded:** 2002 **Assets:** $200 million **Mission:** Invests in education and knowledge businesses through two hedge funds and a private equity fund. **Education investments:** Eduventures, Schiller International University.
Quad Partners *http://www.quadventures.com*	**Founded:** 2000 **Assets:** $200 million **Mission:** SBIC support for ventures serving mixed or low income communities motivates some venture selection. **Education investments:** Teachscape, Platform Learning.
Socially motivated investors that make for-profit investments	
NewSchools Venture Fund *http://www.newschools.org*	**Founded:** 1998 **Assets:** $100 million raised to date **Mission:** Public charity venture philanthropy firm, acts as value-added intermediary between individuals/institutions and K-12 educational entrepreneurs. **Education investments:** For-profit investments include LearnNow (sold to Edison Schools), Teachscape, Carnegie Learning, Revolution Foods.
Raza Development Fund (RDF) *http://www.razafund.org*	**Founded:** 1998 **Structure:** 501(c)(3) public charity (community development lending arm of the National Council of La Raza) **Assets:** $50 million School Building Fund developed with Citibank's Community Development Division **Education investments:** Provides loans, financing and lease guarantees for charter schools that serve Latino and other minority students; recipients include Bronx Charter School for the Arts.
Self-Help *http://www.self-help.org*	**Founded:** 1980 (venture fund established in 1984) **Structure:** 501(c)(3) public charity **Assets:** Unknown; $85+ million in loans issued to date **Education investments:** Provides loans to charter schools in low-income areas with facility financing needs over $2 million; recipients include KIPP Gaston College Prep.
Other	
Ascend Ventures *http://www.ascendventures.com*	**Founded:** 2001 **Assets:** $150 million under management (2007)

	Mission: Venture capital firm that invests in early-stage technology companies that are minority- and women-owned. **Education investments:** LearnNow (education management organization), Platform Learning (supplemental education services), SchoolNet (data tools for districts and states).
Commons Capital *http://www.commonscapital.com*	**Founded:** 2000 **Assets:** Unknown **Mission:** Double bottom line investor, invests in early-stage companies that promote a sustainable economy and address major social and environmental problems. **Education investments:** Apex Learning.

Finally, despite the public sector's role in holding public schools accountable and providing ongoing operating funds to existing schools, it provides very little investment for social entrepreneurs. For example, in 2007, the federal government allocated $214 million to charter school start-up grants and another $36 million to a program that enables charter schools to obtain more affordable facilities loans.[11] This $250 million investment in helping to create new public schools amounts to less than one half of one percent of the U.S. Department of Education's $68 billion budget for the year.[12]

Changing this dynamic is essential to the continued growth of entrepreneurial organizations in education. One powerful example of public support for developing supply is the way that the federal government has approached the market for low-income housing, stimulating demand by providing Section 8 vouchers ($15 billion worth in fiscal year 2007) while also offering investment and tax incentives for investors and developers to work together and create an additional supply of low-income housing (approximately $5 billion in annual budget authority for the Low-Income Housing Tax Credit). In fact, the low-income housing market has also been bolstered by public sector intervention into the housing market as a whole. The private mortgage company Fannie Mae, for instance, was originally established as a governmentally chartered organization to expand the flow of mortgages to home buyers at low rates, and the establishment of the Government National Mortgage Association (GNMA or "Ginnie Mae") made it possible for the fragmented local lending industry to pool loans into a new class of assets called "mortgage backed securities" that could be sold to other investors, thereby helping to standardize the mortgage industry nationally (creating a $6 trillion a year industry).

The federal government also invests over $28 billion annually in the National Institutes of Health (NIH) to support medical research that ultimately helps the biotechnology and pharmaceutical industries with innovation that can later be commercialized[13] – a figure that Larry Berger and David Stevenson note in their chapter is 100 times more than the Institute of Education Sciences' $260 million. Another interesting example of a public policy intervention that affected the capital markets was the revision of the Employee Retirement Income Securities Act (ERISA) in 1979, which dramatically increased the pool of venture capital funding by allowing public pension funds to invest in venture capital funds. By 1983, the value of commitments to venture capital had soared from $200 million annually before the regulations were changed to more than $5 billion per year.[14]

The increased involvement of the public sector is particularly important given how daunting public education is as an investment arena. In the late 1990s, NewSchools saw an increasing number of traditional venture capital firms willing to take on education investments, only to see them later begin to steer clear of the industry after discovering how slow the sales cycle is for companies selling products or services into districts, not to mention the industry's political volatility and the sheer lack of demand for higher quality products by education consumers.

Meanwhile, for philanthropic funders, the significant funding needed to get entrepreneurial education ventures to scale is daunting in comparison to the smaller grant size with which they are comfortable. This dynamic is changing somewhat, thanks to an influx of new education-focused foundations and individual donors willing to think entrepreneurially, but the field of social purpose capital is still very small. This sometimes leads entrepreneurs to contort their business model to cater to prospective investors. One entrepreneur went so far as to say "some funders think they have hired you to work for them when they fund you." (In fact, this small-world dynamic is why most of the entrepreneurs I spoke with for this paper declined to be identified.) For example, one well-known foundation recently put significant pressure on a nonprofit to dramatically change its growth plans – in terms of both pace and geographic locations – to meet the foundation's own priorities, in exchange for funding. The organization ended up declining the offer, but that discipline is hard to maintain in the face of a multi-million dollar check and few alternative funders.

Making the Social Purpose Capital Markets Work for Educational Entrepreneurs

Although the conventional capital market in the United States is far from perfect, it is relatively well-developed and efficient, and therefore can provide a helpful framework for considering how the social purpose capital markets might be improved in a way that better supports social entrepreneurs in education. As mentioned earlier, this includes all three sectors –public, private, and nonprofit – but because the lion's share of funding for social entrepreneurs still comes from foundations, the weight of our observations will focus there.

To recap, we identified five main forces that make the conventional capital markets hum: general agreement on the *definitions of success*; transparency and uniformity of *performance data*; a robust ecosystem of *independent, expert intermediary and advisory organizations*; a secure and reliable *infrastructure*; and a *large and diverse supply of capital providers*. Considering the strengths and shortcomings of the social purpose capital markets in this light will help illuminate areas of opportunity for investors and policymakers who wish to better the odds of success for educational entrepreneurs.

Definitions of Success

In traditional capital markets, it is clear how to "keep score" because success is defined as maximizing shareholder value, which is calculated in dollars. This simple metric allows the rest of the system – information, services, and regulations – to function in reasonable alignment. In public education, the definition of success is highly complex and incredibly political, leading to significant problems for the social purpose capital markets, which after all place their money in social entrepreneurs with the expectation that some sort of value will be created. There are two primary types of confusion: the first, and most troubling, is the lack of clarity on what we mean by success in education, and the second is how to balance organizational sustainability with social impact.

The question of defining educational success is a complex one. What constitutes a successful student – one who graduates from high school, one who enters college, one who finds a fulfilling career, one who becomes a productive citizen? About which students exactly are we talking? At minimum, the move toward state standards and greater accountability has led to greater attention toward *outcomes* in place of an earlier focus on *inputs and processes*, which has opened the doors for entrepreneurs to innovate with different approaches for accomplishing improved outcomes. This very idea is still under attack by some defenders of the status quo, and there is still plenty of disagreement around priorities (e.g. should we focus on adequacy to ensure low-income students do not fall between the cracks, or address our most talented students so we stay economically competitive?) and means (e.g. should we provide more funding to back-to-basics curricula, or focus on more progressive pedagogical approaches?). Overall, this market-wide disagreement over what success looks like and what metrics should be used to quantify the value created by a school (or entrepreneurial organization) has created a volatile system in which laws and regulations shift with the political winds, frightening off for-profit investors and doing little to focus philanthropic funding in a coherent direction.

Even when funders generally agree on educational goals, there is still a tremendous amount of disagreement over how to balance those with organizational metrics like profits or the ability for the organization to remain a going concern. For instance, when NewSchools first considered a grant to nonprofit principal preparation program New Leaders for New Schools in fall 2000, our investment advisors initially encouraged us to ask founder Jon Schnur to charge districts and schools a fee for each principal that they placed. This was commonsense to our investment advisors, most of whom have a business background and thus emphasize the ability of an organization to generate enough revenue quickly to become sustainable.

However, both NewSchools' and New Leaders' teams were concerned that its new model – which demanded that partner districts provide their principals with greater autonomy than they would otherwise enjoy – would fail to gain traction with districts if it also charged this fee up front. Ultimately, NewSchools and New Leaders agreed that they should forego the fee in the early years while its principals proved their merit, and today the nonprofit's program has become so sought-after that prospective district clients agree to raise half the cost of training the principals. The organization had to wrestle with the fine balance between social impact and financial sustainability, opting to place some of its early emphasis on the former in the hopes that success would manifest as more revenue down the line.

What would improve clarity on metrics for success, and thus help this market better align investment behind social entrepreneurs? Unfortunately, there may always be fundamental inefficiencies in this capital market because the definition of educational success will inevitably involve value judgments that purely financial markets can largely avoid. If industry-wide agreement on the definition of educational success is impossible, it is at least important for investors and entrepreneurs to be as clear as they can about their own goals and how they will measure them. For example, the Bill & Melinda Gates Foundation has developed its own clear idea of success: college readiness. The foundation's grants are measured against that benchmark, which has allowed them to hold their grantees to a tangible standard while also allowing them to continue refining what elements lead to college readiness.[15]

Performance Data

> It is disquieting that philanthropists have access to so little of the kinds of information that private investors rely on," says Paul Brest, President of the Hewlett Foundation. "[Private] investors can make use of a broad array of data, ranging from reports of quarterly earnings statements to the historical and current prices at which stocks are traded – all based on standards that are consistent across many industries, markets, and countries. Based on this information, investors can put together portfolios that are aligned with their investment horizons and tolerance for risks. And at the end of the day, or quarter, they will know their actual returns.[16]

Brest is right; it is frustrating for social purpose investors and donors to have so little access to useful, comparable data that they can use to make funding decisions. There are three main types of data that are lacking: achievement data, organizational data and financial data.

Achievement Data. This is a deeply rooted problem in education, where educators themselves are only now beginning to become comfortable with using data to inform their instructional decision-making. There have been some encouraging efforts. An increasing number of states are investing in student-level data systems with unique student identifying numbers that will enable them to track over time how an individual student, class or teacher is doing, and adjust interventions accordingly. And efforts like the for-profit Grow Network (now owned by publisher McGraw Hill) and SchoolNet offer tools that schools and school systems can use to track and monitor achievement and other data. Online tools like GreatSchools.net and SchoolMatters.com have both helped make publicly available information about schools and districts easier to access and understand. While these improvements have increased the availability of achievement data within districts and states, it remains difficult to draw comparisons across them or to understand what exactly is behind these differences.

To address this dearth of uniform achievement data, all three sectors must invest in more of the technological tools that make it easy for public school systems to collect, analyze, report, and act on student-level and program data. Such tools would help both entrepreneurs and their investors understand what is happening, what is working, and what approaches are leading to more value. Another tactic that might very well enable more comparable data comparisons is the adoption of national standards, which would allow investors (along with other stakeholders) to compare results across states and systems. This is a complicated political challenge, but it is clear that entrepreneurial education organizations of varying sorts have spent an inordinate amount of time, energy and money to align programs to different state standards of highly varying quality—and that is energy that could have been better used to serve students.

Organizational Data. In addition to addressing academic data, investors require better access to organizational benchmarks for elements like program design, staffing, and costs. The Center for High Impact Philanthropy at the University of Pennsylvania is one early effort to provide this service for donors. Executive director Kat Rosqueta explains:

> What's really needed is reliable information on the impact and cost-effectiveness of the kinds of activities a philanthropist could fund. Some of this information does exist, but it's locked up in academia, in the gray literature that foundations and policymakers use and generate, and in the heads and experiences of 'experts,' practitioners, and clients. Unfortunately, these are all sources that are inaccessible or unintelligible to the vast majority of philanthropists.[17]

Financial data. In the nonprofit sector, financial reporting is often presented in an inconsistent way that is less than useful to funders, especially those interested in helping organizations grow to a significant size or achieving a level of sustainability that decreases their dependence on philanthropy. For example, nonprofits do not account for their growth capital separately from their general operating revenue, and thus "relatively few donors and foundations are willing to provide money for growth because it is difficult to track what their money accomplishes," says George Overholser of NFF Capital Partners. For example, he notes that if the $18 million that his organization helped raise for youth employment nonprofit Year Up were put toward annual operations, it would allow for an additional 818 young people to be trained. But if that same $18 million were used to cover operating losses while the organization expands to the point where its revenues cover its expenses, that same money would allow the organization to serve 1,100 more young people each year thereafter.[18] Yet this kind of distinction in types and uses of capital in nonprofits is quite rare. This sort of sophistication will need to become more widespread to persuade more investors to support growth investments.

Independent Intermediary Organizations

In the private capital markets, a variety of independent intermediary organizations help to make the flow of capital and information more effective and efficient. Some of these intermediaries trade in knowledge and information, such as bond rating firms, equity analysts and consulting firms, while others specialize in funneling investment funds, such as venture capital firms and investment banks. Because the private capital market is so large and diverse, these intermediaries develop valuable expertise in particular types of investments, categories of capital providers, or spheres of information, allowing them to add value to the space between an investor's capital and an entrepreneur's business. Of particular value are independent intermediaries because they provide information and services free of conflicts of interest. For example, a certified financial advisor that is employed by a bank may try to sell his or her clients money management services, whereas an independent advisor is more likely to provide unbiased guidance.

Because the social purpose capital market in education is young and growing, there are still a limited number of these independent intermediaries and advisors, and fewer still who are focused explicitly on education. Thanks to the influx of philanthropic capital into the market over the last 5 years, several consulting firms have begun to engage with entrepreneurial clients, including the for-profit Parthenon Group and the nonprofit spin-off of consulting giant Bain & Company, The Bridgespan Group. As far as we can tell, there is still just a single organization, Eduventures, Inc., that provides investment analysis of the K-12 and post-secondary education market, allowing investors to track industry trends. Beyond education, a variety of philanthropic advisory firms – including the Center for High Impact Philanthropy mentioned above – provides tools, services and advice to individual and institutional donors. And groups like the Investor's Circle bring together individual investors who are socially motivated to help increase each member's awareness of possible investments and give them a peer group of potential co-investors.

In the private sector, investment intermediaries help add value to the funds that they aggregate by specializing in a particular type or stage of investment. Larger investors, such as pension funds or banks, choose to support intermediaries like venture capital firms because they know that they cannot themselves be experts at everything. For example, the National Venture Capital Association describes venture capitalists as firms that "finance new and rapidly growing companies; assist in the development of new products or services; add value to the company through active participation; take higher risks with the expectation of higher rewards; and have a long-term orientation."[19]

Such specialized investment intermediaries are still relatively rare in the social purpose capital markets. Ten years after our founding, NewSchools is still the only firm that focuses exclusively on social entrepreneurs in education and across both the for-profit and nonprofit sectors. This focus allows us to connect entrepreneurial leaders, track patterns and opportunities over time, and presumably to add value to social entrepreneurs' organizations and also to our donors. Other investment intermediaries have developed their own specializations: New Profit focuses broadly on social entrepreneurs across many fields and partners with consulting firm Monitor to provide consulting and coaching to entrepreneurs in their portfolio; Venture Philanthropy Partners in Washington, D.C. focuses on social entrepreneurs within a limited geographic area; and the Charter School Growth Fund focuses exclusively on charter school organizations across the country that are growing to scale. Despite their differences, all of these intermediaries prioritize social impact, aggregate capital from diverse sources to provide larger and longer term grants, and focus on helping social entrepreneurs grow their organizations.

A few new firms have also emerged to help social entrepreneurs in their quest for growth funds, including the previously-cited NFF Partners, founded by George Overholser within the Non

Profit Finance Fund, and SeaChange Capital Partners, which was created by two former Goldman Sachs partners with a $5 million initial contribution by Goldman Sachs itself. These organizations perform extensive due diligence to choose nonprofits that are poised for growth, present the opportunity to their network of donors, and raise capital from those donors. As NFF describes it, "without major restrictions and with an expectation of return measured by social impact." This approach has helped NFF Partners raise more than $40 million for two education nonprofits, College Summit and Teach for America.

On the for-profit front, there are fewer such intermediaries who focus on social entrepreneurs in education, which means that those social entrepreneurs who choose to create for-profit businesses are hamstrung by a lack of early-stage investment capital and often must seek such funding from individual or "angel" investors. As such, there is a significant need for more investing intermediaries willing to take on early-stage, high-risk, for-profit education investments in the way that venture capitalists have embraced healthcare and technology.

In the near term, the political complexity and fragmentation of this industry may continue to scare off for-profit investors, which means that the philanthropic sector and even the public sector may need to step in and create more social purpose investing intermediaries that are able to invest in both for-profit and nonprofit organizations. Such an expansion would allow entrepreneurs more freedom to develop innovative organizations and greater negotiating power, by giving them more of a choice of investors. It could also allow different firms to specialize in specific sub-areas of education, such as preschool services, technology tools or human capital systems. This will require foundations to delegate consciously some investment decisions and organization-building to such intermediaries. Given the sizeable need that social entrepreneurs in education face, it is crucial to figure out how to provide strong, successful, well-run organizations with greater amounts of long-term growth capital, allowing them to spend less time fundraising and more time building their team and delivering services.

Infrastructure

The most obvious infrastructure supporting the conventional capital markets is institutional or regulatory in nature, such as the public stock markets or specific financial reporting or accounting requirements. As noted earlier, there is little regulation of nonprofit funders other than the prohibition to use these tax-advantaged dollars for person gain or political advocacy, and the requirement to disburse five percent of their assets each year. This is designed to allow such donors to innovate and to encourage experimentation. Paul Ylvisaker, former dean of the Harvard Graduate School of Education, has referred to philanthropy as "society's passing gear" for this very reason because these loose regulations allow donors to move society forward by developing new solutions.[20] However, the unintended consequence is that there is little incentive for donors to be disciplined about how they manage or measure their impact, which makes for a seemingly capricious funding world for social entrepreneurs. Public oversight agencies have become increasingly concerned over the past several years about the way foundations are spending their money. It seems that the best way for foundations to get out ahead of this scrutiny is to make their grant-making criteria and success metrics more transparent.

Meanwhile, investors who choose to back for-profit social entrepreneurs are a very new phenomenon and are generally held to the same regulatory constraints as their peers in the sector in which they operate. One new development that may help to clarify this field is the work by sporting apparel entrepreneur Jay Coen Gilbert, who is trying to create a new kind of corporate class called "for-benefit corporations" or "B Corporations" that would make clear that a for-profit company has chosen to balance both financial and social impact.[21] Gilbert's new investment fund B Lab is developing legal frameworks and other infrastructure that would allow this to happen. It has recently unveiled a slate of 21 charter B corporations that have, among other things, modified their articles of incorporation to account for nonfinancial impact and agreed to transparent reporting of their performance.[22] There are no current tax incentives to encourage social purpose investors to try this blended approach to investing, meaning that for-profit social entrepreneurs must either raise money from for-profit investors who expect a standard rate of financial return (difficult to accomplish in an early-stage education organization) or try to raise capital from philanthropic donors (few of whom support any for-profit entities). We support the development of B Corporations and other innovative approaches to resolving this challenge.

Further, the development of human and intellectual capital will go a long way toward supporting educational entrepreneurs and will also strengthen their ability to raise capital. In particular, greater attention must be paid to programs and organizations that help prepare leaders with experience from across the public, private and nonprofit sectors. We call this "hybrid" leadership and believe that this combination of expertise and capital savvy from across sectors is crucial to the development of the social purpose capital markets. Some programs have begun to address this need for cross-sector leaders, including the dual master's degree in education and business at Stanford University and The Broad Center for the Management of School Systems, which identifies and prepares leaders with varied backgrounds for roles within school districts, not to mention the increasing number of universities with specializations in social entrepreneurship. Because this field is still emerging and is led by relatively young managers and entrepreneurs, more energy and resources will need to be spent on professional development for these leaders and on developing the pipeline of next generation leadership. An increase in industry-specialized strategy consultants, recruiters, and executive coaches would help bolster this aspect of the social entrepreneurship infrastructure.

Large and Diverse Supply of Capital Providers

In the conventional capital markets, there is a broad and diverse set of capital providers, ranging from small community-oriented lenders to large-scale investors who manage the billions of dollars in public pension funds or foundation endowments. Most of these large capital providers diversify their investment risk by placing their funds across a broad array of investment tools, stages of development, and industries. Indeed, a quick look at any newspaper's business pages shows the mind-boggling array of stocks, bonds, commodities, and mutual funds available through public exchanges, demonstrating that there seem to be as many investment opportunities available as there are individual and institutional investors. The bottom line is that for conventional for-profit businesses, there is an immense amount of financial capital available in the United States and it is available in a variety of mechanisms, ranging from start-up equity investments to loans of varying degrees of risk to shares of stock offered to the public on stock exchanges.

Contrast this with the social purpose capital market, which as described above is still relatively limited in terms of the number of players, their coordination, and the types of investment vehicles available – all of which significantly hamper the growth of entrepreneurial solutions in education. The responsibility for fixing this is shared among the nonprofit, private, and public sectors. Specifically, the biggest financial challenges facing these entrepreneurs are: an almost complete absence of early-stage investment capital available to for-profit social entrepreneurs in education (as Larry Berger details in his chapter on barriers to entry); a severe lack of nonprofit capital for organizations that want to grow to scale (at both the early and later stages); and a shortage of supply-side investments or incentives in this important arena by the public sector.

As Keeney and Pianko explain in their chapter, most for-profit investors are intimidated by public education, despite the relatively large and recession-proof nature of the industry. It is not difficult to see why: each of the 50 states has a unique set of education laws, standards, and mechanisms for assessment; the sales cycle into each of the country's 14,000 districts is long, idiosyncratic and relationship-based, making it difficult for new entrants to gain traction; and there is general resistance to adopting new tools and technologies. As such, few private investors are willing to take a risk on unproven for-profit enterprises in K-12 public education, making it difficult for social entrepreneurs to create new businesses in some of the areas where for-profit business models appear to make the most sense – such as technology tools to manage achievement and program data.

Meanwhile, social entrepreneurs in the nonprofit sector – particularly those taking on an ambitious project designed to address the vast scale of the problems in public education across the country – find themselves forced to spend at least half of their time cobbling together dozens of early-stage grants from philanthropic donors. According to consulting firm McKinsey & Company, for-profit companies spend between $2 and $4 raising capital for every $100 that they bring in, compared with $10 to $24 spent for every $100 brought in through fundraising among nonprofits.[23] One social entrepreneur who had a track record of success with earlier companies, Randy Best, found that he actually had to change his organization's corporate structure from nonprofit to for-profit to raise the capital that he needed. "I would tell a foundation that we needed a three-year grant of $500,000 per year and they would award me a one-year $20,000 grant and tell me to reapply next year," says Best. "I was spending all of the time fundraising and I needed to be focused on building the business. I changed our status and went to friends and investors who had supported my previous business ventures. We raised $40 million, and I had the money we needed to get started."[24] That company became Voyager Learning, a provider of research-based reading curriculum and professional development programs that grew to almost $100 million a year in revenue before it was bought in 2005.

Moreover, established nonprofit organizations trying to raise funds for growth often find themselves stymied as well. As social capital markets investor Tim Fruendlich of Good Capital points out, nonprofit donors tend to "nickel-and-dime social change leaders to death" by providing small grants and then cutting off their funding when they begin to demonstrate positive results and reach toward more growth.[25] This is what Bridgespan consultant Jeff Bradach calls the "paradox of success" in the nonprofit sector. "At precisely the moment when large amounts of capital would flow to a proven idea in the for-profit sector, funders in the nonprofit sector frequently back away," he writes. "There are many reasons – donor fatigue, a belief that equity requires spreading money around, hesitance to make ‘big bets’ – but the consequence is that proven solutions to pressing problems do not spread.”[26]

Certainly not all nonprofit investors shy away from providing growth capital to these organizations: both NewSchools and the Charter School Growth Fund aggregate capital from other donors and provide large, long-term grants and loans to charter school management organizations that are trying to grow and serve more students. Some newer foundations established by wealthy entrepreneurs from the business sector – whose founders have an appreciation for what it takes to grow an enterprise to scale – have been willing to provide bigger grants to organizations seeking to provide large-scale change, thus allowing those entrepreneurs to focus more of their energy on running the enterprise. For example, Doris & Donald Fisher Foundation (benefactor Donald Fisher founded the Gap clothing empire) and the Bill & Melinda Gates Foundation (created from the massive earnings of Microsoft founder and former CEO Bill Gates) have both given many millions to the nonprofit charter school network Knowledge is Power Program (KIPP) to sustain that organization’s ambitious growth plans, including at least $40 million from the Fisher Foundation and $17 million from the Gates Foundation.

In a bold move, some exceptional foundations, including the Atlantic Philanthropies and the Gates Foundation, have announced that they plan to “spend down” their endowments. Rather than allocating only the minimum legally required amount of 5 percent of their assets each year, they have set a deadline by which all of their funds will be put to use. This strategy stands in sharp contrast to the vast majority of foundations, whose growing endowments allow them to grant more money to nonprofits but also to support enormous staffs and occupy lush office buildings and operate in perpetuity. The decisions by Atlantic and Gates to spend down their endowments will no doubt increase the amount of philanthropic capital available in this century, but because a small percent is expected to flow into public education, this will not come close to filling the gap of nonprofit growth capital for social entrepreneurs in this market.

Foundations can take a number of steps to address this shortcoming. The simplest is to recognize the capital needs of social entrepreneurs and provide them with larger, longer-term grants. Further, more foundations could take a page from Atlantic and Gates by either spending down their endowments, or at least increasing the percent of their assets that are used toward creating social impact through a variety of "program-related investments" or PRIs. One of the easiest ways to do this is to provide "recyclable grants" for expanded operating capital. These interest-free, long-term loans could be allocated toward nonprofits that generate public fees for their services (such as charter school management organizations) and which could therefore repay those loans over time, allowing the same grant capital to be "recycled" and provided to other organizations.

Another approach would be to create an "equity equivalent" that would allow foundations to provide nonprofits with growth funds without saddling them with debt liability that reduces their access to private sector debt. Although such a tool might look much like a recyclable grant or loan, it could be structured so that it would be accounted for and function more like equity (only to be repaid if certain financial accomplishments were met). Another way to use PRIs is to invest in independent intermediary organizations who could then specialize in selecting and supporting higher risk early-stage organizations – whether for-profit or nonprofit –within areas that complement the work of foundations themselves. These intermediary firms could then leverage these funds with later-stage funds from the private sector or from foundations.

Similarly, the public sector could and should do a great deal more to mobilize private capital into entrepreneurial education organizations by creating new tax credits to reward investment in specific areas of need, such as more sophisticated assessment tools that measure the higher order skills we hope to see in students. Another change might be to revise the New Markets Tax Credits – originally created to mobilize private sector investments into low-income communities – to make them more amenable to education investments by eliminating the requirement to hold investments for 10 years. The public sector could also stimulate the supply of entrepreneurial solutions in education by establishing a pool of funds that would be available through a competitive request for proposal (RFP) process to investment intermediaries to use in supporting organizations that address key areas of need (such as assessment tools or teacher and principal preparation programs), and could even require that these funds be matched by private sector commitments. Finally, the public sector should attend to the needs of one of education's largest entrepreneurial movements – charter schools – by increasing funding to these schools in a way that enables more of them to get off the ground (expanding federal charter school start-up grants significantly), helping more of them to obtain and pay for facilities (by expanding the charter schools facilities credit enhancement program), and encouraging more established operators to develop new schools in the communities that need them (through a new competitive grant programs designed to support quality scale organizations).

Call To Action

"No matter how fertile the seeds of entrepreneurship, they wither without the proper economic soil."

- Dwight R. Lee, University of Georgia[27]

This volume takes as one of its assumptions that educational entrepreneurs are important change agents, are here to stay, and require additional support from their surrounding ecosystem to have the strongest positive impact on the public education system. This chapter goes one step further, arguing that social entrepreneurs – who seek to improve outcomes for those communities that have been underserved, and to transform the system so it better meets those needs on an ongoing basis – occupy an especially valuable niche within the broader entrepreneurial space. We further argue that it is important to consider this field – both entrepreneurs and sources of capital – across the traditional boundary of the economic sector. That is, given the import of this work and the scale of the problems we seek to fix, it will take leaders and resources from all of the nonprofit, private, and public sectors. And lastly, we point out that social entrepreneurs' ability to create significant change has been hampered by the limited size and relative immaturity of the social purpose capital markets intended to serve them.

It is worth remembering that the conventional capital markets have only come into their present structure through the intentional actions of a variety of means – namely, government regulations to establish and refine the ground rules and help guide the flow of capital, and business and nongovernmental organizations to create a range of institutions, practices, and investment tools within those constraints. It will be no different in the social purpose capital markets for educational entrepreneurs. Specifically, for this movement to continue to develop and grow its impact, our most important recommendations include:

More growth funding. The field needs much more funding, both at the early and latter stages of an entrepreneurial organization's development, and it should be committed in larger amounts via multi-year investments and grants with fewer strings.

More patient capital. Building quality in public education takes time, and investors need to recognize that the best way to build financial or social value is by providing consistent quality over time.

A strong ecosystem. Any mature industry needs substantial specialized human and intellectual capital, so investments in entrepreneurial ventures need to be accompanied by greater support of entrepreneurial team capacity, as well as a more robust ecosystem of financial, intellectual, and human capital intermediaries.

Move past old ideologies. Just as we expect entrepreneurs to think creatively – beyond the bounds of the status quo – so too must their capital providers. Foundations need to expand program-related investments, and support a stronger for-profit field through the creation of nonprofit investment intermediaries. For-profit investors need to work toward supporting "blended value" or "double bottom-line" investments. Finally, public sector leaders – who bear ultimate responsibility and accountability for ensuring that the needs of public school students are met – must expand supply-side support for these entrepreneurial organizations by devising approaches that bring together resources from across the public, private, and nonprofit sectors.

[1] A word about terminology: while others may sometimes use the word "sector" to refer to an industry or area of common interest, such as the "education sector" or the "military sector," we have here used "sector" to refer to the economic divisions between sources of capital: the public sector (government), the private sector (business) and the nonprofit sector.
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