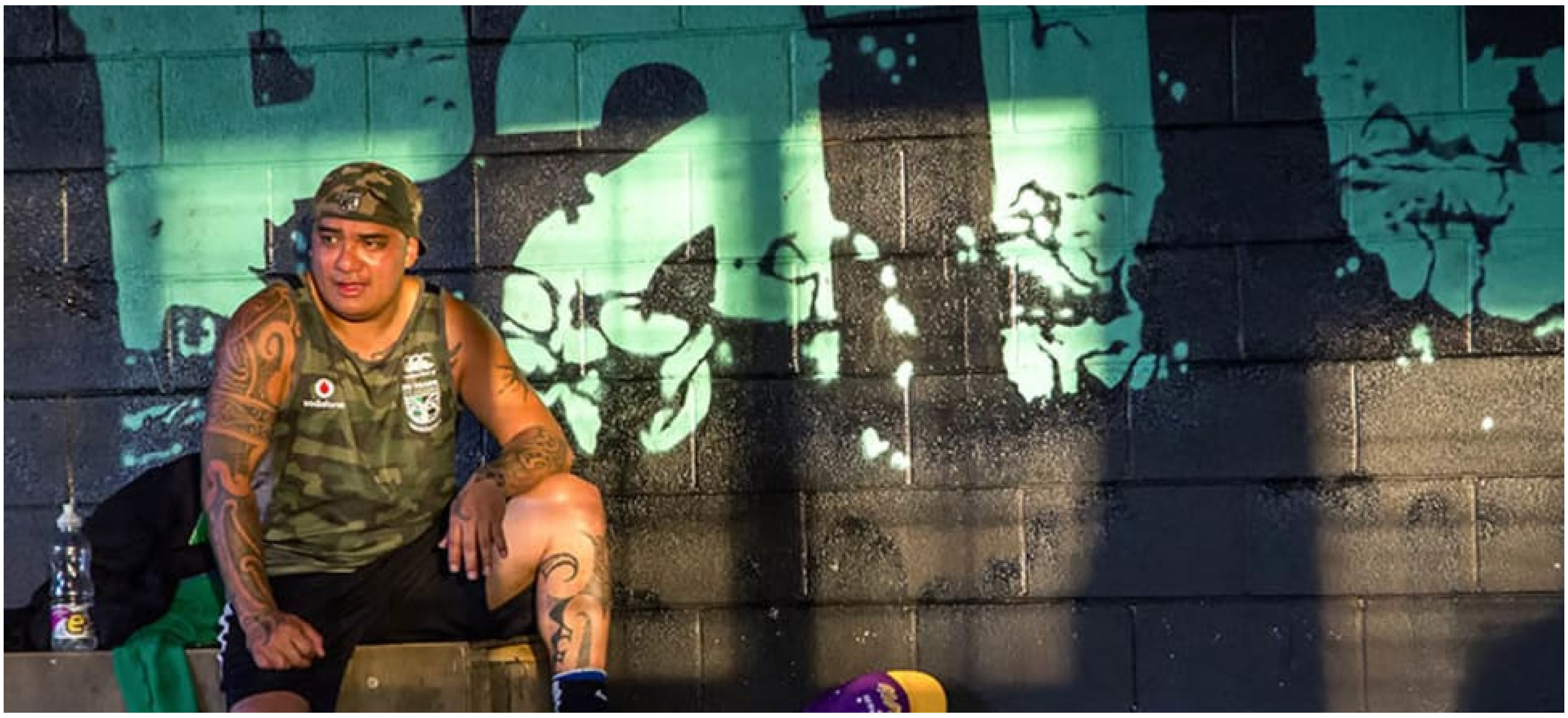
Mandow, 2019a



Whanau fitness business Patu Aotearoa is one of 3500 social enterprises contributing $1 billion to the NZ economy. Photo: Supplied

Nikki Mandow

Nikki Mandow is Newsroom's business editor @NikkiMandow.

BUSINESS

Social enterprises frustrated by NZ law

Twenty five-year-old companies' legislation is hampering the development of social enterprises in New Zealand.

And a new report presents a raft of evidence for why the Government needs to do something about it.

At the moment, social enterprises fall between two stools. On the one hand there are companies, which make money. On the other there are charities which do good. But what about social enterprises, which according to definition make money and do good? Or in many cases make money in order to do good.

Eat My Lunch is the poster child for social enterprise, with its "buy one, give one" model to feed hungry kids at school. But there are thousands of others.

A new report, ***Structuring for impact: Evolving legal structures for business in New Zealand*** doesn't have the world's sexiest title. But that belies the interest and readability of its 72 tightly-written, no-pictures pages.

Commissioned by social enterprise development organisation Ākina, with the Department of Internal Affairs and the Community Enterprise Network Trust, and funded by the Law Foundation, the report argues existing Companies Act legislation penalises social enterprises.

"New Zealand's legal structures and financial expectations are hindering social enterprises being able to reach their full potential," businessman and philanthropist Sir Neville Jordan says in the introduction to the report.

"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."

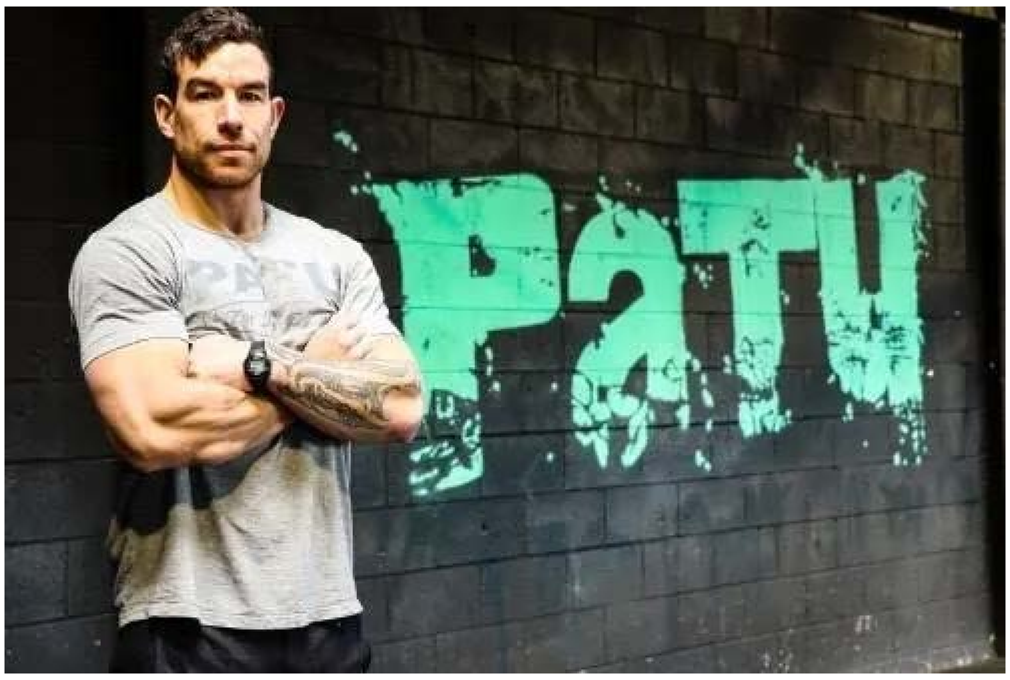
Social enterprise is growing in New Zealand, and around the world. There are an estimated 3500 social enterprises in New Zealand, contributing over $1 billion to the local economy, Ākina says. Many countries including the UK, the US, Canada and France, have legislation specifically covering social enterprises. But not New Zealand.

Here, social enterprise does not exist, legally. Instead we have only companies (for-profit) and charities (not-for-profit).

Social enterprises that choose the company model don't get the tax advantages of a charity, find it hard to access philanthropic donations, and potentially face mistrust from donors and customers questioning their "for impact" credentials. They also have no default method within the structure to signpost and protect their mission.

On the other hand, social enterprises which go the charity route can't give dividends to shareholders, are hit with onerous financial and performance reporting, and also face mistrust. Only this time the concern is about why a not-for-profit is selling stuff. They can also struggle to take on equity investment, and to secure debt.

"Social enterprises do not exist because the available legal structures facilitate the establishment and operation of SE," says Ākina CEO Louise Aitken. "Rather, social enterprise is happening in this country despite hurdles caused by legal structures."



Patu CEO Levi Armstrong

No handout model

Take Patu Aotearoa sets up gyms and exercise classes for Māori and Pacific Island whānau. The aim is to foster health and wellbeing - and to give people jobs and self-esteem.

But Patu co-founder and CEO Levi Armstrong, who comes from a gang background and whose parents were both on benefits, never wanted to go the “charity” route - neither for the organisation or its customers.

“There are just too many handouts and they don’t work,” Armstrong says. “[Whānau] expect it. They expect it all the time.”

Instead Patu was set up as a limited liability company (LLC), with Patu attendees encouraged to take out gym memberships and pay for their sessions. The money goes back into the company to expand the Patu network. These days there are 13 chapters from Kaikohe in the north to Christchurch in the south, and 3000 people involved.

"It’s frustrating. Why does Patu have to set up two entities?" - Levi Armstrong, Patu

Being an LLC meant Patu was able to get private investors. But the structure also had drawbacks because charitable grants often aren’t available to for-profits.

“We’ve had to turn down money from pub charities and foundations willing to support Patu,” Armstrong says.

So when the company needed $50,000 for research to prove to government and investors just what impact Patu was having in its communities, it reluctantly decided to set up a charitable arm.

“We wanted to prove our impact, show government how many dollars they’d save. To quantify the social return on investment. You know, to help someone lose 50kg - how much money would that save the health system? Or one of our trainers who used to be in prison but hasn’t committed a crime since he’s been with Patu, that’s $100,000 a year saved in the justice system.”

So Patu established the Meke Foundation not-for-profit to develop the Meke Meter - an app to chart finess and wellbeing progress, and also to measure social and cultural capital.

But it’s frustrating, Armstrong says.

“Why does Patu have to set up two entities? It cost $20,000 to set up the charitable trust, and that money could have been used to buy more equipment for a Patu site for a community of need.

“And then you have to find the right trustees - that was another mission. People who were on the same page understanding our vision. And having trustees means now if we want to open another gym next week we have to wait so we can run it past the trustees next month.”

Answering the Government’s questions

Louise Aitken is CEO of Ākina. She says the Structuring for Impact report has been six months in the making and came out of a discussion document Ākina wrote for Government in 2017 about setting up a new legal structure for social enterprises.

Economic Development Minister David Parker accepted at the time that “acts designed for not-for-profit entities do not suit the needs of social enterprises”. However he didn’t think "the discussion document provided sufficient evidence of 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."

Fast forward to Appendix B of the Structuring for Impact report and you have those examples. Not just Patu, but nine other case studies of Kiwi social enterprises struggling with the Companies Act as it now stands.

One of the companies featured is Northland community-owned organisation CBEC, which provides jobs in low socio-economic areas and a range of services including energy efficiency for homes, local recycling schemes, running the local swimming pools, and hiring out bikes and scooters.

"They are unable to access funding from lending institutions because they are legally owned by an individual," the report says. "Philanthropic funders can see them as too commercial; [but] local government with whom they want to contract see them as too much like a charity."

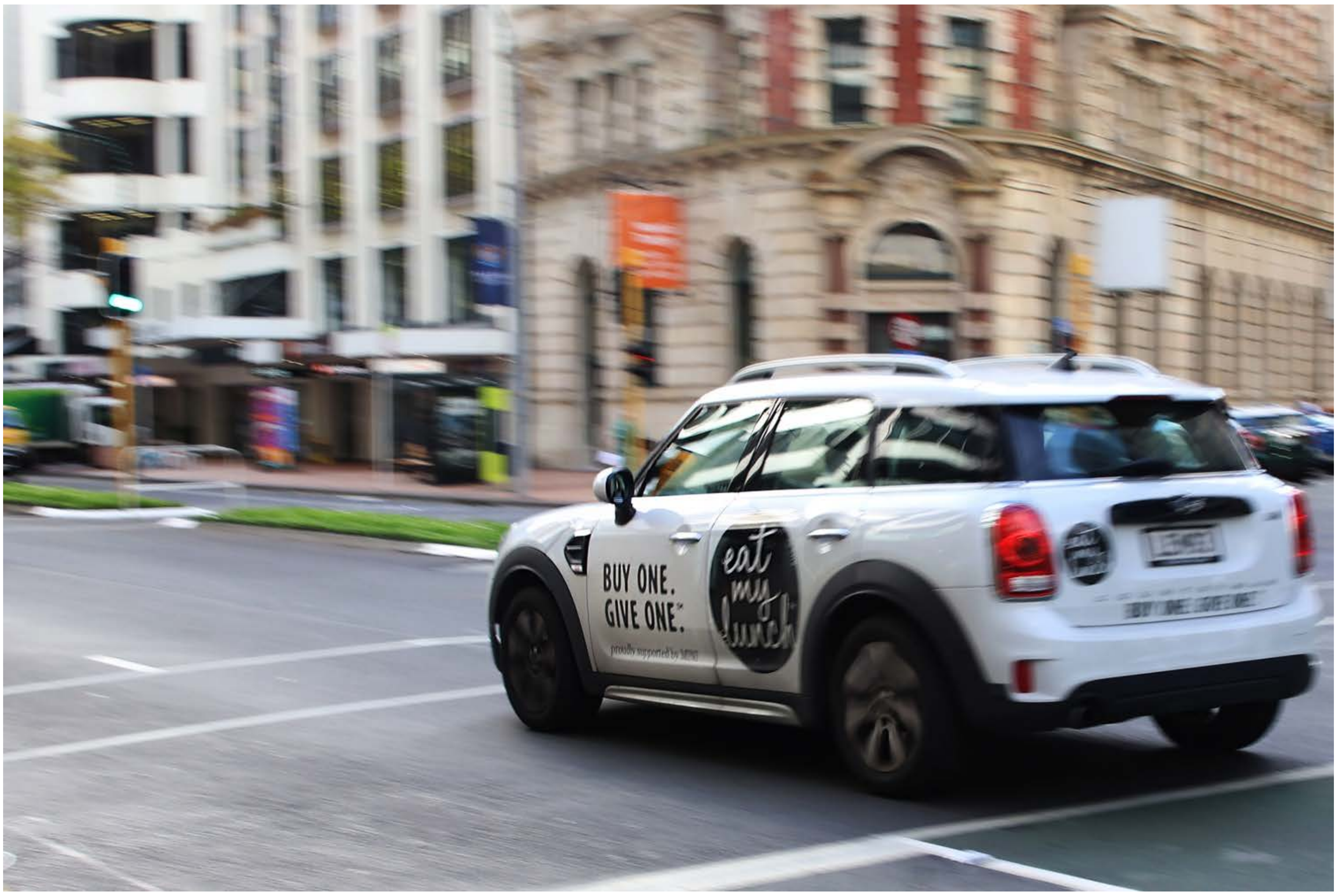
Then there's Kilmarnock, a Christchurch-based company that employs people with learning disabilities. Kilmarnock used to make Anzac Day poppies, but when it lost that contract, it branched out into all sorts of other services - from shrink wrapping to labelling, woodworking to electronic waste recycling.

The company's charitable status is "extremely important" to Kilmarnock, CEO Michelle Sharp says, "because we want to ensure that our profits are always being reinvested towards meeting our higher purpose".

But there are huge disadvantages too.

"We're more hindered by it ... Like any organisation, we need access to market ... access to finance, either seed funding or capital for growth. We need access to R&D money from time to time, to do the things we need to do, because we're trying to be innovative. Yet at the same time we haven't got access to any of those things, because of our status," Sharp says.

"It's exhausting because there's no front door to anything that we do."



Eat My Lunch has found having a charitable purpose in a commercial company model isn't easy. Photo: Lynn Grieveson

Eat My Lunch

No social enterprise report would be complete without Eat My Lunch, New Zealand's best-known social enterprise.

Founder and CEO Lisa King has similar frustrations to others interviewed for the report. She chose the limited liability company (LLC) structure from the outset, because Eat My Lunch was determined to have a "commercial element" - the "buy one" part of the "buy one, give one" mandate.

But having a charitable purpose in a commercial company made it way harder than King was expecting.

"We engaged [law firm] Chapman Tripp. At the time, it was just something that was not being done, and so it all became very complicated around, you know, how would you gift from the commercial side to the charitable? And then how would they do the giving, and what's that cost element, what's the transfer? How does the bookkeeping work, how does the governance work?"

The company could have chosen a straight business model with a charitable arm operating through a trust, but King says she rejected that early on.

"[A charity of some form] is restrictive, there's a lot of red tape, bookkeeping, we didn't want to have to run two sets of accounts, two sets of legal processes."

Having charity status was also going to have disadvantages in terms of transparency, King says. Charities have a significantly higher bar than companies when it comes to disclosure - as they should when they are spending other people's money.

"It's very unclear, very murky. No one has taken a lead on what social enterprises should be reporting on." - Lisa King, Eat My Lunch

But although Eat My Lunch looks like a charity from the outside, there are competitive pressures around the business model and the pricing.

"It's a challenge for us - how transparent should we be in the way we work? How do we make those two lunches?

"We are a private company; no one else divulges this information. But because we are seen to do the sort of work a charity does, some people think we should be as transparent as a charity, but there's IP, commercial know-how and competitive advantage we don't want to disclose to anyone."

What King would like to see in any future legislation is clear rules around what a social enterprise should report on.

"It's very unclear, very murky. No one has taken a lead on what social enterprises should be reporting on, so we've been making it up as we go along."

Meanwhile not being a charity has made it tough to get philanthropic donations, because many organisations are mandated in their constitutions to only give to registered charities.

In the case of Eat My Lunch's new kitchen, they got around this ban by having sponsoring companies buy and own the equipment and then rent it back to Eat My Lunch for a zero rental.

It's not ideal.

On the other side, having not-for-profit intentions has hindered investment - particularly early on.

“The bank manager said to us, ‘There’s no way you’re going to make money by giving away free stuff,’ so they didn’t give us a loan, so we started without any external funds.”

Ākina CEO Louise Aitken would like to see legislative change within five years. Photo: Nikki Mandow

It will happen, but when?

Louise Aitken is optimistic the change to bring social enterprises into the legal companies framework will happen.

She says the establishment of the three-year Social Enterprise Sector Development Programme, a partnership between Ākina and the Department of Internal Affairs is critical.

"We're focused on working with the Government to determine the next steps and time frames," Aitken says.

She doesn’t believe New Zealand needs full-blown new legislation - our Companies Act could be fit-for-purpose with a few tweaks.

“I’d say a refresh; it’s a 25-year-old act, but it’s a highly flexible piece of legislation ... It would be wonderful if [changes] could be in place within five years,” Aitken says.

This subject was proposed to Newsroom by Kiwibank. Kiwibank is a partner of Ākina Foundation, passionate about supporting purpose-led business, and a Foundation Partner of Newsroom.co.nz.

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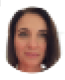

COVID-19

New: How NZ cases compare by region

As NZ moves to stamp out Covid-19 cases, Newsroom is charting the regional breakdown. Find out how many cases your region has in these easy-to-read charts.

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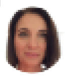

COVID-19

Quarantine measures catch 25 cases

How many international travellers came here with Covid-19, and how many have been stopped by enforced quarantine from spreading the virus? Farah Hancock shows how border controls worked

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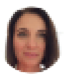

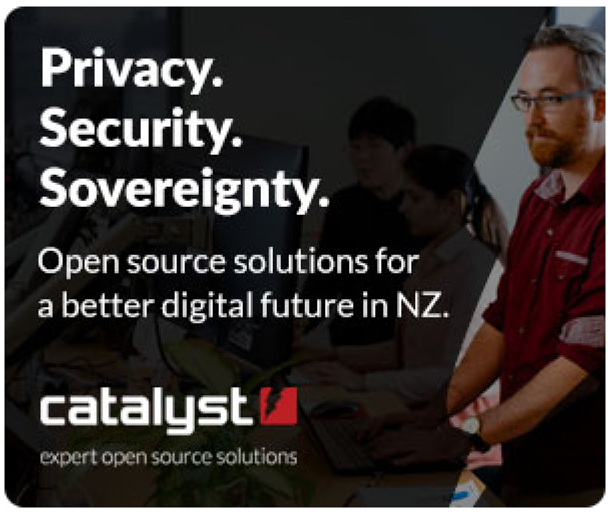

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