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STRUCTURING FOR IMPACT:

Evolving Legal Structures
for Business in New Zealand

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FOREWORD

For our country to better look after our people and environment, we need innovative ways to achieve social inclusiveness and wellbeing for all New Zealanders. Some businesses, often referred to as social enterprises, have long been working for broader versions of social and environmental capital, and have significant, untapped potential to create transformative change for New Zealand, alongside traditional delivery models for social outcomes.

Social enterprise models have the potential to innovate and to create value for a triple or quadruple bottom line. In the process, jobs are created, communities are nurtured, the environment is preserved and maintained, and the economy is fostered.

We are also seeing significant growth in the number of businesses in New Zealand that operate with both an impact, as well as the traditional profit focus, as the world starts to shift towards solving the complex challenges we are all facing. What this report evidences is that New Zealand's current legal structures and financial expectations are hindering social enterprises being able to reach their full potential: Businesses that prioritise more than just financial profit are being disadvantaged in New Zealand.

New Zealand has the potential to enable business-of-the-future, and to establish a suitable, modern legal and commercial environment that does not hinder and disadvantage businesses creating social or environmental impact. The disadvantages which this report identifies, and the potential growth in wellbeing for New Zealand if these are removed, are significant. By dismantling the barriers that

the current legal structures present for social enterprise, we can catalyse private sector-led solutions, and demonstrate how impact through enterprise can be achieved across the entire economy.

If we create the right settings for social enterprise, we have the opportunity to enhance the prosperity and wellbeing of generations to come in New Zealand. Therefore, we encourage the Government, Parliament and the wide range of stakeholders involved in the analysis of our current legal structures, and tasked with growing 'impact investment' in New Zealand, to consider carefully the details of this report, to seek to understand the importance of impact through enterprise, and to take action and to make those reforms that are necessary to let social enterprise achieve its full potential and impact in New Zealand.



SIR NEVILLE JORDAN, KNZM CNZM

Social enterprise models have the potential to innovate and to create value for a triple or quadruple bottom line.

EXECUTIVE SUMMARY

Social enterprise (SE) is about prioritising impact as well as profit. While New Zealand has legal structures which enable organisations who prioritise one or the other (i.e. charity or traditional business), SE does not fit neatly within these models, and often has only a passing resemblance to them. Instead, SE operate with a different logic. The social entrepreneurs behind SE pursue a different set of values from traditional business, with profit being only one factor in the mix, and often only as a means to achieving more impact. Based on the growth and contributions of SE to New Zealand to date, it is clear that organisations who prioritise more than profit have significant potential to positively grow New Zealand's economy in a broad sense, solving significant societal challenges along the way. Because of this, New Zealand needs a legal and policy environment that enables and encourages businesses that are trading for impact.

For the most part, however, operating a SE in this country is more challenging than running a purely profit driven business. This report finds that the legal structures currently available in New Zealand are acting as barriers for, and disadvantage to, SE. The array of issues and challenges SE face using limited liability company structures, or any other legal structure in New Zealand, stems from the reality that these structures developed from a perspective that 'doing good' is separate from 'doing business'. The distinction between doing good as charity on the one hand and doing business on the other is cemented in the prevailing attitudes of what charity as a way of doing good is allowed to be, and what doing business is required to be. This context makes doing business with impact far more difficult than standard for-profit business.

This report sets out evidence from SE about the perceived challenges associated with the current legal structures and argues that evolving legal structures to remove some of those challenges will unlock the potential of business to generate social and environmental impact at scale that grows the wellbeing of New Zealand. Doing so would also support organisations underpinned by Te Ao Māori in a way that really honours Te Tiriti o Waitangi.

All but one of the SE we spoke with in this research found that their legal structure created hurdles for their organisation. These hurdles appear to be most commonly centred around the enterprises' inability to convey and protect their mission, and the consequential challenges that any workarounds to this create. Funding was the other key disadvantage, with many SE finding accessing funding very difficult because of their structures, a hurdle which is having significant implications on the ability of these organisations, and their impact, to scale.

The world is changing. Businesses that exist for profit and purpose are now commonplace. SE prioritise people and the environment, ensuring they are looked after through business – rather than as collateral of profit-making. The way SE operate has the potential to generate significant value for New Zealand and to deliver the Government's social and environmental outcomes, and embodies the ethos of the Living Standards Framework. By making minor amendments to the Companies Act 1993, this report argues that New Zealand has the capacity to create a world first model for business that enables organisations to trade for impact. And in doing so catalyse the extraordinary entrepreneurship that is happening in the SE sector in New Zealand to unlock innovation that will create greater wellbeing for generations of New Zealanders to come.

DISADVANTAGES PERCEIVED BY SOCIAL ENTERPRISES ASSOCIATED WITH THEIR LEGAL STRUCTURES

CURRENT LEGAL STRUCTURES:

A SOLUTION COULD:

MISSION

Do not clearly signal that SE trade with impact/mission front and centre (i.e. purpose is prioritised over profit).

Allow companies trading for-profit to opt-in to provisions that enshrine mission/impact statements in its rules/constitution.

Do not reflect the very nature and function of SE (i.e. as being neither distinctly charitable nor for-profit).

Provide a recognisable variation to the company model that is the vehicle for businesses using company structures to trade for impact. Other legal structure options would still be available for traditional charitable, cooperative or for-profit entities.

Do not recognise the value of the impact generated by SE and the higher levels of skill/efficiency required for social entrepreneurs to sustainably and at scale trade to create that level of social, cultural and environmental impact for New Zealand.

Through the involvement of central government, recognise and legitimise the value created by SE. This recognition would help SE in the tendering/contracting process show how it can meet social, cultural and environmental outcomes.

FUNDING

Make it difficult for SE to access equity funding, being the issuance of shares in the company in exchange for capital, because:

- maintaining ownership of the shares is a way to protect the mission of the SE;
- SE with charitable status cannot distribute dividends to private shareholders;
- multiple classes and types of shares (including, in structures with cooperative ownership models) add complexity to structures that is expensive and makes them unrecognisable or confusing for investors.

Put mission front and centre so that SE do not need to rely on owning all of the company's shares or applying for charitable status to convey and protect the mission of the enterprise, thereby allowing social entrepreneurs to seek capital investment from external investors with confidence, and allow investors to more easily recognise the impact that they can invest in.

CURRENT LEGAL STRUCTURES:

Based on the existing binary model of charitable vs for-profit are unsuited to non-charitable entities trading for impact. This mismatch makes it difficult for SE to access philanthropic funding, which is commonly restricted to registered charities to prevent any risk of personal gain that would affect the charitable status of the philanthropic organisations.

Have historically been used to separate 'doing good' from profit-making. Therefore, SE face difficulty using the current structures to convey the importance of their impact and commerciality. This makes it harder for SE to access funding from banks and traditional lending institutions that are also built on this traditional separation of companies trading for profit and charities delivering impact through grants and volunteer services.

A SOLUTION COULD:

Be a recognisable entity with appropriate reporting and accountability measures that achieves social, cultural and environmental impact that can be expressly included in grant offerings and impact investing criteria.

Reflect the growing movement toward adopting business models that pursue multiple values (i.e. impact as well as profit). The legitimacy afforded by this public recognition may remove some of the hesitancy and caution of lenders that results in the lenders turning SE away for being too risky or not commercially sound at-a-first-glance.

INNOVATION

Either require only basic reporting for non-charitable companies or onerous financial and performance reporting for charitable entities.

Include accountability and reporting measures that show impact, but recognise the commercial nature of the enterprise.

Being modified and adapted for SE are becoming unwieldy, expensive and administratively burdensome multiple-entity structures.

Provide a single model that has the essential requirements of SE, thus removing the need for multiple-entity structures.

Present additional burdens for SE that are not faced by for-profit companies. This status quo does not reflect the benefit, which New Zealand gains from SE generating impact addressing current social, cultural and environmental issues in New Zealand, that instead should be enabled and encouraged.

Provide an identifiable model, recognisable to stakeholders, to partner with or provide funding and support to, to achieve policy goals (for example, meeting criteria for social outcomes set out in the Government rules of procurement or the Living Standards Framework).

PART ONE: INTRODUCTION

1.1 Social enterprise and legal structure

Social enterprise (SE)¹ is about creating impact as well as profit. SE is neither distinctly charitable nor for-profit, and have in many cases only a passing resemblance to these two characterisations, instead operating with varying degrees of a different logic. SE manifest and express a different set of values from traditional for-profit business and, consequently, the value outputs of SE include a combination of human, social, cultural, and environmental capitals as well as financial capital. While business in this form is not new in Aotearoa New Zealand, the last century has seen the economy orient towards a distinct binary between for-profit business and charity. In effect, different versions of value have been allocated to one side or the other of this binary: financial value being the motivation for, and output of, for-profit business. Other forms of value (as in human, social, cultural, and environmental) are found in the domain of 'charity', being the exclusive realm for 'doing good'. In the business domain, money is made, and in the charity domain, money is received. For the most part, this distinction is supported by legal structures, and reflected in the shared societal understandings of what charity as a prescribed way of 'doing good' is allowed to be, and what doing business is required to be.

Conducting an enterprise where financial value along with other forms of value are given equal weight in the process of trading in New Zealand is possible: the increasing number of SE organisations in the New Zealand economy attest to this. But these do not exist because the available legal structures facilitate the establishment and operation of SE. Rather, SE is happening in this country despite hurdles caused by legal structures. SE in New Zealand exist because of the failure of the dominant economic system to entirely look after the social, cultural, and environmental imperatives that are integral to New Zealand society. Importantly, this is also what the introduction of the Living Standards Framework (LSF) from the New Zealand Government is about. The alignment between what SE has been doing for a long time, and what Government is beginning is profound – and why the development of the SE sector will unlock significant benefits for New Zealand.

Why do this research now?

In March 2018, responding to the submission of a discussion document on a new legal structure for SE in New Zealand (*Ākina 2017*), the Hon. David Parker, Minister for Economic Development, sent a letter to Louise Aitken, Chief Executive of Ākina Foundation, stating:

"Ministry of Business, Innovation and Employment (MBIE)... agrees that acts designed for not-for-profit entities do not suit the needs of social enterprises."

MBIE has advised, however, that it views the Companies Act to be accessible by social enterprises. It does not consider that the report provides sufficient evidence or examples of where social enterprises have been hindered or disadvantaged by the Companies Act. To understand your concerns better, we would be interested in learning about specific examples of social enterprises that have been unduly affected by the perceived challenges associated with their legal structure."

In this report we detail specific examples of hindrance and disadvantage that arise from the current legal structures, sometimes directly, other times in more oblique ways. Our insights are based on ethnographically-informed interviews and an online survey (see Appendix C for more details on the methodology).

Structure of this report

PART ONE of this report outlines the scope of the research and provides detail about the conceptual framework that sits as background and orientates the analysis we have used. In particular, it looks at:

- Social change that is happening in New Zealand.
- The LSF that Treasury and the rest of Government are embracing, and how SE is leading the way in doing business in a way that echoes the sentiment of the LSF.
- The relationship between SE as a mode of doing business, and what 'charity' and 'for-profit business' are within New Zealand's dominant economic reality.

PART TWO of this report looks at the ways legal structure affects SE, where legal structure is a direct barrier, or a symptom of an economic system that is hindering SE in this country:

Section 2.1: Mission vs legal structure.

Section 2.2: Funding vs legal structure.

Section 2.3: Innovation vs legal structure.

PART THREE looks at what can be done to alleviate the situation and the opportunity New Zealand has to lead globally in this space.

APPENDIX A lists, with brief bios, the SE organisations and other stakeholders involved and/or associated with the SE ecosystem that we spoke with through the course of this research.

APPENDIX B comprises more detailed case studies of ten SE and their relationships with legal structure.

APPENDIX C gives more detail on the methodology and research process we have used.

¹ Definition of SE and community enterprise (CE): SE are purpose-driven organisations that trade to deliver social and environmental impact. CEs are purpose-driven organisations that trade to deliver social and environmental impact within the community that it was established by. Unlike SE, however, CE do not allow for private gain (beyond usual salaries). Unless specified, references to SE throughout this document will refer to both SE and CE, and any references to the singular may include the plural.

1.2 Conceptual framework

1.2.1 Social change in New Zealand

Social change is happening in New Zealand as a consequence of environmental degradation, and growing inequality. This has manifested in most aspects of life, from the increasing number of children living in poverty, to increasing rates of suicide and mental illness, to the economic and social fragmentation of communities around the country. The way the general public, the business community, and Government are responding to these realities is multifaceted out of necessity. Cliff Colquhoun from CBEC, a Community Enterprise (CE) operating across Northland, identifies this and notes,

“It’s all about energy levels... it feels like that has only really kicked in in a really meaningful way in the last few years. It’s almost like, when you look at corporate New Zealand, it’s only been in the last two years that there’s been this road to Damascus type experience for them, where suddenly you’re seeing the big corporates see the light and try to genuinely do some stuff of significance... In the last election, that discomfort of people showed... the issue of poverty was raised a lot. And I think most people in New Zealand go, ‘I’m not comfortable with what I see, and I want it to change.’ So, that’s a mind shift, no matter where you are in New Zealand, people are going, ‘oh, somethings got to be done about this. We don’t like New Zealand this way.’”

The growing consumer demand for ethically, environmentally, and sustainably produced products and services is a phenomenon that is growing globally and is now discernible as ‘personal social responsibility’ (PSR). A number of the SE we spoke with are catering for this market – and their businesses are growing. Consumer demands on corporates to do more than what has passed as standard corporate social responsibility (CSR) attests to the change and evolving economic parameters that SE are uniquely placed to leverage.

The Government is responding to these broader societal changes by aligning policy directives with the conceptual understanding of the prevailing socioeconomic dynamics. Treasury is looking at more nuanced frameworks to measure and develop policy. The LSF “has been developed by Treasury to consider the collective impact of policies on intergenerational wellbeing” (*New Zealand Government 2018:1*). The approach is about the consideration and analysis of human, social, cultural, and natural capital, as well as financial capital, as contributing factors to the wellbeing of New Zealanders. The focus of Treasury is currently pragmatic and exploratory, and

the set of discussion papers (King, Hiseynli, and MacGibbon 2018; Frieling 2018; Morrissey 2018; van Zyl and Au 2018) are about starting a conversation on the value of these different types of capital in relation to wellbeing. This report adds to this conversation.

The SE we have spoken to in this research project are now running dynamic organisations that have fully integrated multiple forms of value as they conduct their array of enterprises with mission front and centre.

Janette Searle from Achieving@Waitakere and Take My Hands (amongst other SE initiatives) put it like this,

“I think it’s a bigger conversation, and I go back to where we place value. And how we define success, and how we define value. At the moment, a massive majority of it is around financial success and profits, and that’s how we are measuring success [for business]. Because even in those places that aren’t driven to generate profits, we’re still not measuring their success properly. So, if we had a conversation to go ‘yes, generation of financial wealth and all of that kind of stuff is one part of it, but actually, there are these other values systems that are equally important’... And I think there’s a beginning of a move towards that with some of the reporting now, so have that in the conversation, and shift perceptions around financial value being the only measure of success.”

The alignment between what Treasury are starting to do, and what SE has been doing for years with sophistication and entrepreneurship is significant. Evolving legal structures to reflect this reframing of value would unlock the potential for SE to benefit the New Zealand economy.

1.2.2 The relationship between SE, and ‘charity’ and ‘business’

In this section we seek to frame and then reconceptualise the relationship between SE and the logic where ‘charity’ versus ‘business’ is a binary. This is important because unless we understand the nature of the relationship between SE, charity, and for-profit business and how current law reflects this segmentation, the understanding of the nature of the ecosystem in which SE exists will be limited.

While Minister Parker’s letter acknowledges that the not-for profit legal structures are unsuitable for SE, it is a common assertion that a limited liability company (LLC) (often with charitable status) should be a suitable vehicle for SE, because the assumption is that SE is a hybrid of charity and for-profit business. This logic reflects the standard representation of the relationship of SE to charity on one end

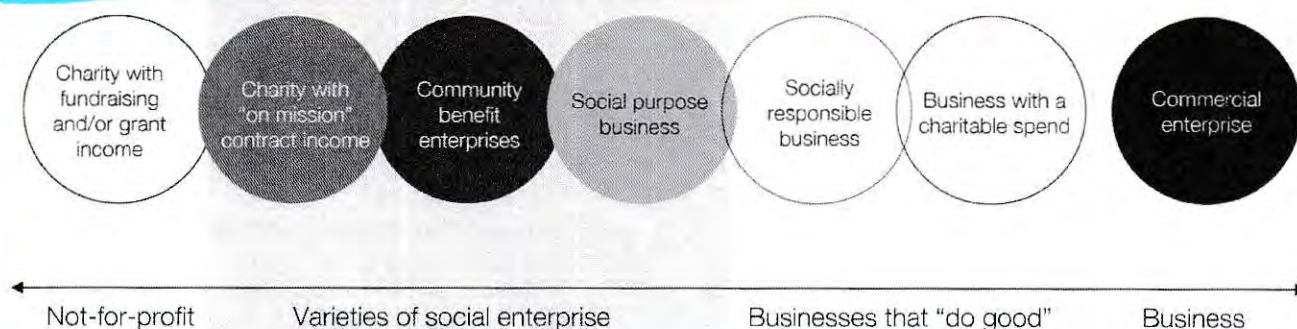


Figure 1: Prevalent charity/business spectrum, with social enterprise sitting within it.

of the spectrum and for-profit business on the other as per Figure 1.

However, while different versions of SE are represented in this schematic, the relationship of charity to for-profit business and SE is inaccurate. Many of the SE interviewed are fundamentally different to the traditional charity or for-profit business because they are founded on the basis of a different paradigm. The inclusion of financial capital along with other versions of capital as the key value outputs from SE is not merely a recipe of 'take a bit of charity and a bit of for-profit business' and combine to make SE. Rather, SE embodies a fundamental change in the motivation and methodology of doing business. We conceptualise this approach in this way:

1. Standard for-profit business and standard charity are two parts of a single whole that comprises the system called capitalism.
2. Capitalism is a subset of a broader notion of economy called 'human economy' which has a broader set of imperatives, including human wellbeing (Hart 2015).

'Human economy' existed before capitalism became the dominant economic structure and remains the model of many indigenous economies including Te Ao Māori. However, the system where personal financial profit can be pursued at the expense of the environment and the wellbeing of human beings, is not the only way to do economy. SE knows this, and this notion is regaining momentum and informing the Treasury's LSF approach to achieve a more complex analysis of policy and capital output.

The segmentation of 'for-profit business' and 'charity' as two separate parts of the economy can be visualised as follows:



Figure 2: Charity/business representation.

The characteristics of for-profit business, and of charity are kept separate from each other by strict boundaries, but that these remain the only parts of the whole is reflected in our legal structures. Interaction between the two realms is regulated to maintain the distinction. Hence, the mandate of Charities Services as gate-keeper, vetting organisations that seek to enter the charities space and declining those that generate profit for personal gain.

Representing the relationship that SE has to the charity/for-profit business binary is more like this:

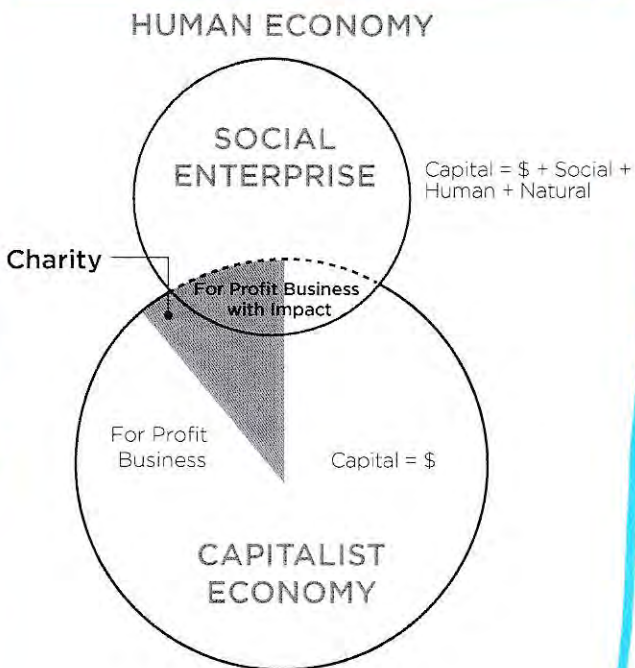


Figure 3: Representation of the human economy, and how SE sits within this.

Here, the human economy is where multiple forms of capital have value and the capitalist economy is where value is defined by financial capital alone. In this schematic, there is cross over between the charity/for-profit binary and SE which is where activity categorised as for-profit business with impact exists – these are standard businesses that do some form of good with their profit, but within the logic that dominates in the capitalist economy.

The LLC and the other legal structures available in New Zealand are products of the logic where charity and doing good are separate from doing business. Therefore, the fundamental nature of mission that is at the heart of SE is not accommodated by the LLC structure or other for-profit legal structures. While the Companies Act and the structure of the LLC is accessible to SE, in that a would-be SE can set up an LLC and get to work doing their mission as they trade, it is difficult to operate as a SE without undue hindrance, let alone thrive, without significant, entrepreneurial capacity and expensive creative legal work.

Despite this, there are some extraordinary organisations doing just that.

PART TWO: HOW SOCIAL ENTERPRISE IS UNDULY AFFECTED BY LEGAL STRUCTURE

In this section, we look at how legal structure affects the SE we interviewed, what the issues are that affect them, and how these are connected directly or indirectly to legal structure. For all the organisations we spoke with, the current legal structure options do not actively help or easily facilitate the process of doing SE – and for the most part the available legal structures are creating an environment where SE is the square peg in a round hole.

The vast majority of those interviewed said they are curtailed by their legal structure to varying degrees, sometimes directly, sometimes in more subtle indirect ways. A single organisation from the research cohort, Little Yellow Bird, who are a standard LLC and do not have charitable status, are neutral about their legal structure and are experiencing no hindrances derived from bigger structural forces in the economy.

Through this research, we have found three core themes that orientate the relationship that SE has with legal structure that debunk the contention that the LLC legal structure is accessible and sufficient to prevent a SE from being disadvantaged in New Zealand. We look at these three areas in turn:

- Mission vs legal structure
- Funding vs legal structure
- Innovation vs legal structure

2.1 Mission vs legal structure

2.1.1 The nature and substance of mission for SE

Difference by a matter of paradigm rather than degree

The variety of missions that the organisations we interviewed operate with are broad and far-ranging, but all address a social and/or environmental need. In one way or another, each SE wants to change the way the world is so that people and the environment are looked after through business – rather than business being to the detriment of people and environment. All the organisations we spoke with are committed to missions that displace the pursuit of profit and the harm that this can have on the environment and people's social and cultural worlds. The mission of a SE is not a derivative of what charity is. It is actually something quite different, Cliff Colquhoun from CBEC made this distinction,

“Most people, actually quite like the idea of what charity does, and they will choose the one they’ll put their money into... So, traditionally charities are dealing with an issue or supporting the community in some way. But they’re not necessarily about changing anything... and they enable people to feel good

by putting money in, and this helps someone who receives assistance. Whereas we’re about changing the circumstances around what’s causing the problem and the need.”

SE mission is integral to their business, and is managed on top of the usual trading activities of typical businesses. Little Yellow Bird is committed to the ethical production of cotton clothing and the creation of global supply chains that specifically address the care of the environment and people at every turn and aspect of production and supply. Samantha Jones’s agenda is nothing less than world changing as well, she said,

“My personal viewpoint is that all businesses should be operating in this whole socially respectful manner... in my opinion, every single business should have to pay the true cost of production from an environmental and social perspective.”

We asked Fraser McConnell and Alex McCall from the SE Choice how they are fundamentally orientated towards a bigger conceptualisation than merely mixing the motivations of standard charity and standard for-profit business. They said,

“Traditional capitalist business models are subsidised by the environment, they’re subsidised by people’s wellbeing and that’s not what we’re here to continue on with. We’re here to change that direction and show that business for good can be achieved using the latest and greatest technology and by putting it in the hands of as many people as possible.”

We asked Fraser and Alex from Choice about their attitude to the differing notions of personal gain that they have as a SE – and how this could be a function of millennial exuberance, rather than a fundamental shift in their approach to doing business with mission. They said,

“We don’t care about making any sort of money without purpose... if we want to be advancing society, and the SE industry, this is not going to happen by just continuing to do what we’ve always done, which is to make more and more profit... But we don’t care about that, we care about serving a greater purpose for the world.”

Pānapa Ehai from Hikurangi Enterprises, an organisation that is developing bioactives from their land to generate economic development for whānau, talked about the way they combine mission, values, and business process. He said,

“our underlying values are that everything that we do has to benefit the land and the people and the wellbeing of those...”

So, our decision-making framework that sits in place is always 'does this benefit the land and our people?' And if it does, then it can move forward into the next space of, 'is it a viable commercial process?'"

Geoff Walker from Trade Aid asserted that their mission is nothing less than changing the very nature of trading, and the essentially exploitative element that for-profit business can too easily get away with under the current system. He said:

"We're exhibiting the way we think all trading relationships should be, so we'll do things like we will pay 50-80% of our craft orders at the time of placing the order... We believe that this way we're balancing the power relationship we have with our trading partners because we're in a lucky position as New Zealanders and we can use our position to help balance the trading relationship."

Michelle Sharp of Kilmarnock considers her organisation to be a not-for loss, because no organisation can be an enterprise without making money. They trade and compete efficiently, and maximise their capacity to deliver so that they can continue to win contracts as an equal player in the field. In other words, they operate just like a for-profit business but their very reasons for existing and conducting the trade that they do, are fundamentally different from a standard for-profit business – because what is different is not the amount of business acumen and strategic vision that powers the organisation, rather it is what they use their earnings for. Their workforce is comprised of around 100 people with learning disabilities. The organisation has evolved over recent years from its former guise as an IHC sheltered workshop into the SE they are now. Their mandate is to change the marginalising and undervaluing of people with disabilities that is common place in New Zealand society, and to evolve and develop models for the future of work that embrace diversity and inclusion in world-leading ways. The education and training that they do for their workforce as a matter of course – i.e. not once profit has been calculated – is life changing for the people that work at Kilmarnock and is affecting the business community that interacts with Kilmarnock by expanding their perception of what diversity can actually be.

Eat My Lunch were committed to being a trading entity from the very start. Lisa King said:

"Our mission is to ensure that no child in New Zealand goes to school hungry... we're not trying to solve poverty or the causes necessarily, but we want to ensure that kids are coming to school, and then when they're at school, they've actually got the right nutrition, the right fuel, to help them learn and maximise the opportunities when they're at school...[we wanted] to do something about poverty, but in a sustainable and scalable way."

The missions that motivate all the SE that we spoke with go to the very heart of who and what they are, whereby the intent to create impact is paramount. In this regard, SE are not unlike charities with their commitment to do good. However, SE are intent on trading to achieve this because they believe that trade is the best way to ensure sustainability. What is even more important to SE – and this is what really sets them apart from standard charities and for-profit business – is their understanding about how the tools of business and business acumen combined with social/environmental mandates creates enterprise that is greater than the sum of its parts. Herein lies the key issue for SE: no currently available legal structure facilitates all these imperatives.

Ill-fitting identity and being 'the square peg in a round hole': Grappling with mission and legal Structure at the outset

According to our research, the current legal structures struggle to accommodate the fundamental differences in operation, motivating values, and the different types of capital when a trading enterprise is mission-led. A number of organisations talked us through the process of how they settled on their legal structure in their start-up phase, and how ill-fitting the set of options were.

Choice, for example, are working with an entirely different logic from a charity or for-profit business. Their mission is to subvert the payment structure of multinational electronic card transaction companies and its accompanying mechanisms that saddle merchants with steep fees, extract the fee from the New Zealand economy, and remove consumers' agency. The Choice technology reverses this. Choice are in beta phase of development of their system so they have considered how they need to be legally structured when their system goes live. Alex McCall and Fraser McConnell said of the initial decision-making process that they went through,

"The [available legal] structures haven't helped us a single bit... We need to figure out what is the best possible model, so that we can ensure not only that our purpose is being forefront and centre, yet also that our profit is being maximised to serve our purpose."

Organisations like Loomio and Trade Aid are examples of where their trading operation is part of showing their mission in action. They can model ways of doing fair trade in the case of Trade Aid, and working cooperatively for Loomio. So both organisations needed structures that allowed them to express their mission. Trade Aid have ended up with a complex legal structure that has been developed over their 40 plus years in business as they continually try to put mission first. As they have expanded their operation to a structure that now comprises approximately 30 legal entities of various types, the ongoing administration and compliance costs are detracting from their capacity to innovate.

Samantha Jones from Little Yellow Bird said that her company is not paying huge amounts of tax at the moment because they are re-investing in growth. However, cash flow can be an issue. The set-up of the way GST is payable when a shipment comes in from overseas for example is a pressure that all importing businesses face, but because Little Yellow Bird are paying more upfront, but are still required to fulfil their GST payment obligations as per standard business, they are in a double bind. Samantha said,

“We had a big order come in the other day [from India], and then we had to pay \$15,000 in GST upfront. Which we get back eventually, but if you’ve looking at structures or ways to help SE, not having to pay right then would be really handy.”

This is not a legal structure issue per SE, but this whole scenario is predicated on a particular way of conducting business as in paying the least amount up front so as to manage these sorts of cash flow issues. By operating as a SE, organisations can be disadvantaged by the tax system.

Income tax relief for CBEC is important, because the levels of surplus they generate via the way they are conducting business whereby they are not operating for maximum profit – but still not for loss – makes a difference. Cliff Colquhoun said,

“Recycling was never profitable in its first 15 years because we’re doing it for the good of the planet. And, so if we were paying tax, we wouldn’t have paid tax anyway because we were losing every year anyway. So maybe it wouldn’t have been such a big issue, because in real terms, as an enterprise, we weren’t making profit out of it anyway. So, was tax a big issue? I don’t know, it’s a good question actually. But as you grow more, then it definitely is a value, like, as an organisation, CBEC has a reasonable turnover, about \$5 million a year. No, we don’t make huge surplus. We might make \$50,000 to \$100,000 surplus which is miniscule. So that, taking a percentage out in tax really does affect our ability to do things in our town. So, yes, it does have an impact if you actually create a surplus as a profitable organisation like we are now, because as a community enterprise we put all our revenue back into our community, and that has an impact, definitely.”

The tax relief given to charity is to acknowledge that these organisations create impact. If SE do not default to charitable status under the current system, they end up having to pay tax and carry the cost of doing their mission. How does that recognise and enable the broader benefits these organisations are generating for New Zealand?

2.3 Innovation vs legal structure

The limiting of innovation and a process of stunting of growth is occurring in the SE sector in New Zealand, and therefore, for New

Zealand as a whole, as a consequence of the disadvantages identified in this report. SE operates in a noticeably more challenging regulatory and funding environment, making it significantly more difficult for them to find the space and resource to be able to innovate.

SE in New Zealand are born into this challenging environment, and because of this environment only the most exceptional entrepreneurs are able to succeed. This is not caused exclusively by the legal structure options available, but if strategic changes are made in legal structure, New Zealand could potentially unleash levels of innovation in this country that could make New Zealand a leader in social, environmental, and economic development. The social entrepreneurs we have spoken with in this research are finding innovative ways to trade in sustainable and efficient ways and pursue their purpose, despite a funding environment that struggles to understand what the business activity is that SE are doing and how clever it really is. Added to this is a legal environment that delineates and maintains a way of doing economy that is fundamentally different to the ways SE operate, and the taken for granted perceptions of what business and charity have long been on the part of the public and to an extent, the Government.

This is an issue because the social entrepreneurs who are innovating in the sector in New Zealand at the moment, are making New Zealand a better place and are effectively creating a more expansive version of economy for New Zealand – which is what the LSF is all about. Many SE have arisen because of failure on the part of existing solutions to look after communities, and others as responses to social, or environmental need. All have innovatively looked to the tools of market, and the process of trading with business acumen and nuanced market strategy, but with a different set of values to motivate them. Michelle Sharp from Kilmarnock expresses what all the social entrepreneurs we spoke with feel,

“The tools of business are critical to solving some of our most challenging social and environmental issues.”

Janette Searle of Achieving@Waitakere and Take My Hands amongst other SE and charity initiatives, is passionate about cross-sector collaboration to create enterprise that is greater than the sum of its parts – and the crucial role that the tools of business need to play.

“I personally have a belief that long term sustainable social change will only happen if you get all the sectors involved, and that they’re all able to work to their strengths... the role of business is not just about access to funds, it’s also about the really good models and practices that you do in business that work really well – because business has been amazing at doing what it was supposed to do: generate profits for its stakeholders. So, if you shift where you place value, you can actually say this is about generating impact and there is value in the impact, and it can happen alongside financial gain too.”

Most of the interviewees identified their charitable status as a barrier to innovation. CBEC identified that the Board of Directors that their legal structure requires affects their capacity to innovate and to be entrepreneurial with new opportunities. Cliff is a serial entrepreneur in the community space, but the governance model of their legal structure, whereby directors are publicly elected, requires considerable work, because the differential between his capacity and vision, and would-be directors' understanding of the space they work in can be problematic,

"We have a couple of people out of our nine or ten board members that change per year. So, we have to educate the new ones each time. And if you get a few vocal people who come in who have similar backgrounds that doesn't involve taking risk [it can be difficult] because what do you think their view of risk is going to be? Very adverse, and everything we do is marginal and risky."

One of the findings that has emerged most strongly from the research is the level of extraordinary entrepreneurship that is taking place in the SE sector in New Zealand - and that this is happening, for the most part, despite the legal structure options as they stand.

Entrepreneurs take risks, but they do this based on nuanced insights and perspectives on the market that they consider gives them the capacity to create and maintain a successful business. They take the componentry of the market – as they understand it – and reassemble these to create new ways of doing things. This componentry is broader than what a standard entrepreneur uses because social entrepreneurs understand how human economy works.

Imagine an environment where SE were enabled, where organisations were encouraged to be born into a structure that helps manifest all four capitals as expressed in the LSF. Imagine how this would deliver a noticeably greater wellbeing for New Zealand and its people – and how this could potentially encourage all business to output financial, as well as human, social, and environmental capitals. The authors of this report suggest that it is imperative for legal structures in New Zealand to evolve to be more enabling for SE to achieve this. The Treasury and the New Zealand Government are making great strides with the LSF. The next section sets out a series of solutions that could be applied to legal structures in this country to help SE continue to lead the way in doing business and create the sort of economy that the LSF envisages.