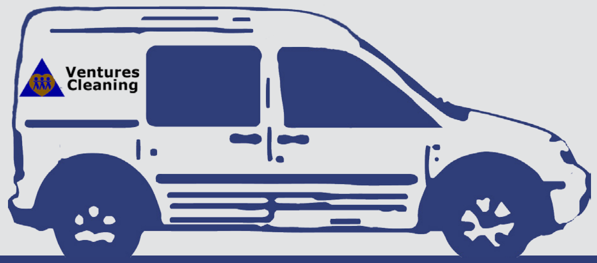
PACE CAA
SOCIAL ENTERPRISES



a CAPLAW case study

LOCATION	Vincennes, Indiana
YEAR FOUNDED	**Pace CAA:** Founded in 1965 as the Economic Opportunity Committee of Knox County **Pace Ventures Holding, Inc.:** Founded in 2007
SOCIAL ENTERPRISES	**Ventures Cleaning:** Commercial and residential cleaning services (operated as a single-member, limited liability company subsidiary under Pace Ventures Holding, Inc.) **WiseCAP Training & Consulting:** Nonprofit and CAA compliance, strategic planning, and professional development services (operated as a division of Pace Ventures Holding, Inc.)
LEADERSHIP	Dr. Bertha A. Proctor, CEO Lori Williams, Associate Director Tai Blythe, Associate Director Terri Wise, Chair of the Board of Pace Ventures Holding, Inc.
TYPE OF CAA	Private, non-profit
SERVICE AREA	Four counties in southwestern Indiana
# OF CAA CLIENTS	Approximately 35,000
BUDGET	$7.6 million (FY 2016)
CAA PROGRAMS	- Head Start and Early Head Start - Low-Income Home Energy Assistance Program (LIHEAP) - Weatherization Assistance Program - Health Connection clinics (reproductive family planning health services) - Women, Infants & Children (WIC) - Individual Development Accounts (IDA) - Emergency food & shelter and rent/ mortgage/utilities assistance (FEMA) - Small Business Revolving Loan Fund - Affordable housing program - Boys mentorship program - Internship program

INTRODUCTION

Nonprofit organizations seeking to reduce their dependence on government grants and private charitable fundraising have long looked to earned income ventures as a way to diversify their revenue sources. For nonprofit CAAs that have traditionally relied upon federal funding to operate their programs and services, venturing into the social enterprise space can feel like entering into a brave new world—although free of some of the rules that apply to nonprofit, tax-exempt organizations, yet rife with other tricky issues they did not previously face. This case study examines how a nonprofit CAA that has served its community since the inception of the Community Action network under the Economic Opportunity Act of 1964 leveraged its experience to establish social enterprise businesses focused on helping individuals reach self-sufficiency. Through Pace Community Action Agency's experiences developing and operating various earned income ventures, this case study offers a lesson in the common legal, governance, and financial issues that federally-funded nonprofit organizations will likely encounter when running social enterprises.

ORIGINS: THE QUEST FOR INDIVIDUAL AND ORGANIZATIONAL SELF-SUFFICIENCY

It all started with a question, followed by a plane ride. As part of its strategic planning process beginning in 2006, the board of directors of Pace Community Action Agency (Pace or Pace CAA) raised the following question: "What are we doing to bring ourselves to self-sufficiency?" Pace's mission statement had long been "to provide support services that improve the community and encourage self-reliance," but its own existence and ability to operate its programs depended heavily upon government grants. As part of its focus on organizational sustainability in the strategic planning process, the board closely reviewed the percentage of federal and state funds used to operate the agency and set a goal to take steps to reduce that percentage.

In addition, the board was not content to simply help people while they were ***in*** poverty; it wanted to know what Pace itself was doing to help people get ***out*** of poverty. While it believed that the services offered by the CAA—

WHY CREATE A FOR-PROFIT SUBSIDIARY?

- **To protect the nonprofit organization's tax-exempt status.** While 501(c)(3) nonprofit organizations are generally exempt from federal income tax, they may be liable for unrelated business income tax (UBIT) on the income generated from activities that are not related to their exempt purposes. The purpose of UBIT is to ensure that tax-exempt organizations do not have an unfair competitive advantage over for-profit entities when a tax-exempt organization engages in commercial business activities. While the nonprofit organization could generate income from unrelated business activities and simply pay any UBIT incurred, at some point, the activity may become so substantial that it could jeopardize the tax-exempt status of the nonprofit organization. Since there is no bright line rule for how much unrelated business activity the Internal Revenue Service (IRS) considers too much for the nonprofit to operate, moving those activities to a separately-incorporated, taxable legal entity, such as a C-corporation subsidiary, can avoid concerns about crossing that line. The nonprofit carries out the activities in a separate but related entity, which will pay income tax on the net income from the activities and which can then remit the after-tax profits as a dividend or as a grant to the nonprofit parent. Dividends received by tax-exempt organizations are considered passive income, and not subject to UBIT. Note that when choosing a taxable entity for the profit-making business, it is important to ensure the entity is not considered "pass-through" for tax purposes. Activities of pass-through entities, such as partnerships, limited liability companies (LLCs) and S-corporations, are generally attributed to their owners. Further, single-member LLCs are generally disregarded for federal tax purposes. The IRS will attribute the profit-making activities carried on by the pass-through entity to the activities of the nonprofit owner, which undermines the tax purpose of creating a separate for-profit subsidiary.

particularly its Head Start/Early Head Start programs, which provided low-income children the opportunity for educational, emotional, and social development, as well as its economic development programs such as matched Individual Development Accounts (IDAs) and a small business loan program—effectively reduced poverty in the longer term, the issue of self-sufficiency loomed large in the board's mind. This was, in the board's view, the most difficult to achieve of the goals outlined in the federal Community Services Block Grant (CSBG) Act, which serves as the bedrock funding of all CAAs. While traditional CAA programs such as energy assistance, affordable housing, and weatherization all share the aim of reducing poverty and revitalizing low-income communities, the board believed that empowering low-income families and individuals to become self-sufficient would require a longer-term solution—a job.

To help Pace answer the question of what it was doing to decrease dependency on public funding and to enable people to become self-sufficient, the board formed an ad-hoc committee called the Ventures Committee, consisting of nine Pace CAA board members. The committee's task was to determine untapped business markets in its community. The Ventures Committee met with other local nonprofit organizations that had started social enterprises, studying their business models and legal structures. The key to individual self-sufficiency, the board believed, was to provide stable jobs, and the key to Pace's self-sufficiency was to expand its revenue stream beyond the federal, state, and local government grants it received year after year to conduct its programs and activities. Thus, not only did a social enterprise need to enable an employee to earn a living, it ideally would earn a profit to provide unrestricted funding for Pace CAA as well.

While the Ventures Committee explored income-earning options, Pace CAA began thinking about how social enterprise operations fit into its organizational structure. By chance, in 2006, Bertha Proctor, Pace's Chief Executive Officer, and Lori Williams, Pace's Associate Director, met an attorney on a flight during a Pace-related business trip. The group discussed Pace's ideas for operating earned income ventures and options for structuring the businesses, including what the Ventures Committee had learned when it studied other nonprofit social enterprises in the community. The attorney's law firm agreed to provide pro bono legal services to help Pace structure its social

WHY CREATE A FOR-PROFIT SUBSIDIARY? (Continued)

- **To provide the nonprofit organization flexibility to pursue profit-making activities.** A nonprofit organization's charitable purpose may limit the types of earned income ventures it can pursue. For example, a nonprofit CAA's mission to serve low-income and underserved communities may decide to start an earned income venture, but sell its products or provide certain services at a lower price in order to ensure that the activity is substantially related to its charitable purpose. This business model, however, may not generate as much revenue as offering its product or service at fair market value. Operating a for-profit subsidiary (and paying corporate taxes on the income generated by the business) enables the nonprofit organization to pursue these types of profit-making activities without worrying about whether the activity is consistent with the organization's charitable mission and tax-exempt status.

- **To shield the nonprofit parent organization from liability.** Nonprofit organizations operating for-profit businesses may be concerned about protecting their charitable assets from the liabilities of the businesses. By moving the business to a legally separate subsidiary (and assuming the parent and subsidiary organizations operate independently of one another and respect their separate corporate identities), the nonprofit organization can isolate the business liabilities in a limited-liability subsidiary. This ensures, for example, that the nonprofit organization's social services programs will not be jeopardized if the business it also owns is sued.

- **Attracting outside investors.** Unlike a nonprofit organization, a for-profit entity can raise money from outside investors by offering equity in the entity. While nonprofit organizations rely on grant awards and other charitable contributions, loans, investment enterprises. Even though the Ventures Committee had not yet decided on what businesses to start, the board decided to move forward with setting up a legal structure that would facilitate business expansion in the future.

While some social enterprise ventures are run directly out of nonprofit organizations, the Ventures Committee wanted to protect the assets of the CAA from the liabilities of the earned income businesses. Thus, Pace's new pro bono legal team created a C corporation, an entity recognized under U.S. federal income tax law as a corporation that is taxed separately from its owners, called Pace Ventures Holding, Inc. (Ventures Holding). Pace CAA became the sole owner and shareholder of Ventures Holding (see "Pace Social Enterprises: Legal Structure" for a description of how Pace CAA's social enterprises are structured). The group envisioned that future social enterprises could be set up as single-member limited liability companies (LLCs) operating as subsidiaries of Ventures Holding.

The nine members of the Ventures Committee became the initial board members of Ventures Holding after it was incorporated as a separate entity. However, the Pace CAA board wanted to ensure that Ventures Holding would operate as an independent entity to preserve the liability shield that ultimately protected the assets of Ventures Holding from those of the CAA, and vice versa. In order to maintain sufficient independence, the Ventures Holding board now consists of nine members, with only two overlapping members who also serve on Pace CAA's board. Dr. Proctor and Ms. Williams, both employees of Pace, also sit on Ventures Holding's board. The remaining five members, who constitute a majority of Ventures Holding's directors, are independent directors with no direct connection with Pace CAA, but who have relevant experience in business and social enterprise. One member, for example, represents the first customer of Ventures Holding's first social enterprise—Ventures Cleaning. As the sole shareholder of Ventures Holding, Pace CAA retains control over the subsidiary by having the exclusive authority to appoint and remove the board members of Ventures Holding.

Pace CAA and Ventures Holding have a management services agreement under which certain Pace CAA employees provide services for Ventures Holding, including human resources, IT, accounting, and other administrative

WHY CREATE A FOR-PROFIT SUBSIDIARY? (Continued)

income, or earned income revenue, because they do not have shareholders or equity owners, they cannot offer ownership interests in the entities themselves. For-profit entities such as C corporations or limited liability companies, on the other hand, can raise capital by offering investors an equity stake in return for their investment, thus generating an additional source of funding for the businesses.

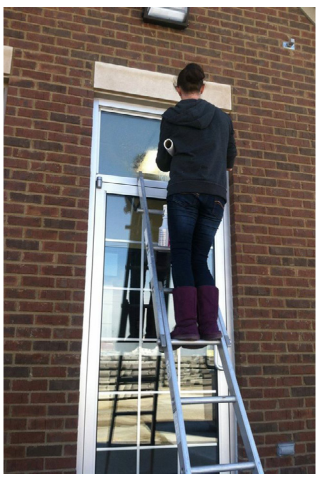
- **Attracting and retaining employees through equity-based compensation.** For-profit entities can enter into profit-sharing arrangements or offer equity compensation to employees in ways that nonprofit organizations, particularly CAAs subject to federal grant rules, may not be able to. Further, a for-profit subsidiary would not be subject to the federal tax rules prohibiting private inurement and private benefit that limit nonprofit organizations, and thus would not need to worry about excessive employee compensation. This allows the for-profit subsidiary flexibility to recruit and retain employees, especially when competing with other for-profit businesses.

- **Public perception and required disclosures.** A nonprofit organization must report its unrelated business activities and income on its annual IRS return (Form 990). A privately-owned, for-profit subsidiary, on the other hand, would not be subject to the same public disclosure rules—for example, the subsidiary would not have to disclose its income and expenditures or the compensation it pays its employees (depending on the individual's role at the nonprofit organization). From a public perception standpoint, the nonprofit organization may also prefer to separate its profit-making activities from the nonprofit's charitable programs and to avoid the impression that the business activities are in competition with its mission-driven activities.

services. Employees allocate and report the time they spend working for Ventures Holding, and Ventures Holding reimburses Pace CAA for a portion of the employees' salaries. Ventures Holding also pays a portion of other overhead costs—including for space, travel, and insurance—based upon its proportionate share of those costs.

VENTURES CLEANING

The first social enterprise launched under Ventures Holding opened for business in 2007 as Pace Ventures, LLC, d/b/a Ventures Cleaning (Ventures Cleaning). Ventures Cleaning provides a range of commercial and residential cleaning services. It counts among its clients local banks, small businesses, universities, nonprofit organizations, and churches. The idea for Ventures Cleaning came from Dwaine (Andy) Anderson, the janitor working for Pace's Head Start program, in 2006. He believed that Pace could create a business around providing cleaning services in the local community. The Ventures Committee of the Pace CAA board considered the idea and began an extensive vetting process to determine (1) whether the business fit Pace's mission and (2) whether there was a viable market for such services.



The boards of Pace CAA and Ventures Holding each ultimately determined that a cleaning company fit the CAA's overall mission. Ventures Cleaning planned to hire employees with few skills and limited work experience. Employees at Ventures Cleaning would work with job coaches to learn basic cleaning skills, build a resume, and receive computer training, preparing them for other cleaning jobs. The idea was that Ventures Cleaning would provide that first job that is often hard to come by for individuals who have been out of work for some time, training them for more specialized positions and thus enabling them to move on to better paid work.

To prepare a business plan for Ventures Cleaning, Mr. Anderson and the members of the Ventures Committee conducted market research, speaking with other cleaning companies in the area as well as potential customers to determine whether there was sufficient demand for the cleaning services. Both the Pace CAA and Ventures Holding boards felt that a cleaning business had fairly low startup costs—since Pace CAA itself continued to need cleaning services for the buildings it owned, Ventures Cleaning could train its employees at Pace CAA's sites. In short, the business was an outgrowth of Pace's own janitorial department and did not require a big upfront investment in a new line of work.

Ventures Cleaning's first major customer was Old National Bank, a local community bank with 12 branch offices. Mr. Anderson was an enthusiastic advocate for the business, meeting with members of the community to market the cleaning services. People who learned about Ventures Cleaning were impressed by the organization's mission of having profits from the business reinvested in the community through supporting the work of Pace CAA. Since then, business has increased steadily. From its first employee, who trained in Pace's buildings and worked side-by-side with Mr. Anderson, Ventures Cleaning now has a staff of 16 employees, with approximately $500,000 in annual contracts. Ventures Cleaning has invested a portion of its profits into upgraded equipment and the purchase of a fleet of vehicles that employees use to get to cleaning sites.

As the business has grown, Ventures Cleaning's employment needs have also shifted. Due to the demand for highly specialized cleaning services, Ventures Cleaning began hiring employees with more specific skills—those who had experience cleaning windows, treating floors, or working in hospitals, for example—and now approximately 60% of its workforce are specialist positions, with the remaining 40% entry-level cleaning positions. This has allowed Ventures Cleaning to expand into cleaning services beyond the regular maintenance and upkeep of commercial buildings and residential homes. Ventures Cleaning is also now known for its expertise in post-construction cleaning and specialized floor care and treatment services. Though its hiring focus has changed, Ventures Cleaning has fought to preserve the original mission of the cleaning company, which is to employ individuals who otherwise would not be able to find work.

Ventures Cleaning operates as a single-member LLC subsidiary of Ventures Holding. From a federal tax perspective, it is a pass-through entity and Ventures Holding (as the taxable parent entity) reports and pays taxes on income generated by Ventures Cleaning at regular corporate income tax rates. Individuals who work for Ventures Cleaning are employees of the LLC. Ventures Cleaning receives administrative support services for its human resources/payroll, IT, and accounting needs through the management agreement between Ventures Holding and Pace CAA.

WISECAP TRAINING & CONSULTING

In 2008, Ventures Holding launched a second social enterprise—WiseCAPTraining & Consulting (WiseCAP), which provides consulting services in compliance, grant management, strategic planning, and leadership development primarily for nonprofits and grant-funded entities. The idea for providing CAA-specific training and consulting came when the Indiana Community Action Association (INCAA) called Dr. Proctor in 2008 and asked if Ms. Williams could provide consultations to other CAAs in the state. Pace had undergone an intensive restructuring process in 2004, resulting in a dramatic transformation in the leadership and operations of the organization. INCAA has worked with outside consultants to provide training and technical assistance to its CAA member network. However, Pace recognized that while consultants were knowledgeable about certain strategic and operational matters, they were not familiar with the complexities and nuances of Community Action.

Based on the success of the consulting services that a few Pace CAA staff members provided through INCAA, Dr. Proctor and other members of Pace's management team felt that there was a market for CAA-specific trainings. Dr. Proctor, Ms. Williams, and Tai Blythe, another Associate Director of Pace CAA, had a shared passion for teaching and organizational leadership development. WiseCAP provided an initial training at the national Community Action Partnership's annual conference in 2008. Following the conference, individual CAAs began contacting WiseCAP to ask for targeted trainings for their organizations, as they realized the trainers were able to connect with their programs and systems in a way that external consultants often did not.

Compared to Ventures Cleaning, WiseCAP's business has grown more slowly and organically. On average, WiseCAP provides approximately five to six paid trainings per year. Many WiseCAP trainers are employees of Pace CAA and train in their individual areas of expertise—for example, in human resources matters, early childhood education, and technology systems. WiseCAP has also established a network of consultants who are engaged on a project-specific basis to provide training on matters such as talent management and diversity, succession planning, and conflict resolution. Currently, WiseCAP operates as a division of Ventures Holding, rather than as a separate LLC subsidiary under Ventures Holding (as Ventures Cleaning is structured).

ONGOING CHALLENGES

As for-profit enterprises of a nonprofit organization, both Ventures Cleaning and WiseCAP have had to deal with challenges that traditional for-profit businesses do not typically face. Some of these challenges are described below.

UBIT. While 501(c)(3) nonprofit organizations are generally exempt from federal income tax, they may be liable for UBIT on the income generated from activities that are not related to their exempt purposes. UBIT ensures that tax-exempt organizations do not gain an unfair competitive advantage over for-profit entities that pay income taxes on their income. Activities are considered "unrelated" and thus subject to UBIT if they (1) constitute a trade or a business, (2) are regularly carried on, and (3) are not substantially related to the furtherance of the organization's tax-exempt purposes.

Since Ventures Cleaning and WiseCAP both operate out of Ventures Holding, Ventures Holding reports and pays taxes on income generated by both businesses at regular corporate income tax rates. Thus, Pace CAA is not liable for any UBIT as a result of the revenue from its for-profit enterprises (see the sidebar "Why Create a For-Profit Subsidiary?" for additional reasons to house social enterprises in a separate, for-profit entity). However, Ventures Holding contracts for and pays Pace CAA for various administrative services, including human resources, IT, and accounting, and under the management agreement between Pace CAA and Ventures Holding, Ventures Holding reimburses Pace CAA for these services. Under IRS rules, providing such services may in certain circumstances be considered "unrelated business activities" and the fees received may be subject to UBIT. A nonprofit organization that generates more than $1,000 in annual gross unrelated business taxable income must report the income on its annual Form 990-T, though it would only pay UBIT on any net income after deducting for allowable business expenses.

> Under IRS rules, providing [administrative] services may in certain circumstances be considered "unrelated business activities" and the fees received may be subject to UBIT.

Employee Benefits. Employees of Ventures Cleaning enjoy certain benefits that typical cleaning company employees do not. Ventures Cleaning offers its employees, for example, the opportunity to participate in Pace CAA's 401(k) retirement plan as well as the same health insurance packages Pace CAA employees receive. By having its employees on a separate payroll from the nonprofit CAA's, it is easier for Ventures Cleaning to offer incentive compensation such as bonuses and attendance-based incentive pay, since it does not have to follow the IRS and federal grant rules on these compensation options. Having certain benefits that were only available to Ventures Cleaning employees, however, presented administrative challenges for Pace's human resources department, which has to manage two sets of personnel policies and employee benefits.

Conflicts of Interest. Because Pace and Ventures Cleaning are related parties, they have to carefully navigate the conflicts of interest that are inherent in providing services to one another. Pace and Ventures Cleaning maintain separate procedures that cover organizational conflicts of interest, as required by the Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Awards (Uniform Guidance), 2 C.F.R. § 200.318(c)(2). Members of both boards are subject to their respective organization's conflict of interest policy and complete annual conflict of interest disclosures. When a board decision involves the other entity, board members who sit on both boards will abstain from the discussion and vote. One recurring source of organizational conflicts involves Pace CAA procuring cleaning services from Ventures Cleaning for Pace CAA's buildings and facilities. Pursuant to its procurement procedures, Pace CAA has reviewed price quotes from other local cleaning services prior to engaging the services of Ventures Cleaning. Pace CAA has historically paid for cleaning services from Ventures Holding at cost to avoid the appearance that the social enterprise is profiting off its nonprofit parent organization.

Use of Profits. Pace's social enterprises generate approximately $500,000 per year in gross revenue. With the exception of one year, the businesses have always generated a small combined profit. The Pace CAA and Ventures Holding boards have discussed the best use of the profits—while to date, none of the profits have been transferred to Pace CAA, the profits serve as a source of unrestricted funds that provide a cushion for potential cash flow shortages. Ventures Holding has used some of the net profits to purchase equipment and vehicles for Ventures Cleaning. The boards constantly review how to best reinvest the funds to facilitate the enterprises' future growth. If Pace CAA were ever to need to use the funds, the boards would consider the best way to transfer these funds to the nonprofit parent (through declaring a dividend or making a grant to Pace CAA) with guidance from its accounting firm. At a minimum, this transfer would require a formal board vote by the Ventures Holding board that it is in the best interest of the entity to transfer the funds to Pace CAA.

ADVENTURES CHILDCARE: AN EXPERIMENT AND LESSON LEARNED

When asked whether Ventures Holding has plans to launch additional social enterprises, given the success of Ventures Cleaning and WiseCAP, Dr. Proctor and Ms. Williams hesitate. They indicate that while they will always think entrepreneurially and pursue new businesses, at this point, there are no concrete plans to start a new enterprise. Simply because there is a market in their community for a social enterprise that they have the experience and ability to provide does not mean that Pace CAA and Ventures Holding are planning to jump in. They have learned this the hard way. In 2007, after Ventures Cleaning's successful launch, a local child care center approached Pace and asked if it would consider taking over the center's child care operations. The center had run into financial trouble and indicated it would have to shut its doors imminently. As a result, over 40 children would no longer have access to the largely voucher-funded child care services. Pace seemed like a logical partner because of its experience running Head Start and Early Head Start, as well as its proximity to the child care center. Pace eventually decided to acquire the day care center—renamed Adventures Childcare—as another social enterprise.

Pace seemed like a logical partner because of its experience running Head Start and Early Head Start, as well as its proximity to the child care center.

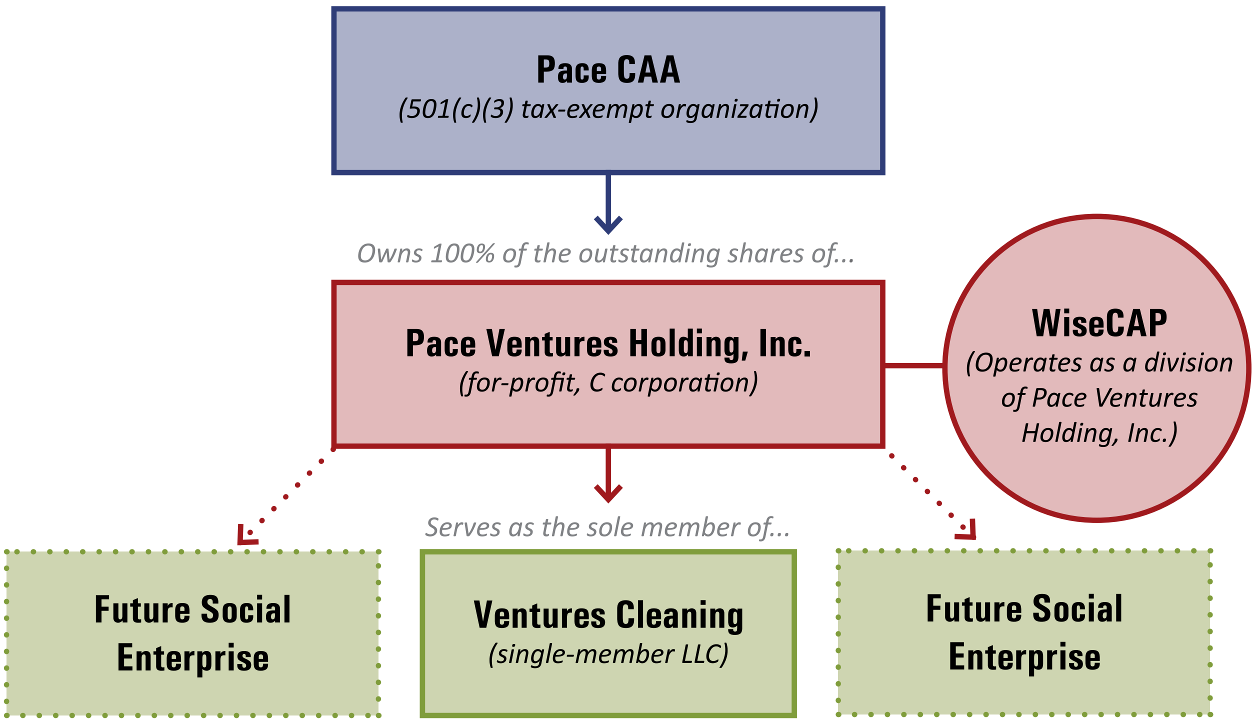
Soon after Pace assumed operations of Adventures Childcare, however, it faced a number of unanticipated costs. Pace had conducted financial due diligence on the center and believed that it could step into the licensing shoes of the child care center. However, the state informed Pace after it had acquired the center that Adventures Childcare would have to restart the licensing process and could not continue the center's prior, grandfathered status. This process was lengthy and costly, and all of the child care center's facilities were subject to inspection. The center also needed a new roof and new HVAC system—upgrades that Pace had known it would have to undertake—representing significant upfront launch costs. Even after Adventures Childcare opened its doors, it experienced difficulties collecting on the co-payments that parents made to supplement the voucher program.

The child care business bled cash for a few years, as Pace tried a number of different strategies to bolster the fledging business. It attempted to combine Adventures Childcare with the services Pace was providing through its Head Start programs, eventually replacing the voucher system entirely with additional Early Head Start and Head Start classrooms. There were also issues integrating the staff and culture of the child care center with Pace's Head Start staff. Eventually, Pace decided Adventures Childcare was not a sustainable business and wound down the center, selling the buildings it had acquired to a local homeless shelter at a loss in 2015.

PLANS FOR THE FUTURE

Looking back at what it now calls an "emotional decision" to take over the Adventures Childcare business, Pace CAA has changed its approach to pursuing new social enterprises. Thus far, the boards of Pace CAA and Ventures Holding have identified a few possible enterprises, including providing a meal service that could be a benefit for working parents, the elderly, or other individuals who may not have time in their schedule to prepare healthy meals. This could be a natural outgrowth of the Head Start meals that Pace is already putting together in its newly renovated commercial kitchen. The board also thinks there may be a market for small renovation and construction projects that larger-scale contractors in the community typically avoid, which could capitalize on some of the expertise developed in Pace's Weatherization program. While Pace may decide to pursue either of these ventures at some point, it plans to do so by investing in its employees first, developing leaders within its own organization to oversee these enterprises.

PACE SOCIAL ENTERPRISES: LEGAL STRUCTURE



LESSONS LEARNED

- **Be clear about the market for the product or service.** Conduct market research by surveying potential customers and competitors in the community to be sure that there is sufficient demand for the products and/or services the CAA intends to offer. Doing this initial research will also help the CAA put together a viable business plan with proper marketing and pricing strategies.
- **Allow businesses to develop organically and nurture them carefully.** This is especially important for nonprofit organizations that have not previously operated earned income ventures or are new to the social enterprise space. Resist the urge to scale up too quickly; allow opportunities for expansion to develop naturally and pursue them thoughtfully. For example, Ventures Cleaning started out providing general cleaning services, but gradually moved into more specialized services, such as floor treatments and construction cleanup, as it became more familiar with client needs. This has allowed Ventures Cleaning to expand its expertise and develop a niche market for cleaning services.
- **Build off of the CAA's strengths and existing infrastructure.** When considering which social enterprises to pursue, consider the CAA's prior experience and look for opportunities to leverage its existing infrastructure and personnel to develop earned income businesses. For example, a CAA that receives a grant to provide senior citizens with transportation in rural areas could consider expanding its client base to non-seniors and charging a small fee for rides. The CAA may already have vehicles and drivers, minimizing its startup expenses, and can build on its experience coordinating a transportation network. Note, however, that any income generated using grant-funded facilities, equipment, or personnel will be treated as "program income" and will be subject to all of the rules that apply to the federal grant

LESSONS LEARNED (CONTINUED)

funds. Therefore, it is advisable for the social enterprise to pay its fair share of the costs of using the CAA's facilities, equipment, and personnel at fair market value so that the income generated by the enterprise will not be considered "program income."

- **Get experienced business people on board.** While many individuals on Pace CAA's board and staff have longstanding experience overseeing and running a nonprofit social services organization, Pace CAA knew that in order for its social enterprises to succeed, it needed individuals with backgrounds in the corporate, for-profit sector. Thus, once it established Ventures Holding as a legally separate entity, the members of Pace CAA's Ventures Committee actively recruited individuals in the community who had relevant business, marketing, and accounting expertise to join the Ventures Holding board. These board members have proved to be invaluable resources over the years—they have guided the businesses as they grew from nascent ideas into full-fledged operations, helping to establish client contacts and vet potential business ideas.
- **Set up a legal structure that protects the CAA while facilitating future growth.** From the outset, Pace CAA's goal was to create an environment that facilitated the growth of social enterprises as they developed over time. Thus, it was important to the Ventures Committee and the Pace CAA board to set up a legal structure that protected the CAA's assets while providing the flexibility to add on businesses in the future. Pace CAA considered the reasons discussed in the sidebar "Why Create a For-Profit Subsidiary?" and determined that creating a separate, for-profit subsidiary (Ventures Holding) gave the CAA the most flexibility to pursue earned income ventures. The structure chart "Pace CAA Social Enterprises: Legal Structure" illustrates how Pace CAA set up Ventures Holding to serve as a platform to house future businesses. To ensure that courts will treat Ventures Holding as a separate, taxable corporate entity and not as a mere "instrumentality" of the CAA, Pace CAA maintains a separate bank account and separate financial books and records for Ventures Holding, separate logos for Ventures Cleaning and WiseCAP, and a separate website URL for Ventures Cleaning. Though they share a mailing address, the entities maintain strict financial and operational separation and do not co-mingle assets. The boards operate independently, conducting separate meetings and keeping separate minutes, and there is limited overlap in board membership. Pace CAA and Ventures Holding enter into arm's length written agreements covering any shared resources (e.g., facilities, personnel, equipment, supplies, etc.), and Pace CAA is fully reimbursed for any use of its office space or administrative services. Maintaining separate identities and operations is crucial to ensuring that the liabilities of one entity will not be attributed to the other entity.
- **Have a champion who will advocate for the enterprise.** Pace learned the hard way that it is not enough to identify a need in the community that a social enterprise can fill. It is also vital to have a champion of the enterprise who doesn't just see the enterprise as a side project of the CAA. For Ventures Cleaning, that champion was Mr. Anderson; for WiseCAP, it has been Dr. Proctor, Ms. Williams, and Ms. Blythe, who not only have practical strategic planning experience but also the passion for training others. These individuals are invaluable advocates for the enterprises and are invested in their growth and development.

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