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# **Not just for profit: an empirical study of social enterprises in South Yorkshire.**

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Registration Number: U0371689

**A thesis submitted to University of Huddersfield Business School in fulfilment  
of the requirements for the degree of Doctor of Philosophy**

May 2011

## Contents

CHAPTER 1: INTRODUCTION .....	12
1.1 The social economy and social enterprise .....	12
1.2 Why investigate social enterprise? .....	15
1.3 Social enterprises in the United Kingdom.....	16
1.4 Focus of the study .....	18
1.4.1 <i>Research questions</i> .....	18
1.5 Structure of the thesis .....	20
CHAPTER 2: CONCEPTUALISING SOCIAL ENTERPRISE: A LITERATURE REVIEW .....	23
2.1 Introduction .....	23
2.2 Conceptualising social enterprises.....	23
2.3 Theoretical frameworks.....	24
2.4 Institutional political economy framework (IPE) .....	26
2.5 Origins of social enterprises: the industrial revolution and the social economy.....	27
2.5.1 <i>The social economy in social enterprise discourse</i> .....	29
2.5.2 <i>The social economy and the development of contemporary social enterprises</i> .....	31
2.6 Contested understanding of social enterprise .....	32
2.7 Characteristics of social enterprise .....	37
2.7.1 <i>Hybridity</i> .....	38
2.7.2 <i>Mission</i> .....	38
2.7.3 <i>Governance of social enterprises</i> .....	39
2.7.4 <i>Thematic activities</i> .....	40
2.7.5 <i>Recruitment and employment</i> .....	41
2.8 Financing of social enterprises.....	42
2.8.1 <i>Grant funding</i> .....	42
2.8.2 <i>Loans and Equity investments</i> .....	43
2.9 Legal structures and social enterprise.....	44
2.10 Choice of legal structure .....	46
2.11 Types of social enterprise legal structures .....	47
2.11.1 <i>Company limited by guarantee (CLG)</i> .....	47
2.11.2 <i>Industrial and Provident Societies (IPS)</i> .....	49
2.11.3 <i>Company limited By Shares (CLS)</i> .....	51
2.11.4 <i>Company limited by shares (social enterprise)</i> .....	52
2.11.5 <i>The Community Interest Company (CIC)</i> .....	54
2.12 Summary of legal structures .....	56
2.13 Chapter summary .....	60
CHAPTER 3: A FRAMEWORK FOR THE ANALYSIS OF SOCIAL ENTERPRISE .....	62
3.1 Introduction .....	62
3.2 The Theory of the Firm .....	63
3.2.1 <i>The theory of the firm in social enterprise discourse; profit maximisation</i> ....	65
3.2.2 <i>Internal organisational analysis and social enterprise</i> .....	66
3.3 Behavioural theory of the firm (BFT) .....	67
3.4 Emergence of the behavioural theory of the firm.....	69
3.4.1 <i>Behavioural theory of the firm and social enterprise</i> .....	71
3.5 Governance and social enterprise.....	72
3.6 Governance theory .....	73
3.6.1 <i>Agency theory (AT)</i> .....	75
3.6.2 <i>Resource dependency theory</i> .....	80
3.6.3 <i>Stewardship model</i> .....	83
3.7 Chapter summary .....	88

3.8 Key emerging issues from literature reviews .....	89
3.9 Towards a framework for analysing social enterprises in South Yorkshire .....	90
3.10 Hybrid framework for analysing social enterprises .....	91
CHAPTER 4: METHODOLOGY .....	93
4.1 Introduction.....	93
4.2 Researching social enterprise.....	93
4.2.1 <i>The South Yorkshire perspective</i> .....	93
4.3 Duration of the study.....	94
4.4 Researching social enterprises: the research design .....	95
4.4.1 <i>The research sample and sampling techniques</i> .....	98
4.5 Research methods and techniques.....	99
4.6 Data collection methods.....	102
4.7 The questionnaire survey.....	102
4.7.1. <i>Accessing respondents</i> .....	103
4.7.2. <i>Design and administration of questionnaires</i> .....	104
4.7.3. <i>Data analysis of questionnaire returns</i> .....	107
4.8 Qualitative data collection: support organisations .....	107
4.8.1 <i>Administration of support organisations' interviews</i> .....	108
4.8.2 <i>Analysis of support organisations' data</i> .....	111
4.9 Detailed case study analysis (January - April 2007).....	112
4.9.1 <i>Method of case study approach</i> .....	114
4.9.2 <i>Case study selection</i> .....	115
4.9.3 <i>Case study data collection</i> .....	121
4.10 Archival research .....	124
4.10.1 <i>National/ political context</i> .....	125
4.10.2 <i>Local context</i> .....	126
4.11. Data analysis .....	128
4.11.1 <i>Analysis of case study qualitative data</i> .....	129
4.11.2 <i>Analysis of data from documents</i> .....	131
4.12 Case study quality.....	132
4.12.1 <i>Mixed methods and triangulation</i> .....	132
4.13. Summary of data collection techniques.....	135
4.14 Ethical considerations and validity .....	136
4.15 Constraints and challenges faced .....	137
4.16 Chapter summary .....	138
CHAPTER 5: SOCIAL ENTERPRISES IN SOUTH YORKSHIRE: CONTEXT .....	140
5.1 Introduction.....	140
5.2 Nature of contemporary social enterprises in the United Kingdom .....	140
5.3 Challenges facing contemporary social enterprise in the UK.....	142
5.3.1 <i>Achieving financial sustainability</i> .....	142
5.3.2 <i>Access to funding and investments</i> .....	143
5.4 The geography of South Yorkshire.....	146
5.5 Economic history and business context in South Yorkshire.....	147
5.6 Socio-economic context of social enterprises in South Yorkshire.....	148
5.7 Social enterprise history and population in South Yorkshire.....	150
152	
5.8 Age of social enterprises in South Yorkshire .....	153
5.9 Social enterprise support organisations in South Yorkshire.....	155
5.10 Chapter summary .....	158
CHAPTER 6: RESULTS: ORGANISATION AND STRUCTURE OF SOCIAL ENTERPRISES IN SOUTH YORKSHIRE .....	160
6.1 Introduction.....	160
6.2 Scope of the case study analysis.....	161
6.3 Legal structures of social enterprises in South Yorkshire .....	162
6.4 Determinants of legal structure .....	163

6.4.1 Policy environment.....	164
6.4.2 Social objectives.....	169
6.4.3 Ownership of business.....	174
6.4.4 Access to funding.....	179
6.4.5 Access to equity investments.....	182
6.4.6 Expert advice on legal structures.....	187
6.5 Mission and legal structure.....	191
6.5.1 CLS social enterprises and mission.....	192
6.5.2 CLG social enterprises and mission.....	195
6.5.3 Balancing objectives.....	196
6.6 Summary of determinants of legal structure of social enterprise.....	198
6.7 Governance of social enterprises and legal structure.....	199
6.7.1 Board of directors, composition and purpose.....	200
6.7.2. Board functions.....	205
6.8 Sources of funding and legal structure.....	210
6.9 Nature of turnover and legal structure.....	212
6.10 Summary of financial position.....	216
6.11 Chapter summary.....	219
CHAPTER 7: DISCUSSION AND ANALYSIS.....	221
7.1 Introduction.....	221
7.2 Summary of case study analysis results.....	224
7.3. Determinants of legal structure.....	225
7.3.1 Determinants of legal structure and their functions.....	229
7.4 Governance of social enterprises and legal structure:.....	231
7.4.1 Summary of governance and legal structure.....	235
7.5 Economic sustainability and legal structure.....	236
7.5.1 CLS legal structure and financial sustainability.....	236
7.5.2 CLG legal structure and financial sustainability.....	239
7.5.3 Sources of funding and economic sustainability summary.....	240
7.6 Chapter summary.....	242
CHAPTER 8: CONCLUSION AND RECOMMENDATIONS.....	244
8.1 Addressing research questions and contributing to knowledge.....	244
8.2 Legal structures of social enterprises in South Yorkshire.....	244
8.2.1 Contribution to knowledge.....	245
8.3 Determinants of legal structures of social enterprises in South Yorkshire ....	246
8.3.1 Theoretical contribution to knowledge.....	247
8.4. Influence of type of legal structure on outcomes of social enterprises.....	248
8.4.1 Contribution to knowledge.....	248
8.5 Overall conclusions.....	249
8.6 Recommendations.....	250
8.6.1 Understanding legal structures and governance of social enterprise.....	250
8.6.2 Researching social enterprise.....	251
8.6.3 Policy implications.....	252
8.7 Further questions and theoretical challenges.....	253

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## **Appendices**

- Appendix 1: Social enterprise postal questionnaire
- Appendix 2: Interview guide 1 - Support organisations in South Yorkshire
- Appendix 3: Interview guide 2 - Social enterprise support organisations
- Appendix 4: Selected case studies interview guide
- Appendix 5: Example of a case study interview
- Appendix 6: List of the archival documents located and analysed
- Appendix 7: Categorisation of case study information
- Appendix 8: Funder's application form

## List of tables

Table 1.1: Scope of the investigation.....	19
Table 2.1: Theoretical frameworks for analysing social enterprise.....	25
Table 2.2: Social enterprise model (Pearce, 2003).....	33
Table 2.3: Perceptions of social enterprise.....	35
Table 2.4: Summary of legal structures of social enterprise.....	57
Table 3.1: Neoclassical and behavioural theories of the firm.....	63
Table 3.2: Understanding internal governance of firms.....	75
Table 4.1: Research time line.....	95
Table 4.2: Mixed –methods approach.....	101
Table 4.3: Questionnaire returns.....	105
Table 4.4: Thematic activities of social enterprises in South Yorkshire.....	106
Table 4.5: Social enterprise support organisations in South Yorkshire.....	108
Table 4.6: Key regional and national social enterprise support organisations.....	110
Table 4.7: Categorisation of social enterprise support organisations.....	111
Table 4.8: Case study classification.....	113
Table 4.9: Case studies under investigation.....	116
Table 4.10: Schedule of case study interviews.....	122
Table 4.11: Tests and techniques for establishing validity.....	134
Table 4.12: Summary of data collection methods.....	136
Table 5.1: South Yorkshire economic performance.....	148
Table 5.2: Socio-economic deprivation in South Yorkshire.....	149
Table 5.3: Social enterprise support organisations in South Yorkshire.....	156
Table 6.1: Thematic activities of case studies.....	161
Table 6.2: Types of legal structures of social enterprises in SY.....	163
Table 6.3: Criteria for accessing business support in South Yorkshire.....	166
Table 6.4: Type of legal structure and organisation's social objectives.....	173
Table 6.5: Type of legal structure and reasons for adopting legal structure.....	177
Table 6.6: Types of legal structure and availability of financial support.....	181
Table 6.7: Type of legal structure and financial objectives.....	185
Table 6.8: Availability of business and legal advice.....	190
Table 6.9: Description of organisation and financial objectives.....	193
Table 6.10: Determinants of legal structure of social enterprise.....	199
Table 6.11: Governance of social enterprise.....	203
Table 6.12: Type of legal structure and means of generating income.....	214
Table 6.13: Nature of turnover.....	215
Table 6.14: Financial health of case studies.....	217
Table 7.1: Functionality of determinants of legal structures of social enterprise...	229

## List of figures

Figure 2.1: Company limited by guarantee structure.....	48
Figure 2.2: Company limited by shares structure (NEWCO).....	52
Figure 3.1: Hybrid framework for analysis of social enterprises.....	91
Figure 4.1: Classification of research design.....	96
Figure 4.2: Key phases of the study.....	102
Figure 4.3: The Trainer description.....	117
Figure 4.4: The Landscaper description.....	118
Figure 4.5: The Cafe description.....	119
Figure 4.6: The Community Champion description.....	120
Figure 4.7: Qualitative data analysis process.....	131
Figure 5.1: The locus of social enterprise.....	143
Figure 5.2: Map of South Yorkshire.....	149
Figure 5.3: Social enterprise population in South Yorkshire.....	152
Figure 5.4: Ages of social enterprise in South Yorkshire.....	154
Figure 7.1: Determinants of legal structures of social enterprises.....	223



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## **List of abbreviations**

BLSY: Business Link South Yorkshire  
BRASS: Centre for Business Relationships, Accountability, Sustainability and Society  
CAF: Charities Aid Foundation  
CCSE: Canadian Centre For social Entrepreneurship  
CDFI: Community Development Finance Institution  
CIC: Community Interest Company  
CLG: Company Limited by Guarantee  
CLS: Company Limited by Shares  
CITR: Community Investment Tax relief  
COP: Commission on Poverty  
DSC: Directory of Social Change  
DTI: Department of Trade and Industry  
ERDF: European Regional Development Fund  
EU: European Union  
GB: Great Britain  
GOYH: Government Office for Yorkshire and Humber  
IMBY: In My Backyard  
IPPR: Institute of Public Policy and Research  
IPS: Industrial and Provident Society  
IPSEYH: Investment Plan for Social Enterprises in Yorkshire and the Humber 2004  
KFSE: Key Fund for Social Economy  
LEA: Local Education Authority  
LRS: London Rebuilding Society  
NAVCS: National association of Councils or Voluntary Service  
NEF: New Economic Foundation  
NEWCO: New Company  
OFFER: Open Forum For Economic Regeneration  
OECD: Organisation for Economic Co-operation and Development  
OFFER: Open Forum For Economic Regeneration  
RDA: Regional Development Agency  
RES: Regional Economic Strategy 2003)  
SCDG: Sheffield Co-operative Development Group  
SCEDU: Sheffield Community Enterprise Development Unit  
SEB: Social Enterprise Barnsley  
SEC: Social Enterprise Coalition  
SEDSSES: Social Enterprise Development and the Social Economy in Scotland  
SEL: Social Enterprise London  
SRB: Single Regeneration Budget  
SRI: Strategy Research Institute  
SY: South Yorkshire  
SYKFSE: South Yorkshire Key Fund For Social Economy  
SYIP: South Yorkshire Investment Plan  
SYOF: South Yorkshire Open forum  
TFSE: The Financing of Social Enterprise  
UK: United Kingdom  
UKSIF: Social Investment Task Force, UKSIF  
WEDC: Western Economic Diversification Canada

## **Abstract**

This thesis seeks to investigate the development of social enterprises in the UK. Specifically, it analyses the determinants, nature and forms of legal structures of such organisations in South Yorkshire and how these impact on their operations. In order to do so, the thesis develops a hybrid conceptual framework of analysis which is broadly informed by political economy approaches but also draws on the behavioural theory of the firm and its contractual elements. The research design of the thesis is based on a mixed method approach involving the complementary use of quantitative and qualitative data collection methods. Data from a postal survey of 102 self-defined social enterprises and semi-structured interviews of 18 support organisations in South Yorkshire is complemented by detailed analysis of four selected cases and some key informant interviews. The study findings are based on the critical analysis of two key legal structures, Company Limited by Guarantee (CLG) and Company Limited by Shares (CLS) that underpin the activities of social enterprises in South Yorkshire. While there has been an upsurge of academic interest in social enterprise over the past decade, little is known and understood about the determinants and types of social enterprises' legal structures and how these influence their operations. The thesis makes significant empirical and theoretical contributions to existing knowledge on this subject and provides new insight into understanding the determinants and formulation of legal structures of social enterprise. The investigation identifies a complex taxonomy of six exogenous and endogenous factors which influence the type and nature of a social enterprise's legal structure and its ability to achieve financial sustainability. The thesis reveals that those social enterprises with charitable, less flexible legal structures such as CLG struggle to operate as viable businesses in competitive environments compared to those with CLS legal structures. The study recommends that social enterprises adopt legal structures that allow them to maximise the extraction and delivery of value to the communities they serve.

# CHAPTER 1: INTRODUCTION

Contemporary enterprise policy discourse in the UK defines a social enterprise as a business with 'primarily social objectives and whose surpluses are principally re-invested for that purpose in the business, or in the community, rather than being driven by the need to maximise profit for shareholders and owners' (DTI 2002, p, 7). The history of social enterprises in the UK stretches back to the industrial revolution of the nineteenth century, though the concept became more widespread in the 1980s and 2000s. When the Labour party came to power in 1997, one of its flagship policies centred on the idea that markets could contribute to social welfare by complementing the state's social protection systems. The creation of viable and sustainable social enterprises was therefore at the core of the government's social reform programmes, a strategy which has continued under the current Conservative/Liberal Democrat coalition government. Social enterprise is therefore encouraged as a way of ensuring that communities generate additional resources from enterprises that contribute to the regeneration of deprived areas and tackle poverty and exclusion ( Pharaoh et al, 2004);McCabe and Hahn, 2006).In addition, social enterprises are generally regarded as a way of harnessing local social capital, an important element in promoting and sustaining community regeneration (DTI,2002). A major assumption of this strategy, however, is that social enterprises should be run not as welfare interventions but as businesses that can generate surpluses to plough back into the community. This thesis therefore examines the development of contemporary social enterprises in the United Kingdom, particularly focussing on the development and growth of such enterprises in South Yorkshire. Specifically the focus of the thesis is on how the nature of social enterprises' legal structures influences their operations and ultimately their effectiveness in complementing the state's efforts to regenerate deprived areas. Before looking at the specific objectives of this work, it is important to consider the origins of social enterprise as this helps in contextualising contemporary discourses.

## 1.1 The social economy and social enterprise

Laville and Nyssens (2001) argue that the concept of social enterprise derives from discourses on the social economy that date back to the nineteenth century. This was the time of the industrial revolution, characterised by extreme poverty and worker exploitation (Levesque et al, 2001). In an attempt to improve the welfare of

vulnerable workers and address these injustices, a number of philanthropic interventions were launched (Laville and Nyssens, 2001; Defourny and Develtere, 1999). Then as now, the term social economy refers to everything that sits outside the traditional private and public sectors, incorporating all voluntary/community sector activity (Haugh, 2005). Moulaert and Ailenei (2005) and Gueslin (1987) see the social economy as primarily focused on the welfare of vulnerable groups that were considered victims of capitalist development during the industrial revolution. The term therefore subsumes under it a number of philanthropic interventions such as co-operatives and mutual aid practices all predicated on the need to achieve social, rather than economic objectives (Laville and Nyssens, 2001).

In order to continue ameliorating the prevailing socio-economic problems, the second half of the nineteenth century saw an increased number of such philanthropic activities addressing deprivation and poverty. To some extent the social economy was, and still is, seen, as an instrument for redistributing wealth in market economies (Laville and Delfau, 2000). This view perhaps stems from the efforts the social economy organisations make in ensuring that economic growth is commensurate with social justice. Consequently over the years, we have seen extensions of social economy organisations in the form of small to medium scale enterprises (SMEs), co-operatives and not-for-profit organisations. The main objective of these interventions remains primarily to address socio-economic ills and to foster community cohesion (Moulaert and Ailenei, 2005).

In the UK, the economic upheavals of the 1980s and 1990s, characterised by a decline in the coal and steel industries, contributed to the continued development and growth of the social economy (Thompson et al, 2000). The growth of this sector in Europe has led to it being identified as a Third Sector that is neither private nor public (Levesque et al, 2001). This sector has become increasingly effective in integrating social justice and economic progress, especially through the provision of jobs in deprived communities (Moulaert and Nussbaumer, 2005). It is in this context that the development of social enterprises is analysed in this thesis because they are an integral part of the social economy. Some researchers have described them, as a 'modern incarnation of the nineteenth century of self help and cooperation' (Tropman Report, 2003). Social enterprises therefore play a combined welfare and market function. They are generally regarded as a distinct part of the much broader social economy, though some researchers have argued that any difference between these terms is purely semantic (Smith, 2005). These organisations have ideological appeal

in that they claim to plough surpluses and value back into the communities they serve in order to ameliorate deprivation (Schofield, 2005). Rather than relying on grant funding (as is the case with traditional not-for profit organisations) they engage in enterprising activities to generate profits that are used to further their social aims (Dart, 2002).

Social enterprises come in various forms such as employee owned businesses, co-operatives, development trusts, community businesses and Charities' trading arms (Peattie and Morley, 2008). However the concept of social enterprise is contentious and for many it remains confusing and unclear (Carter, 2003; Kodithuwakku and Rosa, 2002). Researchers and academics concur that there is no single definition that captures the true character of social enterprise and there is uncertainty and confusion around its 'meaning, values and activities' (Carter, 2003; OECD, 1999a). For example, the UK Department of Trade and Industry (DTI ,2002) concurs with Prabu (1999) and Paton (2003) that a social enterprise should be a business and profits that are generated should be used to reinforce the organisation's social aims. On the other hand, Dees (2001) takes a slightly different view by describing this type of enterprise as a hybrid of commercial and philanthropic methods. Social Enterprise London also regards social enterprises as competitive businesses owned and trading for a social purpose (SEL, 1999).

The above definitions of social enterprise arguably reflect the views of two distinct schools of thought. The DTI (2002) definition represents the views of those who emphasise the achievement of social aims over profit distribution .Others, such as Dees (2001), consider profit distribution to be an integral aspect of social enterprises. The former view perhaps stems from the generally agreed fact that traditionally within the social economy, there has been a stronger emphasis on achieving social rather than commercial objectives. It is only recently, as the concept of social enterprise continues to evolve, that they appear to 'blur boundaries between business and social principles', as they seek to strengthen their trading activities to further their social aims (BRASS, 2004).

Despite different views on its definition, there is consensus that a social enterprise is first and foremost, a business engaged in some form of trading to produce a surplus or profit (Stutt, 2001). Researchers also generally agree that social enterprises have three common distinguishing characteristics. These are enterprise orientation, social aims and social ownership (SEL, 2003). In addition, there is a general consensus

that the development of sustainable social enterprises is a powerful means of combating social exclusion and deprivation in disadvantaged communities. The concept of social enterprise has therefore continued to evolve around this hybrid nature that aims to create both social and economic value (Alter, 2003). The heterogeneity and diversity that characterise the social enterprise sector thus continues to be a source of debate and the dust raised by these debates is far from settling. The development of social enterprises is discussed in depth in Chapter 2 of this thesis.

## **1.2 Why investigate social enterprise?**

The above discussion has demonstrated that social enterprise is a developing phenomenon about which little is known. Despite persistent interest from academics, various aspects of social enterprises remain largely under researched compared to conventional businesses, (Doherty et al, 2009). There is no doubt however that the concept continues to evolve as social enterprises are becoming an integral component of the mainstream economies of many countries, including the UK. Social enterprise is therefore part of the drive to create new institutions with the capacity to address socio-economic problems without the support of the state. In contemporary discourse there is consensus that this type of institution needs to become more businesslike in order to survive in an increasingly global and competitive market, while at the same time retaining its key ethos (Peattie and Morley, 2008; Schofield, 2005; Dees, 1998b). These significant challenges include the current economic recession and the subsequent decline in traditional financial support systems and infrastructure for social enterprises (Flockhart, 2005; Cook, 2009). These developments are forcing social enterprises not only to look for alternative sources of financial support but also to review their internal organisational systems and processes in order to achieve financial sustainability (Simons, 2000). It appears therefore that there is a cultural shift among the social enterprise sector, underpinned by the desire to generate more income and rely less on the now severely reduced sources of grant funding (GHK Consulting, 2005). Given the resurgence of the social economy, a re-interpretation of social enterprise is therefore required, as the concept develops and evolves in response to the emerging challenges.

The development of the social enterprise concept in the context of competitive markets is a topic that is currently heavily debated by scholars and researchers (Dees and Anderson, 2003; Spear, 2001). While several key success factors and



strategies have been identified, the readiness and ability of social enterprises to operate as commercial businesses and accommodate the requirements of external stakeholders such as investors and the private sector are important areas that have escaped deeper intellectual scrutiny (Harding,2006;Alter,2006;Sharir and Lerner,2006;Brown,2007). It is therefore becoming apparent that social enterprises require a suitable infrastructure to facilitate mutually beneficial arrangements with stakeholders outside the social economy (Bank of England, 2003; Brown, 2003). A key element is a legal structure that would allow them to interact with a multiplicity of stakeholders to mobilise resources and expand opportunities, given the demand of current economic challenges (Letts et al, 1999).While researchers and academics such as Dees (2001), Alter (2006) and Mendell and Levesque (2004) agree that social enterprise should be more entrepreneurial and expand beyond the social economy, the determinants of the success of such strategies are still unclear. Contemporary discourse on social enterprise increasingly suggests that the nature of their legal structure is key to making social enterprises more entrepreneurial and enabling access to the resources and expertise necessary for their survival (Brown,2007; Barker,2002a; Martin and Thompson, 2010) .This has emerged as one of the key operational components of social enterprise that remains under researched (Peattie and Morley,2008;Alter,2004). These developments and gaps in knowledge within the social economy provide the impetus for this investigation of social enterprises in South Yorkshire. Further discussions on the motivations for this study are contained in the methodology chapter of this thesis.

### **1.3 Social enterprises in the United Kingdom**

The concept of the social economy is 'relatively new in the United Kingdom, though social enterprises have a much longer history' (Employment, 1998). Their history dates back over two hundred years. Throughout the twentieth century a number of organisations with explicit socio economic objectives have provided services and products to markets ignored by both private and public sectors (Hines, 2005). But it was only after the election of the Labour government in 1997 that central government's espousal of the social enterprise model became explicit (BRASS, 2004). Since then the concepts of the social economy and social enterprise have become central to the government's policy of tackling exclusion and deprivation. After Labour won the general election in 1997, the then Secretary for Trade and Industry Mr Byers said in a House of Commons Debate

*'The government recognises the important contribution and role that social enterprises play in the nation's economy, including helping to overcome problems of social deprivation'* (House of Commons Hansard, 2000)

This position is not surprising when one considers the history of the Labour Party itself. The Labour Party was formed in 1900 as a party of the poor, representing the working class who were faced with the harsh working conditions of the late nineteenth century Industrial revolution (German, 2000; Edmonds, 2000). The party's Election Manifestos from 1997 to 2005 revealed a clear desire to promote business growth by reducing constraints and promoting economic prosperity (Labour Party Manifestos, 1997; 2001 and 2005).

As we have discussed, social enterprises existed long before the Labour Party's election victory in 1997. Over the years, they have become attractive to politicians across a broad political spectrum as a potential vote winning strategy (Toynbee, 2006; The Economist, 2005). Some commentators, such as Brown (2002), point out that community businesses and cooperatives existed in the UK in the 1970s and 1980s. However these initiatives failed dismally despite massive public financial support. Brown (2002) argues that the size of these organisations was the main cause of their failure; they were simply too small to achieve financial sustainability. This historical perspective assists us in examining closely the concept of social enterprise so as to gain traction on the issues surrounding its contemporary development.

More often than not, prevailing political ideology determines the level and forms of support for voluntary sector organisations and non-profits (Carter, 2003). The previous UK Labour government pursued its social agenda through social enterprise development. To this effect, a dedicated unit within the Department of Trade and Industry (DTI) was established to foster the development of social enterprises (Marshall and Lovatt, 2004). The current coalition government, through its 'Big Society' strategy seeks to continue the development of social enterprises but with an increased emphasis on autonomy and viability (Schwartz, 2010). The government would like to see enterprises operating as sustainable businesses and taking advantage of all legal, financial and taxation structures available to them to achieve their objectives (Hampson, 2010; Jones, 2010).

## **1.4 Focus of the study**

The aim of this study is to investigate how their legal structures (the way social enterprises are currently conceptualised and constituted) influence the operations and outcomes of social enterprises in the UK. The legal structure of an organisation is also referred to as its legal framework (Peattie and Morley, 2008). Specifically, the empirical focus of the study is on the development of social enterprises in South Yorkshire. This region contains some of the most deprived communities in the United Kingdom, typified by the lack, or low levels, of educational qualifications, blighted local environments, low life expectancy and high levels of unemployment. Consequently South Yorkshire is one of the regions to benefit extensively from European structural funding such as the European Regional Development Fund (ERDF) after being designated an Objective 1 Area (the highest category of European Support) at the Berlin summit in 1999 (IPSESY, 2000). One of the main aims of the European Union structural funding programme is to assist in reducing economic and social disparities through the creation of sustainable social enterprises (SFCCF, 1999). The conceptual focus of this work is therefore on the determinants of legal structure and how these influence the operation and outcomes of social enterprises in deprived areas. This is pursued through three key research questions outlined below.

### **1.4.1 Research questions**

This study focuses on the development of social enterprises in South Yorkshire and the emerging outcomes after six years of European and national government social enterprise support programmes in the region. The study therefore seeks to answer the following questions;

1. What are the different types of legal structures of social enterprises in South Yorkshire?
2. What are the key determinants of social enterprises' legal structures?
3. In what ways does the nature and type of legal structure influence the outcomes of social enterprises?

This research will explore current developments within the social enterprise sector focussing specifically on how their legal structures have impacted upon their scope, nature and character. These research questions address current gaps in knowledge,

evident in the extant literature on social enterprise. The discussions in Section 1.2 and the later literature review chapters show that social enterprise is an evolving concept and is relatively underexplored from an intellectual and academic perspective. The evolution of this concept is now challenging the ideological foundation of the concept itself as it seeks to adapt to changing socio-economic and political conditions. Hence there is need for further work to understand this phenomenon.

Table 1 below illustrates the scope of the investigation and the key elements underpinning the research questions. The table shows various inter-related elements that may have an impact on the ability of a social enterprise to achieve its objectives and/or attain sustainability. In this investigation sustainability is understood as the ability of social enterprises to achieve both financial and social objectives (Dees, 1998a).

**Table 1.1: Scope of the investigation**

<b>RESEARCH QUESTION</b>	<b>KEY ELEMENTS</b>	<b>SOURCES OF INFORMATION</b>
<b><i>1. What are the different types of legal structures of social enterprises in South Yorkshire?</i></b>	<b>Analysis and evaluation of:</b> Type and characteristics of social enterprise legal structures Desired outcomes of adopting specific legal structures Opportunities and constraints associated with different types of structures	<b>Literature review: Chapters 2 and 3</b>  <b>Context: Chapter 5</b>  <b>Methodology: Chapter 4</b>
<b><i>3. What are the key determinants of social enterprises' legal structures?</i></b>	<b>Analysis and evaluation of:</b> Governance of social enterprises Motivations of social enterprise External and internal environmental influences	<b>Literature review: Chapter 3</b>  <b>In-depth case study analysis: Chapter 6</b>  <b>Discussion and analysis: Chapter 7</b>
<b><i>4. In what ways does the nature and type of legal structure influence the outcomes of social enterprises?</i></b>	<b>Analysis and evaluation of:</b> Resource mobilisation strategies Governance models Social and economic objectives	<b>In-depth case study analysis: Chapter 6</b>  <b>Discussion and analysis :Chapter 7</b>

This study seeks to identify and analyse the different legal structures of social enterprises in the UK, particularly in the South Yorkshire region. The investigation will entail a critical in-depth analysis of the culture underpinning social enterprises and the nature and effects of different forms of legal structures on their performance, governance and sustainability. Analysis and evaluation of the opportunities and constraints associated with the different types of legal structures will also be undertaken.

One of the key objectives of the investigation is to gain an understanding of why social enterprises choose particular legal structures, an area that continues to elude critical analysis despite its importance in enabling social enterprises to achieve their objectives. The analysis will also investigate the impact of key internal and external factors such as governance, ownership, remuneration and availability of finance, on the development and growth of social enterprises.

Furthermore, the investigation will critically analyse how the nature and type of legal structures adopted by social enterprises influence their outcomes. The focus will be on key elements such as governance models, resource mobilisation strategies, objectives of the social enterprises and how they are influenced by the type of legal structure. Access to appropriate funding is a challenge for most social enterprises (Bank of England, 2003). The study will assess and analyse the sources of funding available to social enterprises as well as investigate and identify possible vehicles for investment.

## **1.5 Structure of the thesis**

The thesis is structured and organised as follows;

Chapter 1 introduces the area of study, the key issues underpinning the investigation, the research questions and the rationale behind the research. Punch (2000) identifies the literature review as important in assisting the researcher to identify gaps in the area being researched. Therefore Chapters 2 and 3 contain a critique of the literature on the evolution of social enterprises and the implications of the type and nature of their legal structures.

Chapter 2 discusses the extant literature on social enterprises, critically analysing the evolution and development of the social economy and social enterprise from the Institutional Political Economy (IPE) perspective. This chapter includes a critical analysis of the legal structures associated with social enterprise and how they influence outcomes. Chapter 3 introduces the alternative conceptual framework underpinning this investigation. This is the Behavioural Theory of The Firm (BTF) which is an extension of the neoclassical theory of the firm. Contractual elements of the theory of the firm, namely Agency Theory (AT), Stewardship Theory (ST) and Resource Dependency Theory (RDT) are used to critically analyse the internal governance of social enterprise. This includes scrutiny and discussion of how these governance models influence outcomes. These approaches thus provide the basis of the epistemology of the analytical tools used in this study. Smyth (2004, p. 1) argues that a conceptual framework is useful in providing the scaffolding needed to support and guide an investigation. He goes on to add that a framework can also 'assist a researcher to make meaning of subsequent findings'. Characteristics of these analytical frameworks are applied to the analysis of the development of social enterprises and their associated legal structures.

Chapter 4 discusses the data collection methods and techniques used in this investigation. It also outlines in detail how the research design was developed to ensure that the data obtained would accurately address the research questions. The case study methodology used in the investigation rests largely on the work of Yin (1994a), Tellis (1997), Kohn (1997) and Thomas et al (1998) on various facets of this type of research tool. The parameters of the study, including its limitations and problems encountered during the course of the research are also described in this chapter.

Chapter 5 introduces the study area, South Yorkshire, and describes the UK context in order to illuminate how national policy influences the development of social enterprise in South Yorkshire. The challenges that social enterprises face and how they seek to address them are, also discussed. Background information on the South Yorkshire region is presented and analysed, particularly focussing on socio-economic conditions and their impact on the development of social enterprise across the region. Relevant regional information, drawn from quantitative data on social enterprises across the region together with secondary information is analysed and used to discuss contextual issues in this chapter. Chapter 6 contains the results of the in-depth analysis of four case studies. Evidence to support the analysis is also

drawn from descriptive statistics from questionnaire returns as well as semi-structured interviews undertaken in the investigation. This is done through tests of associations between key emerging themes from case study analysis and the quantitative data collected in this investigation.

Chapter 7 contains further analysis of emerging results from case studies across South Yorkshire. Links are also made to the results, research questions as well as theoretical frameworks discussed in chapters 2 and 3 to reinforce knowledge of what we know about social enterprises. Finally, Chapter 8 concludes and makes recommendations, illustrating this thesis' contribution to our knowledge of social enterprise. Suggestions are also made for future research.

The next chapter focuses on the literature on social enterprise.

## **CHAPTER 2: CONCEPTUALISING SOCIAL ENTERPRISE: A LITERATURE REVIEW**

### **2.1 Introduction**

This chapter reviews the literature on the development and evolution of social enterprises in the United Kingdom. The purpose of this literature review is to establish the current state of knowledge on the social economy and social enterprises and to identify key trends and gaps in this knowledge. The chapter also looks at various ways of analysing the origins and emergence of social enterprises through selected theoretical frameworks and identifies the framework that will be used in this investigation. These analytical frameworks are compared and contrasted and the rationale for their use explained. This comparison is important in ascertaining their contribution to our understanding of the development and evolution of the concept of social enterprise. This chapter also focuses on existing empirical work and how it has contributed to what we know about social enterprises. The chapter is divided into four sections. The first introduces the concept of social enterprise specifically focussing on how it is understood in contemporary discourse. The second introduces the theoretical frameworks of analysis and uses them to scrutinise the origins and development of social enterprise. The third analyses the characteristics of social enterprise and the ideology underpinning the concept. The last section discusses and analyses social enterprises' legal structures and how they influence their operations.

The next section introduces social enterprise and how it is understood in contemporary discourse.

### **2.2 Conceptualising social enterprises**

The concept of social enterprise is relatively new, underdeveloped and inherently complex (Peattie and Morley, 2008; Heath, 2006). Social enterprise has grown over the years, becoming an integral feature of most national economies (Simons, 2000; Johnson, 2000). The discussion in Section 1.1 reflects the complexity of social enterprise and the lack of consensus on its nature and characteristics. However, researchers and academics generally agree that a social enterprise is a business that seeks to bring people and communities 'together for economic development and



social gain' (Martin and Thompson, (2010, p.6). Alter (2004, p.1) puts it more simply as the new 'institutional animal, which is part business and part social'. Unlike conventional commercial businesses, surpluses or profits generated by social enterprises are reinvested into the organisation to develop its capacity to deliver more services or goods to the communities that they serve (Barker, 2002a; Reis, 1999; DTI, 2002). This implies that there is no distribution of profits or material gain to those that are involved in the enterprise (Martin and Thompson, 2010, DTI, 2002). Social enterprises are therefore, by their nature, embedded in the communities they serve. They come in a variety of forms such as development trusts, co-operatives, social firms, credit unions, community finance initiatives, community businesses and trading arms of charities (Marshall and Lovatt, 2004). The social enterprise concept has developed from a complex framework involving economic, political and social changes and has a longer history than that of the corporate sector (NEF, 2001). As well as in Europe, social enterprise has been researched and debated in the United States of America for some time, culminating in the Social Enterprise Initiative started by the Harvard Business School in 1993 (The Economist ,2005).

### **2.3 Theoretical frameworks**

The challenges facing social enterprises and their need to operate as sustainable businesses is taken as the starting point in developing this research's conceptual understanding and locating this understanding within the broader theoretical discourse .Contemporary social enterprise literature largely dwells on practical elements of social enterprise and there is a dearth of intellectual analysis to frame this emerging concept. This chapter therefore seeks to establish ways in which social enterprise can be conceptualised and unpacked for detailed analytical treatment in this thesis. From an academic perspective, social enterprise is a relatively new area of study as the discussions in Chapter 1 and Section 2.2 above illustrate. As an emerging concept, there is very little theoretical development and research on social enterprise in contemporary literature and so most of the work derives from a framework of political, economic and social changes (Johnson, 2000). A review of the literature identified Institutional Political Economy (IPE) and an extension of the theory of the firm, Behavioural Theory of the Firm (BTF), as the key analytical approaches to the emergence and evolution of social enterprises which will be used in this investigation. The contractual elements of the theory of the firm, namely Agency Theory (AT), Stewardship Theory (ST) and Resource Dependency Theory

(RDT), will also assist in framing this emerging area of research and analysing the historical vacillations of social enterprises. These approaches have been drawn from the fields of economics, psychology, sociology and managerial sciences in order to critically analyse the development of social enterprises. Further consideration will be given to the methodological implications of using such approaches in the analysis of social enterprises in South Yorkshire. The selected theoretical frameworks are shown below in Table 2.1 which highlights their theoretical contribution to the understanding of the development and evolution of the concept of social enterprise in this investigation.

**Table 2.1: Theoretical frameworks**

	<b>Institutional Political Economy (IPE)</b>	<b>The Behavioural Theory of the Firm (BTF) &amp; its contractual elements</b>
<b>Analytical Concepts</b>	The state, welfare provision, society and markets	The firm and governance
<b>Theoretical Approach and Normative Commitments</b>	Historical institutionalism Economic transformation Economic justice	Institutional economics Non-profit management – aligning market dynamics with social outcomes Internal organisation and economic efficiency

Table 2.1: Adapted from Gonzales (2008), Bowen (2007), Cyert and March (1963), Dees and Anderson (2006)

The above table provides a conceptual understanding of how social enterprises are critically analysed in the literature. The analytical concepts and associated theoretical approaches as well as normative commitments illustrated will be discussed in succeeding sections.

In order to critically analyse social enterprise further, it is important to gain insight into how this concept emerged and evolved into its contemporary form. The following sections therefore focus on our understanding of social enterprise deriving from the Institutional Political Economy (IPE) discourse that expands on the key constructs shown in Table 2.1 above. The section commences by introducing the IPE approach and its implications for the analysis of social enterprise.

## **2.4 Institutional political economy framework (IPE)**

The literature associated with the IPE framework has its foundations in the work of Karl Marx, John Commons, Thorstein Veblen and, most recently, Ha-Joon Chang. Chang (2002) identifies the three distinguishing characteristics of the IPE framework as analysis of the state, politics and markets as shown in Table 2.1. He argues that greater understanding of the market can be achieved by a deeper understanding of the institutions that are affected by or affect it (p.552). Markets are considered to be essentially political constructs; it is not possible to separate economics from the political and social system within which it is embedded, a view shared by Hodgson (1998). More crucially, the state is considered to play a key role in influencing the behaviours and motivations of individuals and institutions.

The IPE approach provides a model to discuss and critically analyse the evolution of the social economy as an example of capitalism and surplus value extraction working for a greater common good rather than for the benefit of an individual. Crucially, the framework suggests that the ideological significance of social enterprises cannot be divorced from the functional elements of a capitalist economy. According to Commons (1931) the approach focuses on the legal foundations of the economy and the evolutionary processes by which institutions are established and changed. The framework therefore is underpinned by discussions and analysis of the historical development of the social economy and social enterprise. Work will often focus on structural elements and the space occupied by institutions within a broader social structure (for example, see Hodgson (1998) and Chang (2002). Historically, public policy and state intervention have played a major role in addressing problems of the capitalist state through pro-poor social and welfare reforms (Po-hi, 2003; Gonzales, 2008). Work done under this framework therefore sees social enterprises as having evolved from a sector associated with socio-political action (Nyssens, 2005). It is clear that the IPE approach prioritises the historical analysis of the evolution of capitalism and how social enterprise as a concept has emerged from the social economy (Po-hi, 2003; Moore, 1963). The origin and evolution of social enterprise are key constructs of the IPE framework as illustrated in Table 2.1.

The IPE approach has been criticised by neo liberal economists such as Coase (1992) and Friedman (1962) for the importance it attaches to the role of the state in the market and welfare provision. These researchers and their like minded

contemporaries cast doubt on the impartiality of the state in providing sustainable welfare solutions in the face of globalisation and increased competition (Chang, 2002; Gilbert, 2002). Gonzales (2008) also suggests that the IPE fails to recognise the impact of other factors, in addition to the state, in policy formulation and implementation. IPE has been criticised for failing to recognise the impact of changes in the global economic environment on the state's fiscal policies and its ability to provide adequate public services (Atkinson, 1992; Castells, 1997).

For this work however, the IPE approach enables us to gain a deeper understanding of the rationale and impetus behind the legal set up of social economy organisations distinct from other forms of private enterprise. More importantly, IPE's focus on structural analysis makes it possible to analyse the asymmetric power relations between the state, markets and society (Gonzales, 2008). These are the three key features that are considered in developing an analytical framework for this work as shown in Table 2.1.

In the next section we take a detailed look at the development of the social economy, a key construct of the IPE framework.

## **2.5 Origins of social enterprises: the industrial revolution and the social economy**

The concept of the social economy underpins contemporary understanding and analysis of social enterprises. Most researchers agree that the industrial revolution of the nineteenth century, characterised by rapid industrialisation and harsh economic conditions, probably marks the beginning of the social economy (Hines, 2005; Moulaert and Ailenei, 2005; Mendell, 2005). Extensive analytical work undertaken by (Borzaga and Defourny, 2001; Defourny and Develtere, 1999; Moulaert and Nussbaumer, 2005; Carpi, 1997; Laville and Nyssens, 2001; Moulaert and Ailenei, 2005; Polanyi, 1957; Chang, 2002) provides an interesting etiology of the social economy by focusing on its establishment and growth. Seminal works, such as Polanyi (1957), concur that in the nineteenth century the social economy was seen as a counter-narrative to the pervasive exploitation of labour by the capitalist modes of production prevailing at the time. However, some researchers such as Defourny and Develtere (1999) argue that the social economy predates the industrial revolution, citing the early Roman Colleges of Craftsmen. Despite these differences over historical origins, researchers generally agree that the staggering technological

advancements and innovation of the industrial revolution led to the creation of the first world economy as well as social economics (Lindsey, 2005; Gueslin, 1987). Polanyi (1957) describes the nineteenth century socio-economic environment as an intense struggle between the free market system and protectionism i.e. the protection of elements of production from being fully commoditized. This struggle resulted in the emergence of various programmes and institutions aimed at improving the welfare of workers (Moulaert and Ailenei, 2005) which are often seen as the forerunners of the social economy as we know it today. McClelland (1963) gives a bleak overview of the socio-economic situation during this period, using an analogy of a garden where plants crowd each other out as they grow to describe free enterprise. Those plants which are crowded out represent the alienated and vulnerable industrial workers. McClelland's observations referred to the effects of the internal logic of a self-regulating market system which led to industrial workers being the inevitable casualties of rapid industrialisation (Alan and Thomas, 2000; Levesque et al, 2001). This harsh macro-economic environment with rigidity of wages and a highly inflexible labour market offered few opportunities for workers to escape poverty or exploitation (Moulaert and Nussbaumer, 2005). The development of the social economy therefore emerged as a key intervention to improve public services and human development (Bridge to social economy, 2003). The exploitative nature of the capitalist system provided the impetus for philanthropists to explore ways of alleviating poverty and deprivation (Bruyn, 1997; Monzon, 1989).

In the UK, the Friendly Society Acts of 1757 and 1797 resulted in the formation of various organisations that were, from a juridical point of view, co-operatives and mutual societies (Conaty and McGeehan, 2000). These entities' activities were primarily aimed at addressing the upheavals of the industrial revolution (Alter, 2006; Mendell and Levesque, 2004). Other typical examples included savings clubs or 'coffin clubs' (Conaty and McGeehan, 2000). Bridge et al (2009) refer to these developments as utopian socialism underpinned by a focus on the values of cooperation and mutual support. The main characteristics of these organisations included the associative structures they adopted and their dedication to addressing the socio-economic problems of industrialisation (Levesque and Mendell, 1999; Laville and Delfau, 2000). The Industrial and Provident Society Acts of 1852 and 1862 provided some form of legal status (Conaty and McGeehan 2000) but the emphasis was on the welfare of people rather than assets (Favreau and Levesque, 1997). These organisations were democratically managed and were dedicated in perpetuity to addressing deprivation rather than being run as businesses (BRASS,

2004). Defourny and Develtere (1999) argue that the political and ideological pluralism advocated by these organisations has become a defining feature of social economy organisations as they evolve. In reality, such organizations were never meant to trade or generate profits (Conaty and McGeehan, 2000). The legislation of that period, such as the Industrial and Provident Society Act, served only to legitimise these entities rather than recognise them as potential trading entities (Pearce, 2003).

The next discussion focuses on the development of the contemporary social economy.

### ***2.5.1 The social economy in social enterprise discourse***

The various philanthropic organisations discussed above gave rise to the concept of the social economy that has continued to attract research and academic interest (Seyfang, 2001). As for social enterprise, despite this attention, the social economy lacks a precise definition (Carpi, 1997; Mendell, 2005). MSEI (2003) describes it as 'encompassing everything that sits outside the traditional private and public sectors incorporating all voluntary/community sector activity'. Similarly, Neamtam (2002) regards the social economy as including all initiatives which are part of neither the public nor private sectors. Mendell (2005) refers to it as a collection of enterprises and associations whose guiding principles are ethical and moral considerations. She goes on to say that such entities are opposed to the notion of material gain for anyone involved in them. The Bank of England (2003) describes the social economy as encompassing trading entities of various sizes and 'operating across a range of activities and for a variety of purposes'. Moulaert and Ailenei (2005) say that the social economy involves activities closely associated with the (re)introduction of social justice into production and allocation systems. These views are consistent with the historical development of the social economy as an anti capitalist initiative as discussed in Section 2.3. Just as there is no consensus on the definition of the social economy there is also a divergence of views on the types of organisations considered to be part of it. For example, Gui (1991) includes social and political organisations as part of the social economy. Kendall and Anheier (1999) even include non-governmental organisations in their conceptualisation of this phenomenon.

The differences in the above conceptualisations and definitions reflect historical and ideological struggles between neo-liberal and structuralist perspectives. Carpi (1997)

and Laville and Nyssens (2001) argue that the social economy is different from other sectors because it is characterised by the maximisation of social benefits rather than political power and financial gain. This view fits perfectly with the historical emergence of the social economy and the ethical principles associated with the phenomenon, revealing a distinct non-commercial or non-profit maximisation concept of the social economy. On a similar note, Moulaert and Nussbaumer (2005) use what they term an essentialist view in describing the social economy. Although their conceptualisation remains embedded in historical institutionalism they assert that their view is 'ahistorical' as it also considers contemporary issues associated with the development of the social economy. Moulaert and Nussbaumer (2005) describe the social economy as that part of the economy which;

1. Organises economic functions primarily according to the principles of democratic cooperation and reciprocity
2. Guarantees a high level of equality and distribution and organises redistribution, when needed, in order to satisfy human basic needs in a sustainable way (Moulaert and Nussbaumer ,2005)

Overall, the above views are consistent with anti-capitalist interventions and programmes aimed at the protection of vulnerable members of our societies from the effects of socio-economic deprivation. Other researchers such as Restakis (2006) have used the term 'old social economy' to describe such interventions. They use this term to denote the traditional philanthropic nature of the social economy devoid of commercial economic activities.

The dynamism, creativity and innovation of the sector are evident in the increased interest in the social economy and steady growth of social enterprise over the past decade (SEL, 2001a; Restakis, 2006). For example, the 1994 European White Paper on economic policy demonstrated the growing interest in the social economy in Europe. Of particular interest has been its capacity to generate employment opportunities and foster community cohesion (Employment, 1998). In 1995, it was estimated that the social economy accounted for some 5 % of total employment in the European Union (SBS, 2001). The sector has become a strategic policy instrument in the UK as well as in most European and American (North and South) governments' strategies to tackle socio-economic ills (Carpi, 1997). Such strategic developments mean that the social economy is no longer a subordinate form of production. It has become an indispensable tool for tackling deprivation and poverty

as well as enabling citizens to involve themselves in regenerating their communities through enterprise (EU, 2006).

However, despite the growth of the social economy, conceptual issues around its meaning and operational effectiveness persist (Moulaert and Ailenei, 2005). The sector remains largely dependent on both the public and private sector for support (Amin et al, 2002). Giraldez (2005) argues that the social economy should not be regarded as an economy of poverty, but an intervention that still requires the participation and support of the state. Some researchers discount the concept of the social economy altogether. For example Barker (2002a) argues that there is no such thing as the social economy and that the enduring importance of this notion seems to be both political and practical. Politically, the social economy has, in recent years, become an increasingly useful peg on which to hang regeneration initiatives and practically, it has become a convenient way of alluding to enterprise of a particular character (Barker, 2002a).

The next section considers the development of contemporary social enterprise from an IPE perspective. Institutional transformation is a key element of this approach.

### ***2.5.2 The social economy and the development of contemporary social enterprises***

Carpi (1997) described the continued growth of the social economy from its origins in the economic upheavals of the industrial revolution as an 'expression of a dynamic and creative civil society' (Carpi, 1997). He further argues that, despite its structural weaknesses, the social economy is still important in understanding the contemporary development of some of the key organisations that are associated with it, such as social enterprises.

Social enterprises are therefore not considered to be replacing the social economy but complementing and extending it through their entrepreneurial activities aimed at achieving their social objectives (OECD, 2006a; Hines, 2005; EU, 2006). Moulaert et al (2000) and Moulaert and Nussbaumer (2005) regard the development of social enterprises as a product of institutional innovation (i.e. innovation in social relations, governance and empowerment dynamics) and the innovation of the social economy itself. They further argue that social enterprises evolved because, it was inevitable that the welfare model, characterised by state support and philanthropic



interventions, would not be sustainable indefinitely. Borzaga (2007) argues that the sustained social and economic pressures on this form of support eventually caused an increased demand for service provision. Bridge et al (2009) agree, asserting that the early twentieth century political and economic turbulence emanating from post-Fordist manufacturing systems exerted pressure on the state to provide effective welfare intervention. The inability of the state to address this problem resulted in the emergence of self-governing enterprising organisations to fill the gaps (Salamon, 1994; Peattie and Morley, 2008). Some of these organisations developed into social enterprises as we know them today. To a large extent, social enterprise therefore evolved as a response to the state's failure to provide adequate public services (Borzaga, 2007, Peattie and Morley, 2008). Furthermore, serious questions were being asked about the effectiveness of traditional charitable solutions which relied on philanthropic support to address socio-economic problems (Dees, 2001).

The next section focuses on the contested understanding of social enterprise in contemporary discourse from the IPE perspective.

## **2.6 Contested understanding of social enterprise**

Despite the popularity of social enterprise, its definition remains contested (Doherty et al, 2009). Researchers and academics concur that there is no single definition that appears to capture its essential nature. As a result, as mentioned in Chapter 1, there is uncertainty and confusion around its interpretation and understanding (Carter, 2003; OECD, 1999b; Po-Hi, 2003; BRASS, 2004). Peattie and Morley (2008) argue that researchers tend to focus on the specific characteristics of a social enterprise in their definitions which then cannot be applied across the sector. Social enterprises view themselves variously according to their legal structure, their mode of operation, their functions or their relationship with communities (BRASS, 2004; Martin and Thompson, 2010; Doherty et al, 2009). The plethora of definitions associated with social enterprises highlights the lack of consensus on their typology in contemporary literature. Analysis of the various definitions of social enterprises indicates two distinct schools of thought. There are those who emphasize social aims over economic aims and those that see profit distribution as a key aspect of social enterprises.

Proponents of the first school of thought include Paton (2003), Baderman and Law (2006), OECD (1999b), Prabhu (1999), Chell (2007) and Pearce (2003). These

commentators take the view that the core aim of social enterprise is to provide social benefits rather than achieve economic objectives. Chell (2007) in particular is clear about what a social enterprise should be and what it should achieve. She insists that social enterprise exists to create social rather than economic wealth, arguing that the culture and ethos of social enterprises are based on 'principles of volunteerism, ethical behaviour and a mission with a social cause' (Chell 2007, p. 11). Others, such as Baderman and Law (2006), put it even more simply by stating that social enterprise means doing good. However, Pearce (2003) perhaps typifies researchers who are adamant that the main objective of social enterprise should be social rather than commercial. His model of a social enterprise has six tenets as shown in Table 2.2 below:

**Table 2.2: Social enterprise model**

Non distribution of profits to individuals Holding assets in trust, Democratic governance Being accountable to a constituency and community Social purpose Engaged in trade	Pearce(2003)
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Analysis of the characteristics of the above model clearly indicates a strong philanthropic orientation totally opposed to full scale commercial activities and capital gain for those involved. Peace (2003, p. 115) argues that the above characteristics 'should be fixed and therefore non-negotiable'. In essence Pearce (2003) and like minded researchers argue that the maximisation of personal gain is antithetical to social enterprise. This normative view identifies the social enterprise as purely welfare-orientated and democratic (COP, 2005; Doherty et al, 2009), and depicts a clear philanthropic orientation for them and their wider social relationships. This orientation is based on the structuralist ideological perspective which achieved credibility in the 1960s and 1970s and challenged the neo-liberal market-led tendencies of advocates of 'free markets'. Such arguments are also consistent with the historical development of the social economy from which social enterprises emerged as discussed in Section 2.5.1 above. We have already seen that the social economy has been strongly associated with the achievement of social aims rather than economic objectives. Chell (2007) says that historically, social enterprises have been modelled on what she refers to as the tenets of not-for-profit charitable

organisations. In this regard, social enterprises continue to uphold/resist the destruction of the mutual system, typified by limited trading and resistance to globalisation. Billis and Harris (1996) concur with this view. They argue that, by concentrating on achieving social objectives, social enterprises are much more likely to respond more effectively and sensitively to states of disadvantage than are for-profit enterprises. It is hardly surprising therefore that the continued survival of such organisations is to a large extent reliant on grants, rather than generated income.

The above analyses have also shown that, to some extent, the objectives of social enterprises are linked with how they define themselves. For example, most such organisations describe themselves as not-for-profit, implying either that they are not trading or they are not making a profit (BASSAC, 2002a). As Battenheim (2002) argues, social enterprises are having a problem with this mentality, if they are to achieve their socio-economic and environmental objectives. Consequently there is now a growing movement of researchers with different views on how social enterprise should develop. These regard trading as an integral part of social enterprise. For example while Westall (2001), Dees (1998), Barker (2002b) and Defourny (2001) retain the emphasis on common ownership in their definitions of a social enterprise, they also recognise the significance of trading and market relationships.

However, other commentators have different views on the nature and character of social enterprise. They regard the generation of surpluses and commercial activities (in addition to the delivery of social value) as key components of a social enterprise's objectives. They argue that profit and not-for-profit organisations should not be differentiated (Leat, 1998). For example, Dees (2001) describes a social enterprise as a hybrid of 'commercial and philanthropic methods'. Marshall and Lovatt (2004) define a social enterprise as a business that exists between the traditional private business and public/government and charitable sectors. On the same note, Social Enterprise London (1999) describes social enterprises as competitive businesses owned and trading for a social purpose. The UK government regards a social enterprise as a business with primarily social objectives whose surpluses are principally re-invested for that purpose in the business, or in the community, rather than being driven by the need to maximise profit for shareholders and owners (DTI, 2002, p. 7). A common theme is that social enterprises should be competitive hybrid business firms, whose survival is dependent on robust business models. This

conceptualises social enterprises as seeking innovative approaches to welfare provision, rather than relying on traditional philanthropic approaches.

The above discussion demonstrates the contested understanding of the concept of social enterprise. It highlights an emerging nascent taxonomy of social enterprise which focuses on two different ideological perspectives (Johnson, 2000). Table 2.3 below summarises these two different perceptions and interpretations of the concept of social enterprise.

**Table 2.3: Perceptions of social enterprise**

TYPE OF SOCIAL ENTERPRISE		
Characteristics of Social enterprises	Philanthropic/Welfare view	Market View
Mission	<ol style="list-style-type: none"> <li>1. Purely philanthropic.</li> <li>2. Mission and value driven and embedded in the community.</li> </ol>	<ol style="list-style-type: none"> <li>1. Hybrid: - pursuit of economic and social or environmental goals</li> <li>2. Mission and value driven and embedded in the community</li> <li>3. Economic value creation through trading activities</li> </ol>
Profit/surplus management	<ol style="list-style-type: none"> <li>1. Non- profit distribution.</li> </ol>	<ol style="list-style-type: none"> <li>1. Profits/surpluses re-invested in the organisation to develop capacity and reinforce social ethos</li> </ol>
Governance and legal structure	<ol style="list-style-type: none"> <li>2. Limited or no trading</li> <li>1. Social ownership characterised by agency-principle relationship (e.g. Co-operatives, Company limited by guarantee)</li> </ol>	<ol style="list-style-type: none"> <li>2. Profits distributed to shareholders depending on type of legal structure</li> <li>1. Social ownership</li> <li>2. Allows participation of external shareholders (E.g. Company limited by guarantee, Community interest company, share capital model)</li> </ol>

Table 2.3: Adapted from Virtue Ventures, SEEP Network (2006)

Table 2.3 above illustrates the perceptions of social enterprise from a philanthropic or welfare view and a market view respectively. The welfare view constitutes an extension of the values and ethos of the pioneering social economy organisations which are the precursors of contemporary social enterprises as discussed in Section 2.4. By adopting a purely philanthropic stance they make it clear that they exist to respond to and address social needs (Mendell and Levesque, 2004). It is also likely

that a majority of these types of social enterprises would be largely reliant on grants and volunteer contributions as discussed in Section 2.5 (LRS, 2002). It is also doubtful whether such organisations could be run as successful businesses, or whether they should be called enterprises at all. This is why some researchers have suggested that the concept of social enterprise tends to be used selectively, perhaps sometimes just to access funding or specific forms of support (GHK, 2005). It is therefore unlikely that such organisations could develop the capacity to be financially self-reliant and so substitute for the state in welfare provision. Their legal structures are characterised by social ownership, grant funding and a not-for-profit orientation (Barker, 2002b). While such structures may permit these organisations to trade, their nature places severe restrictions on building a wider resource base.

Every enterprise seeks to be economically sustainable and social enterprises should be no exception (Strothotte and Wustenhagen, 2005). The market view of social enterprise shown in Table 2.3 depicts a social enterprise as a business which seeks to integrate commercial trading activities in its operations to achieve financial sustainability, despite its ideological focus on addressing social issues. The key difference from a conventional commercial firm is on how surpluses are managed, with the firm associated with profit distribution and personal gain. This view highlights the blurring of traditional boundaries between private firms and social enterprises (Johnson, 2000). It implies that a social enterprise is essentially a firm keen to ensure its survival by engaging in sustainable trading activities and forging corporate partnerships with organisations outside the social economy (Dees, 1998; Barker, 2002b; Defourny 2001; Wallace, 2005). This is consistent with contemporary discourse on social enterprises which focuses on the decline in traditional sources of income and the convergence of the private, public and non-profit sectors, in addressing complex socio-economic problems (Borgen, 2003; Murray, 2007). For example Dyson (2003) argues that dependence on grants as a strategy has failed for social enterprises and there is a need to develop new strategies for survival within the global economic environment (de Kam, 2005).

The market view therefore considers the social enterprise to be a hybrid firm that seeks to achieve both social and commercial objectives rather than a voluntary or charitable organisation (Leadbeater, 2002; Bode et al, 2004; Kosko, 1994; Martin and Thompson, 2010). Such an enterprise can respond to new opportunities in the market (Mendell and Levesque, 2004). Manning (2006) supports this view, arguing that where social enterprises have been successful, it has been largely through

pursuing commercial aims through trading without compromising their social ethos. It is important to note that the adoption of a commercial orientation does not imply maximisation of profit, but instead maximisation of value delivery (OECD, 2006b; Dees and Anderson, 2006). This is primarily because their activities involve a limited distribution of profits, particularly in the case of co-operatives and newly introduced share capital companies such as the CIC (OECD, 2006b; Peattie and Morley, 2008). For social enterprises generally, the term 'profit' is an anathema (Barker, 2002b). This is not surprising given their ideological origins in the rejection of capitalism and personal gain. The market oriented social enterprise represents a credible and sustainable alternative to the state in the provision of social welfare because it seeks to be financially self sustaining (Toynbee, 2006). Therefore this type of enterprise requires a flexible legal structure that allows it to develop and sustain commercial activities to achieve its multiple objectives. It is this model of social enterprise that this investigation considers. It must be noted however that there is no consensus on the precise definition of trading activities associated with social enterprise. There is nevertheless a general acceptance that trading activities also include income generated from public sector contracts (Gordon, 2006). However social enterprises, like any other commercial firm, have to contend with pressures from the macro-environment which are beyond their control in order to remain viable and competitive (Clift, 2000; Arradon and Wyler, 2008). In addition, one of the major challenges for them is managing the inevitable philosophical clash between non-profit and for profit cultures as well as the organisational structures required to expand sources of income beyond traditional boundaries (Etchart and Davis, 2003; Arbor, 2005; Doherty et al, 2009; Low, 2006; Barker, 2002a).

The next section focuses on a set of key social and economic characteristics of social enterprise, expanding on those shown in Table 2.3 above.

## **2.7 Characteristics of social enterprise**

Below are some key defining characteristics of social enterprises on which there is broad agreement in the literature although Shaw and Carter (2007) argue that they may not all need to be present.

### **2.7.1 Hybridity**

A social enterprise is a hybrid business that seeks to achieve a triple bottom line of economic, social and environment objectives as shown below (Bode et al, 2004).

- (i) Enterprise oriented; they seek to be viable businesses, making a surplus from trading. However, this surplus is ploughed back in the enterprise rather than being used for amassing personal wealth or distributed to shareholders (Martin and Thompson, 2010; Doherty et al, 2009)
- (ii) Social aims; they have explicit social aims such as job creation, training or the provision of local services. They have ethical and environmental values including commitment to local capacity building and environmental preservation. They are accountable to their members and the wider community for their social, environmental and economic impact.
- (iii) Social ownership; they are autonomous organisations with governance and legal structure based on participation by stakeholder groups (users or clients, local community groups, etc) or by trustees. A common legal structure for social enterprise is therefore Company Limited by Guarantee (CLG) as this permits wider participation in ownership and control of assets (SEL, 2003; Martin and Thompson, 2010, Pierce, 2003). This includes socially excluded and deprived sections of the community.

### **2.7.2 Mission**

Another key defining characteristic of social enterprises is that they are mission driven. Dees et al, (2001, p.20) defines 'mission' as the organisation's reason to exist. In most cases social enterprises are a reaction to social and economic problems, such as the closure of a factory, social exclusion or lack of employment opportunities (DTI, 2002). The development of social enterprise, particularly in the UK, has therefore tended to be clustered around areas of deprivation, although some surveys appear to challenge this assertion. For example, in one such study, only half of the social enterprises surveyed were based in areas of high deprivation, with 49% working in more affluent areas (SBS, 2005). Such results indicate the continuing evolution of social enterprise beyond traditional paradigms and its ability to survive without traditional sources of funding.

### **2.7.3 Governance of social enterprises**

Section 2.7.1 states that social ownership of the organisation and its assets is a characteristic of social enterprises. Associated with this type of ownership is a democratic model of governance that emphasises the development of trust and solidarity among those involved (Low, 2006). This type of governance has its origins in the philanthropic organisations of the nineteenth century as discussed in Section 2.5 and continues to be a key feature of the governance of contemporary social enterprises (Evers, 2001). The boards of directors or trustees associated with the governance of social enterprises are usually voluntary in nature (Barker, 2003; Pearce, 2003; Evers, 2001; Paton, 2003). The individuals on these boards do not receive any form of financial remuneration for their participation in these organisations (DTI, 2002). This is consistent with the view of most contemporary researchers on management theory and practice of non-profit organisations such as Cohen and Cyert (1965) who argue that not all stakeholders are motivated by financial considerations. Dees (2001) and Campbell (2007) argue that, despite being voluntary, such boards of directors are pivotal to the success of social enterprise because they are vital in ensuring accountability, legitimacy and transparency in the operations of such organisations. For example, venture capitalists often regard governance as one of the key drivers and determinants of success of a social enterprise and therefore this influences their investment decisions (Tranquada and Pepin, 2006). Such a governance model is likely to be driven by a legal structure that reinforces social ownership, such as the cooperative or company limited by guarantee models (Barker, 2003). These legal structures are discussed in-depth in Section 2.7 of this chapter.

Carver and Carver (2009) argue that effective board governance of non-profit organizations is, however, a rare phenomenon and that the purpose of the board in a social enterprise has not been clearly understood. In addition, while volunteer directors usually possess specific skills, expertise or knowledge that can contribute to the organisation's organic growth, this is not always the case (SEL, 2001b; Bridge et al, 2009; Barker, 2002a). Other researchers, such as Etchart and Davis (2003b) and Ridley-Duff (2002b), are of the opinion that the democratic governance associated with volunteer-dominated boards is inconsistent with the operations of a modern business. They argue that this type of governance model does not promote ownership or foster partnerships with a wider stakeholder base involving institutions beyond the social economy. In addition, Dees (2001) argues that voluntary board



members tend to have a more hands-on approach than those in for-profit organisations, making them difficult to manage.

The democratic governance model therefore implies that personal ownership and profit distribution should not be part of the defining characteristics of a social enterprise, a position strongly supported by Birkhoelzer et al (1997) and Pearce (2003). Instead, these authors suggest that shared ownership is what makes the governance of social enterprise unique and sets it apart from conventional businesses. Some researchers, however, such as Barker (2002b) and Dees (1998a), argue that shared ownership creates governance models that do not support the motivations of individual entrepreneurs such as ownership of the business and the possibility of personal remuneration, which are key drivers of enterprise.

#### **2.7.4 Thematic activities**

Thematic activities are also a major defining characteristic of social enterprises. These organisations operate in diverse thematic areas and generate significant employment opportunities (SBS, 2005). Typical thematic areas include childcare, support of the elderly, recycling and environmental preservation and provision of care for the disabled (IPSEYH, 2004; Leadbeater, 2002). Some researchers however consider social enterprises to operate in three distinct fields:

- Work integration: activities aimed at training and support of the unemployed.
- Personal services: activities mainly relating to childcare and supporting the elderly or disabled.
- Local development of disadvantaged areas: activities aimed at neighbourhood renewal or sustainable communities (EU, 2005).

The above classification reflects the purely philanthropic approach, devoid of commercial activities, consistent with the historical traditions of non-profit organisations as previously discussed. From this perspective social enterprises reinforce the mutual system in that they reject exploitation and instead 'choose to invest in society's most disadvantaged people' (Ogden Newton, 2007). However, the contemporary development of social enterprises has seen them widening their thematic areas, extending their operations from pure philanthropy to include those that are fully commercial (Dees, 2001). For example, some social enterprises are

beginning to operate in non-traditional high growth areas such as commercial transport and information and technology (Regeneration and Renewal 2005a). These developments reflect the potential of social enterprises to contribute positively to a diverse range of economic activities in the same manner as for-profit enterprises. This means that although social enterprises are mission led, they are also driven by markets (Alter, 2006). The range of activities also indicates the diverse range of skills and competencies needed to manage social enterprises (Carter, 2003). This development is inconsistent with the widely accepted view that social enterprises operate in areas of market and state failure i.e. areas where there are identifiable gaps in provision due to the inability, or unwillingness of the private sector or the state to deliver services (Simons, 2000; BRASS, 2004).

### ***2.7.5 Recruitment and employment***

A further key defining characteristic of social enterprise is their employment culture (Haberberg and Rieple (2001). Generally social enterprises struggle to create jobs in volume, or engage highly paid and skilled staff. Hence many staff are volunteers, and a very limited number of employees are paid (Evans, 2001). Volunteers constitute the majority of staff in most voluntary and community enterprises (Regeneration and Renewal, 2005b). The historical development of the social economy makes this rather unsurprising, given the nature of the organisations that have been associated with it. However the impetus behind volunteerism itself has been a source of debate. It is argued (Haberberg and Rieple, 2001; Strothotte and Wustenhagen, 2005) that the common denominator driving the involvement of volunteers in non-profit organisations is their high level of commitment to the organisation's values and mission. Such volunteers and staff often work for little or no pay. They are motivated by the satisfaction they get from the intrinsic nature of what they do. Trained volunteers can also be an invaluable asset to social enterprises and can facilitate the generation of social capital crucial for the success of voluntary organisations (Zappala et al, 2000). Pearce (2003) views unpaid labour as a key income generator for non –profits, arguing that without such help many enterprises would not survive. The role and effectiveness of volunteers, especially in assisting social enterprises to achieve financial sustainability has, however, been questioned by some researchers such as Barker (2002a). He argues that most volunteers in social enterprises, especially those at management level, lack the required business acumen and skills. Other researchers, such as Marston et al (2000) and Farmer and Fedor (1999), also argue that not all voluntary activity generates positive results or is productive,

pointing out that, while most volunteers are highly committed, they are often transient and therefore can adversely affect the long-term strategic planning of organisations. Handy (1988) also says that volunteerism can result in what he terms 'strategic delinquency'. This is where volunteers place their own ethos and values ahead of the organisation's objectives thus compromising its functionality.

The next section focuses on the operational aspects of social enterprise, starting with grant funding. This is crucial in understanding the relationship between social enterprise and the market, a key element of the IPE approach.

## **2.8 Financing of social enterprises**

### **2.8.1 Grant funding**

Social enterprises require different forms of investment at various stages of their development (Emerson, 2000; Alter, 2004; LRS, 2002). They are usually funded by a mixture of grants and trading income (Grenier, 2003; Shaw and Carter, 2007). Grant funding represents a crucial part of a social enterprise's funding mix, particularly for covering the core costs such as human and financial resources which are critical for successful business start-up (Walker, 1995). The types and sources of grant funding that are available to social enterprises include donations, subscriptions and financial support from institutions such as governments, charitable trusts and foundations (Bank of England, 2003). Social enterprises usually trade within tightly defined communities that are unable to pay market rates for their services, hence their reliance on grant funding to cover core set-up costs and assist them to lever in additional financial support as they expand and grow (Walker, 1995; Shaw and Carter, 2007; Simons, 2000). Overreliance on grant funding has, however, stigmatised social enterprises as transitional or what Carter (2003) describes as 'stepping stones to the real economy', thereby severely limiting their ability to attract the investment critical for growth. Case (2005) supports this view by saying that reliance on grant funding traps organisations in a 'perpetual supplicant' model, with little prospect of developing into sustainable businesses. A report by on financing options by Barclays Bank (2007) in the UK also painted a rather gloomy picture of the future of grant funding, saying that even wealthy philanthropists are no longer influenced by emotion when they are giving. Instead, they are giving strategically, suggesting that competition for their funds will intensify. While grant funding has the advantage of not being re-payable, overreliance on this type of financial support

predictably tends to limit trading activities. The growing social enterprise sector therefore requires more capital from sources outside the social economy (Heaney, 2010).

The next section focuses on non-traditional sources of finance for social enterprise.

### ***2.8.2 Loans and Equity investments***

In the social enterprise sector the emergence of venture capital, described by Mayo (2003) as the 'touchstone of Anglo-American capitalism', is an example of how the funding landscape is changing. A number of social enterprises are taking advantage of external finance investment packages being offered by institutional funders in Europe and America. The value of loans to the social enterprise sector has increased dramatically over the past four years, indicating this change in the financing of social enterprise (Brown, 2007). Loan finance is increasingly becoming an alternative option for social enterprises wishing to expand their activities or plug gaps in their funding. Two UK based organisations, Future Builders and the Unity Trust Bank, exemplify this development. Future Builders in particular has an investment package of £215m, exclusively available as loan finance for social enterprises (The Economist, 2005). Recently the organisation has signalled its intentions to provide facilities for quasi equity investments (Warrell, 2008). The development of loan finance packages for social enterprise saw the introduction of The BIGinvest in 2007 as a specialised loan finance provider for the sector. The Unity Trust Bank launched a £50 million loan financing facility for social enterprises at the same time (Cook, 2009). Doherty et al (2009), however, argue that not all social enterprises are willing to use loan capital as they fear putting their assets at risk should they default on the loans they acquire. There is also evidence that social enterprises are making use of Patient Capital (a form of investment structured as debt and equity) where investors are willing to accept lower financial returns in exchange for social outputs (Bank of England, 2003). The providers of loan finance are likely to be attracted by more profit driven social enterprises because they offer greater possibilities for recovering investments through loan repayments (Waste Paper, 2006).

These developments in non- traditional finance for social enterprise are significant. They demonstrate that social enterprises are seeking creative approaches to solving socio-economic problems and becoming effective agents of social change (West, 2005; Favreau, 2000). There are also implications for the legal structures of recipient

organisations as they require suitable infrastructure and capacity to draw down loan finance and accept equity investments in return for shares (Brown, 2007; Heaney, 2010). An appropriate legal structure is required, given that current investment incentive schemes, particularly in the UK, are not compatible with the legal forms associated with social enterprise (Heaney, 2010; Bank of England, 2003; Cox, 2000; Etchart and Davis, 2003).

A key element of the IPE approach is the insight it provides into the rationale and impetus behind the legal set up of social economy organisations as distinct from other forms of private enterprise. The discussion in Section 2.4 shows how social enterprise emerged from philanthropic organisations which were, from a legal point of view, set up primarily to address social objectives. The next discussion therefore focuses on the different types of legal structures of social enterprise and how they influence their operations.

## **2.9 Legal structures and social enterprise**

Its legal form (or structure or constitution) provides the operating framework for an organisation. A legal structure is a key operational component of social enterprises that drives, protects and allows their boards of directors to discharge their duties effectively (Osterloh and Frey, 2000). In essence it relates to the way a business is set up and the rules and regulations that govern it (SEL, 2003). Firms are legal entities in their own right and therefore their legal structures have implications for their liability, the legal protection of those running or associated with them and their ability to attract suitable investments (Doherty et al, 2009; Barker, 2002b). The last point in particular is crucial for social enterprises as the discussion in Section 2.8.2 indicates that a suitable vehicle is required to facilitate their access to loans and equity investments. For example, while a company limited by guarantee can access loan finance, this legal vehicle cannot attract equity investments, which are predicated on the ability to issue dividend bearing shares (SEL, 2001a; Dart, 2004). This suggests a relationship between a social enterprise's ability to achieve financial sustainability and its institutional legal form (Etchart and Davis, 2003; Tropman, 2003; Bank of England, 2003). Peattie and Morley (2008) support this view by arguing that the emerging innovative forms of investment discussed in Section 2.7.2 indicate that social enterprises need new ways to attract and manage investments. These authors call for further investigation in this area.

For a social enterprise, having a legal structure is also a way of managing risk and giving the organisation, and those involved in it, a legal identity (DFID, 2000). Once incorporated, a company becomes a legal entity or virtual person in its own right, and can employ staff and own or lease property. A legal structure therefore allows stakeholders to participate legally in the governance of a company in addition to protecting them from risk. A legal structure also protects the personal assets of individuals involved in companies from unlimited liability, except in circumstances where they have been engaged in fraudulent activities (SBS, 2005). Behind the constituted company therefore is a group of directors or trustees who have limited liability and benefit from a clear separation between the business and their personal assets. The legal structure is thus important in defining the activities and decision making process of a firm (Ellerman, 1984). There are also additional financial benefits associated with having a legal structure. For example, it is generally agreed that a social enterprise with a legal structure is more likely to attract funders than one without one (ACEVO, 2005).

Most researchers agree that there is no single preferred legal structure for social enterprises and that, whatever legal structures they adopt, they have to survive as independent businesses (SEL, 2003; DTI, 2002; Manning, 2006). Social enterprises take a variety of legal structures including amalgams of different organisational forms to pursue their objectives (OECD, 2006a; Martin and Thompson, 2010; Virtue Ventures, 2004; Barker, 2002b). Common social enterprise structures include company limited by guarantee (CLG), industrial and provident societies (IPS), cooperatives and companies limited by shares (CLS) (DTI, 2002; Doherty et al, 2009). These structures are commonly associated with social or democratic ownership (Low, 2006). Another legal vehicle with a share capital variant was recently launched in the UK, the Community of Interest Company (CIC).

However, it is also not uncommon for groups of individuals to operate as unincorporated associations, without a legal structure, to run community related projects. These groups run the risk of unlimited liability mentioned earlier so most social enterprises are unlikely to go down this route. Some social enterprises have charitable status. However due to restrictions on trading imposed by the Charity Commission in the UK, most social enterprises who wish to consolidate their trading activities avoid the charitable option. If they do choose charitable status, they usually set up separate trading arms with their own legal structures, typically companies limited by guarantee. A trading arm allows a social enterprise to generate

unrestricted revenue over and above its primary purpose and remit profits back to the charity under Gift Aid (SEL, 2003).

The next discussion focuses on the factors that influence social enterprises' choice of legal structure.

## **2.10 Choice of legal structure**

Research and interest in the legal structures of social enterprises has increased over the past decade. The focus has mainly been on the reasons why social enterprises choose their particular legal structure. Particularly in view of the changes in the economic environment and the need to facilitate the growth of this sector (Snaith, 2007) social enterprises continue to generate debate in academic literature. A common view among researchers is that the choice of a legal structure is merely an 'administrative matter' (Gair 2005, p. 5). However, this reveals a simplistic approach to the governance of social enterprises. Social Enterprise London (2003) argues that the choice of legal structure is influenced by the nature of the social enterprise and its particular requirements i.e. form follows function and the choice of legal structure is an accurate reflection of the enterprise's needs. Others, such as the Commonwealth Ventures (2003), consider the legal structure of a social enterprise to be determined by its financial requirements. Similarly, Alter (2003) notes that it is not uncommon for social enterprises to opt for a legal structure consistent with the funding it requires. Ahmed et al (2004) argue that the type of legal structure depends on the nature of the organisation, adding that most social enterprises' legal structures can be adapted to suit most purposes.

Bridge et al (2009) have attempted to scrutinise what influences social enterprises when they choose their legal structure. Arguing that this choice is not 'narrowly restricted (p.116), they imply that it is determined by the activities the social enterprise is involved in. They also consider that stakeholders' requirements, the governance structure and the ability to access finance all influence the choice of legal structure.

Such arguments assume that social enterprises have the knowledge required to make informed decisions when selecting a legal structure. However Lawrie (2002) regards the selection of a legal structure as an ongoing complex process. He argues that this selection should not be a mere afterthought but should be made well before

the organisation has commenced operations. In practice social enterprises have tended to decide on a legal structure without considering other important issues such as stakeholder participation, personal and corporate tax and their financial needs (Cox, 2000). As they are also hampered by a lack of advice in this key area, Alter (2006) considers many social enterprises to be operating in legally 'grey areas' because they are afraid of losing their status.

Given that the legal framework is complex and constantly changing, it is argued that access to legal advice is essential to enable social enterprises to select an appropriate legal vehicle (Ahmed et al, 2004; SEDSES, 2003). This is not an easy task and often requires expert external advice, particularly if considering complex models such as share capital legal structures. Current evidence suggests that the sources of legal advice available to non-profits lack the capacity to nurture new and emerging social enterprises (BASSAC, 2002b). Carter (2003) also notes that expert advice on appropriate legal structures for social enterprise is not readily available, and, when available, is usually far too expensive for social enterprises. Typically, voluntary groups within the social economy play a critical role in providing the sector with advice on their legal structures, advice which is usually free of charge and at a very basic level (SCEDU, 2002; Barker, 2003). Improving social enterprises' access to business and legal advice is one of the key objectives of the UK government's policy on social enterprise development (DTI, 2003b; DTI, 2006).

The next sections critically analyse the different types of legal structures available to social enterprises and how they influence the way they operate.

## **2.11 Types of social enterprise legal structures**

### ***2.11.1 Company limited by guarantee (CLG)***

This type of incorporation does not have shareholders but members who are guarantors instead of shareholders (Brown, 2003; Ahmed et al, 2004). These guarantors or members give an undertaking to contribute a nominal amount towards the winding up of the company in the event of a shortfall upon cessation of the business. This guarantee is nominal and is limited to £1 (DTI, 2003a; Bridge et al, 2009). A company limited by guarantee is not owned by an individual, but held in stewardship by a board, elected by members of the organisation. These members are responsible for electing the board to run the organisation (Bank of England, 2003). A CLG is probably the most common legal structure within the social



enterprise sphere, being fairly simple to set up and flexible to administer (Economic Partnerships, 2004; Leslie, 2002). CLGs are therefore popular with non-profit organisations requiring corporate status. A simple structure of a company limited by guarantee is shown in Figure 2.1 below.

**Figure 2.1: Simple structure of a company limited by guarantee**

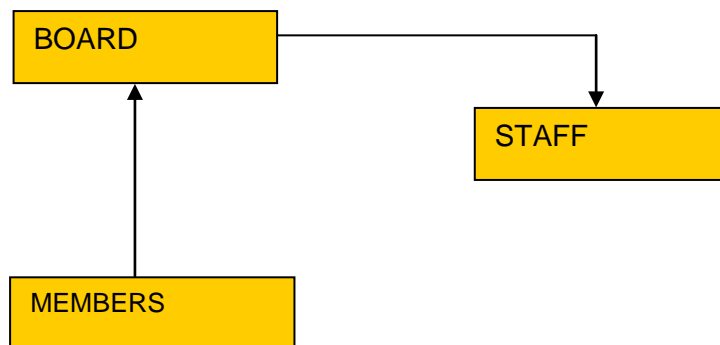


Figure 2.1: Adapted from SCEDU's internal training document (2002)

It is common for most CLGs to include a non-profit distribution clause in their memorandum and articles of association. The implication of this is that no members have an automatic right to a share of the profits or surpluses in the event that the company is wound up (DTI, 2003a). This does not mean, however, that CLGs cannot generate profits; indeed doing so is a key determinant of survival (SBS, 2005). The company limited by guarantee, by its nature, precludes the social enterprise from distributing profits to its members and promotes volunteerism to support its operations (Vidal, 2003). In the UK this type of incorporation is also common with development trusts, social firms and trading arms of charities.

### **Power structure and decision-making**

There is clear separation of powers in a company limited by guarantee. No one individual owns the organisation. A (usually unpaid) board of directors, mandated by the members, is responsible for creating and implementing policies for the organisation, as shown in Figure 2.1 above (SBS, 2005). Day to day activities are typically carried out by paid staff, led by a chief executive or executive director (Vidal, 2003).

### **Advantages**

The CLG structure is popular with the public and voluntary sectors because of its ability to facilitate relatively easy access to grant aid. Liability, as discussed previously, is limited to investments made and so members' personal assets are not exposed to risk, provided the directors have not acted negligently or fraudulently (SBS, 2005). Clauses can be inserted in the Memorandum and Articles of Association to make provisions for payment of trustees or directors (SBS, 2005). If a trading arm of a charity is structured as a CLG, then it can enjoy significant relief on tax and rates payments.

## **Limitations**

The CLG, however, has limited applicability to social enterprises. For example, tax efficient financial participation is not possible, unless the organisation is a trading arm of a charity (Barker, 2002b). It is also difficult for guarantee companies to raise commercial equity finance as they cannot issue dividend bearing shares (Economic Partnerships, 2004; Brown, 2003; Bank of England, 2003). Critics of the CLG argue that the independent and unpaid board of directors that are characteristic of this type of legal structure can stifle social enterprises' development and growth (Barker, 2003). They argue that some of the board members of these organisations cannot grasp the economics of business, thereby resulting in largely unviable enterprises. The separation of powers between board of directors and members as shown in Figure 2.1 above can also be a barrier to organisational effectiveness. The board and the members may need to work closely for effective strategic management of the social enterprise (SCEDU, 2005).

The following discussion critically analyses the industrial and provident society which is another significant legal structure associated with non-profit organisations.

### **2.11.2 Industrial and Provident Societies (IPS)**

An IPS is a bona fide cooperative which is described as an 'association of persons united to meet common economic and social needs through joint enterprise' (Marshall and Lovatt, 2004). This type of organisation has its roots in the philanthropic organisations of the nineteenth century as previously noted. In the UK, cooperatives are registered under the Industrial and Provident Societies Acts 1965-78. They must be either a bona fide cooperative or a society for the benefit of the community to be included under the act (ICOM, 1994; Bridge et al, 2009). The latter i.e. a society for

the benefit of the community is normally associated with housing associations and is not a common form of the IPS. Cooperatives usually have a registered written constitution rather than a memorandum and articles of association. Over the years, the evolution of cooperatives has resulted in new forms of this structure, namely worker and producer cooperatives, formed as a result of competitive market pressures (Borzaga, 2007). Some cooperatives are now being registered with UK Companies House, as opposed to the Financial Services Authority. This is further evidence of how cooperatives are changing to meet current challenges and opportunities (SCDG, 2005).

### **Power structure and decision making**

Cooperatives are managed, owned and controlled by members in a democratic way (EU, 2006). Other external corporate organisations can be members as long as their objects allow them but unincorporated associations can only nominate a representative (SEL, 2003). The directors of an IPS have delegated powers specified in their constitution or rule book (SEL, 2003). Their flexibility in terms of governance and decision-making makes this type of structure popular with social enterprises. Cooperatives do not provide a return on investment and are jointly owned and democratically managed entities.

### **Financing**

The IPS can mortgage its assets to a lender, doing so by granting charges over its assets. However its power and ability to attract loan capital depends on its governing rules (SEL, 2003). The capital invested in cooperatives also has a limited return (EU, 2006). The rules and regulations governing IPS do not allow a member to hold shares in excess of £20,000 (SEL, 2003). Irrespective of the number of shares held, voting rights are distributed equally among the members. This makes an IPS unattractive to venture capitalists although it can still issue loans stock (especially debenture stock) and securities to raise capital' (Bank of England, 2003).

### **Advantages**

Most co-operatives can enjoy corporation tax concessions through their mutual trading status although this benefit is not applicable to worker co-operatives

(Economic Partnerships, 2004). As in limited companies, there is limited liability for members involved in the IPS.

## **Limitations**

The share holding structure in an IPS is not attractive to venture capitalists and so limits potential sources of finance. This stems from the fact that this type of legal structure does not provide a return on investments (EU, 2006). In addition, the one member one vote scenario, results in a laborious decision making process. Potentially, this can compromise the enterprise's ability to exploit opportunities expeditiously. The IPS, unlike the CLG, is relatively expensive to register, the statutory registration fee being thirty times that of a normal company (ICOM, 1994).

The next section critically analyses the company limited by shares legal structure.

### ***2.11.3 Company limited By Shares (CLS)***

A company limited by shares is a legal entity whose principle purpose is to earn profits for the shareholders, who may or may not also be the directors or secretary of the company . This type of company can be either a private or public entity (DFID, 2000). A CLS can own property in its own right, distinct from the shareholders. The shareholders are responsible for all key decisions regarding the company. While these individuals are liable for the cost of the shares they hold should the company fail or go into liquidation, they are also able to make personal gain should the company be successful.

## **Shares**

A CLS usually divides its share capital into fixed amounts and this is referred to as the company's share capital. Typically for a small enterprise, the share capital is £100 (SEL, 2003). This process allows a company to distribute its wealth in proportion to the financial contributions made by its stakeholders. The share capital model remains largely unexplored within the social enterprise sector (SCEDU, 2003c). Conaty and McGeehan (2000) consider the lack of a critical mass of CLS-type social enterprises to have been a key weakness in the sector. They argue that the failure to consider alternative legal structures that can take advantage of equity investments has been one of the reasons for the very limited development of the

social enterprise sector prior to the 1980s in the UK. A few social enterprises, notably Traidcraft plc, have issued ethical shares that enabled external investors to inject capital into the enterprise (Bank of England, 2003). But the picture, especially in South Yorkshire, has been changing over the past few years due to the emergence of new social enterprises with share capital legal structures. This type of legal structure is discussed in the next section.

#### **2.11.4 Company limited by shares (social enterprise)**

In its basic form, the share capital model is not common within the social enterprise sector because of its ownership structure and uncertain contribution to the delivery of socio-economic value (Barker, 2002b). However SCEDU produced and pioneered a model that recognises possible private, public, social and employee representation in its operation. Significantly, the model captures and supports entrepreneurialism at the heart of the business. It is a flexible vehicle that enables mutual ventures within a defined structure to allow stakeholders to participate in the running of a social enterprise (Barker, 2002b.) This new structure, known as New Company (NEWCO), introduces a significant innovation in that the company has a legal and tangible capital ownership that provides for majority ownership by employees and social economy organizations. In essence, the company's share structure reflects the entrepreneur, employees and other key stakeholders on the one hand and, on the other, includes a separate class of preference shares for investors. The aims and objects are specifically designed to return value to the community, both tangibly and intangibly. A simple example is shown below in Figure 2.2.

**Figure 2.2: Company limited by shares (NEWCO)**

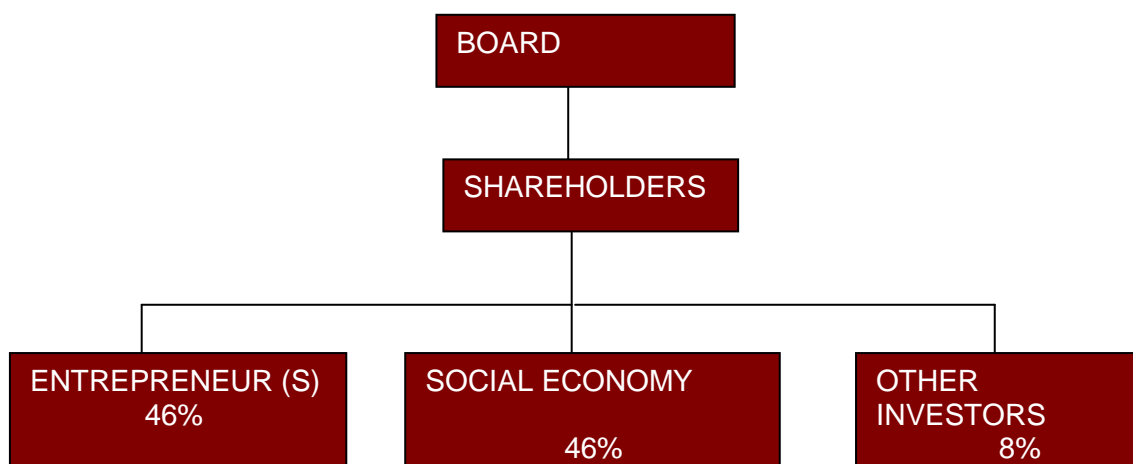


Figure 2.2: Adapted from SEC (2005)

## **Financing and decision-making**

The entrepreneurs at the heart of NEWCO have a minority shareholding in the company and the board structure reflects this ownership. Figure 2.2 above shows the capital and wider associate structure of the share capital model comprising entrepreneurs, the social economy and other investors. This structure is such that major decisions regarding the distribution of surpluses as investment into the social economy are effectively taken by those organisations with which NEWCO has worked and which have contributed through their fees to the generation of those surpluses (Barker, 2003). An effective asset lock to maintain the social ethos of the organisation can be achieved through appropriate clauses in the memorandum and articles of association. This type of legal vehicle allows the control of the organisation and its activities at both governance and management levels to be adequately defined and shared between the stakeholders. Shared ownership in this model involves shares being owned by a number of people or organisations, some of whom might be social enterprises and so might benefit from capital growth (SCEDU, 2003a).

## **Advantages**

NEWCO offers the same advantages as any company limited by shares model, but with some added benefits. For example, it can attract both grant and loan financial packages. It has now been recognised by some social enterprise support organisations in South Yorkshire, such as the Key Fund, as a suitable legal vehicle for social enterprises. The model also enables the majority of the generated surpluses to go to the community of benefit in addition to allowing socially minded entrepreneurs to make some personal gain. There is another important, though intangible, benefit of this improved community involvement and ownership of local investment i.e. the enhancement of the social enterprise's accountability to the communities that it serves (SCEDU, 2003b). The model provides a mechanism to reward personal entrepreneurial innovativeness and protects personal investments in the organisation such as intellectual property. Limited liability applies as for any company limited by shares. Most significantly, this type of legal structure allows social enterprises to attract equity investments without restrictions, thus widening the sources of finance available to them.

This type of legal structure allows social enterprises to pay dividends to investors. Dividends are a proportion of the earnings of a firm that is returned to shareholders and investors according to the shares they hold (Grant, 2002). For social enterprises these are normally determined by a fixed rate and are based on the enterprise's latest profits (Investor guide, 2010). While not all companies are obliged to declare dividends, those which do, are those that have progressed past the growth rate (Investor guide, 2010). It is important to note however that very few social enterprises will be in a position to declare dividends. The ability of social enterprises to attract private capital is debatable but encouragingly, the sector is beginning to attract the attention of private investors (Stutt, 2004).

## **Limitations**

Social enterprise support organisations that are not familiar with share capital structures are likely to be reluctant to invest in them. In its basic form the CLS legal structure does not seem a likely model for social enterprises because of its ownership structure and how the profits are distributed. Funders in the social economy do not tend to fund organisations whose focus is more on financial objectives at the expense of delivery of social value (Cox, 2000). Few would disagree that equity investment in social enterprise is problematic, as the market for selling the shares is not always available. In addition, there is evidence that most social enterprises are not familiar with the concept of equity investments (Bank of England, 2003). It is also true that the majority of social enterprises are unlikely to generate sufficient returns to attract private equity investors (Barker, 2003).

The next section discusses and analyses the CIC, a new legal structure for social enterprise.

### **2.11.5 The Community Interest Company (CIC)**

The search for innovative ways to make social enterprises more sustainable and able to access mainstream finance resulted in the introduction of Community Interest Company (CIC) in 2005. This is one of the developments that seek to define, characterise and influence the continuing development of the social economy. The CIC type of incorporation is designed for those social enterprises that desire to use their profits and assets for public good. The concept first appeared in the UK Cabinet Office Strategy Unit report entitled 'Private Action, Public Benefit', published in

September 2002. The CIC emerged as a custom made legal vehicle and a new brand for social enterprises. It has an asset lock on profits and assets to prevent their abuse and mechanisms to attract social and philanthropic investors (Enterprise for Communities Report, 2003). This legal structure can be a company limited by shares, limited by guarantee or public limited by company (DTI, 2004; Bridge et al, 2009). There are now 2,321 CICs operating in the UK since their launch in 2005 (Cabinet Office, 2008). Registration of a CIC is carried out in the normal way (to the Registrar of Companies). However, the Regulator of CICs has to confirm that the organisation meets requirements for CIC status, before incorporation is completed (DTI, 2004). The regulator also monitors the conduct of individual CICs (DTI, 2003b).

### **Advantages**

Historically, private sector investment in social enterprise has tended to be philanthropic in nature and the CIC was designed primarily to take advantage of such investments. If the CIC is structured as a share capital model, then the organisation will be able to issue shares that pay a dividend to the investors (DTI 2003b; DTI, 2004). This will obviously enable it to take advantage of external equity financial packages from social and philanthropic investors. The liability of members of the CIC is limited to the amount paid 'on shares or by guarantee' ACEVO (2004). The CIC asset lock can protect assets of the company more securely than can companies limited by guarantee or shares (Law Society, 2003). For example the cap on dividends will allow the social enterprise to extract value and retain wealth to strengthen its social ethos and commercial activities.

### **Limitations**

The introduction of the CIC was preceded by a comprehensive public consultation exercise. Some commentators argued that the model has a number of features that are unattractive to social enterprise such as capping of shares (SCEDU, 2003c). In addition, it is not possible for an organisation to be both a charity and a CIC (DTI, 2004) making this option unappealing to those social enterprises that wish to have charitable status. The presence of an external regulatory mechanism has been criticised by some who argue that this gives the regulator too much power to influence the development of CICs and might stifle entrepreneurial spirit (SCEDU, 2003c). Restrictions on shareholder voting and the 'capping of dividends on shares' is unattractive to venture capitalists and this has reduced financing options for those



social enterprises who opt for the CIC legal entity (Jump ,2009). The recent government consultation on possible revision of dividend and interest caps on CICs testifies to this point (BERR, 2009). One of the features of the CIC management model is an assumption that its directors can manage conflicts of interests between shareholders and investors. This might not be possible given that investor shareholders have no powers to appoint directors in a CIC (Law Society, 2003).

## **2.12 Summary of legal structures**

Table 2.4 below summarises the common legal structures associated with social enterprises that have been described above.

**Table 2.4: Summary of legal structures**

CLASS	TYPE OF LEGAL STRUCTURE	CHARACTERISTICS		
A	Company limited by guarantee	<p>Structure of Ownership</p> <p>1. No individual ownership. Company held in stewardship by an elected board of directors (usually unpaid).</p> <p>2. Allows community ownership.</p>	Limited Liability Yes	<p>Enterprise and Financial Structures</p> <p>1. Cannot attract equity finance.</p> <p>2. Can attract both grant and loan finance.</p>
	Industrial and Provident society/cooperative	<p>1. Controlled and managed by members.</p> <p>2. Directors have delegated powers.</p> <p>3. Democratic structure, with one member, one vote</p> <p>4. Equitable and fair distribution of economic results.</p>	Yes	<p>1. Strict share holding rules, therefore unattractive to venture capitalists.</p> <p>2. Can attract both grant and loan finance as well as tax concessions.</p>
B	Community Interest company (CIC)	<p>1. No individual ownership.</p> <p>2. Can either be a CLG or CLS</p> <p>3. Has an asset lock on profits and assets.</p> <p>4. Has external regulatory mechanism.</p>	Yes	<p>1. Can issue shares but dividends on shares are capped.</p> <p>2. Attractive to philanthropic rather than venture capitalists.</p> <p>3. Can also attract grant and loan finance.</p>
C	Company limited by shares (CLS)(NEWCO)	<p>1. A legal entity in its own right.</p> <p>2. Private/public finance initiative allowing various stakeholder participation in the enterprise.</p> <p>3. Allows ownership of idea and intellectual property.</p>	Yes	<p>1. Can attract equity finance.</p> <p>2. Allows profit distribution to investors and community organisations.</p> <p>3. Can attract both grant and loan finance.</p>

Table 2.4: Adapted from ACEVO (2005), SCEDU (2002), Cox (2000), ICOM (1994)

Table 2.4 summarises the menu of different legal structures available to social enterprises in the UK. The legal structures have been grouped in classes, according to their type, nature of management, profit distribution and ability to attract a wide range of financial investments packages.

Class A legal structures are the most common legal vehicles within the social economy and continue to allow social organisations to achieve their objectives. Their governance models are characterised by common ownership where a core group of individuals elected by the members of such entities provides day to day management of these organisations (SEL, 2001a). However they are by no means the most efficient and there is no guarantee that they will necessarily allow social enterprises to maximise the delivery of social value (DTI, 2003a). For example, they are unable to attract venture capital because of their inability to issue shares in return for equity (Cornforth, 2003; Barker, 2003). Although they can allow social enterprises to access grants, the organisations need to demonstrate financial viability to attract significant loan finance packages (Bank of England, 2003). Organisations with these types of legal structures are therefore heavily dependent on grant funding to cover the core costs of delivering their interventions (Cox, 2000).

Awareness of the inflexibility and inappropriateness of some of the current legal structures prompted the introduction in the UK of the Community Interest Company in 2005 (DTI, 2003b). This model is shown as Class B because of its triple functionality. A CIC can be structured as a company limited by guarantee, private or public limited share capital entity. As explained in the preceding sections of this chapter, its external regulatory mechanisms (caps on shares and dividends) make it more attractive to philanthropic, rather than venture capitalists (DTI, 2004). The dividend cap is a significant disincentive to investors who may be reluctant to invest their capital in an organisation where an external regulatory mechanism determines the return on their investment (Giddens, 1998). Therefore the CIC's financing options, though significantly better than Class A legal structures, are still limited. Only recently the regulator of CIC announced a consultation exercise to consider raising the dividend caps on CIC surpluses from the current 35% limit (Jump, 2009). This move is confirmation that the restrictions on the CIC share capital model have become a barrier to investment.

Class C legal structures are company limited by shares models. While there are a limited number of social enterprises that are structured as share capital entities, there is anecdotal evidence that they are increasing (SCEDU, 2003a). These types of legal structures, in certain cases, can attract both grant funding and equity finance, providing they are appropriately structured, such as the NEWCO (Barker, 2003). This legal vehicle was pioneered in Sheffield and, unlike the CIC, its shares are not capped. It also has an internal regulatory mechanism comprising organisations and individuals involved in the enterprise (SCEDU, 2003a). This structure recognises the contribution of individual entrepreneurs and allows for their financial remuneration. The concept of equity investments in social enterprise, as previously discussed, needs further exploration and scrutiny. Research has shown that most social enterprises are unfamiliar with the concept of equity investments (Bank of England 2003). This may partly explain why share capital legal structures are not a common feature of the UK social economy (IPSEYH, 2004). The discussion in Section 2.8.5 however suggests that innovation in legal structures may be the key route to market competitiveness for social enterprises. Social enterprises may need to embrace unconventional legal frameworks to ensure sustainability (Barker, 2003; Low, 2006; Social Futures Institute, 2004; Martinson, 2007).

The above discussion and summary of legal structures from the IPE perspective shows that, while traditional legal structures of social enterprises such as CLGs and IPS continue to be relevant, macro environmental pressures have necessitated the investigation of other legal structures. The consideration of risk capital for social enterprises is in itself a clear indication of the need to find an appropriate mechanism for attracting private capital into the sector. On the same note, the Bank of England Report (2003) suggests that share capital financing is likely to increase in popularity in the social enterprise sector (Bank of England, 2003). Despite these developments, the Social Catalyst (2006) urges caution, arguing that the solution to attracting equity investments in social enterprise may lie in expanding the definition of a social enterprise itself.

The arguments and discussions in this investigation focus on the share capital model of social enterprise discussed above as the NEWCO. Its for-profit orientation and other characteristics make it ideal for the analysis of social enterprises in the context of competitive markets.

## **2.13 Chapter summary**

As this review of the literature on social enterprises has shown, the IPE model is useful in a number of ways which are summarised below.

### ***Recognising the historicity of social enterprise***

Social enterprise as a concept is contested and has emerged and evolved within a broad, historical, macro-economic perspective. The discussion in Chapter 2 explains the institutional background of historical events such as the industrial revolution, from which social enterprises emerged in the UK. The philanthropic ideals that developed during this time became key tenets of the ideology underpinning contemporary social economy organisations. Social enterprise is therefore a product of the evolution of the social economy. Its objectives are associated with a rejection of profit maximisation and material infrastructure and instead a focus on the provision of welfare to the communities it serves. Its characteristics reveal how the concept has morphed over time as an example of capitalism and surplus value extraction working for a greater common good rather than for the benefit of an individual.

### ***Conceptual divergence***

There is no consensus on the nature and identity of social enterprise or its impact on practice. Divergent views on social enterprises reflect the definitional and conceptual issues which will be addressed in this thesis. Irrespective of differences in conceptualisation, researchers concur that the concept of social enterprise involves a business model predicated on the principles of exchange despite the philanthropic ideology that underpins its operations. This implies that a social enterprise is in essence a business that operates with financial discipline, as does a commercial firm, and seeks to be competitive and viable so as to achieve its social objectives. The decline in traditional sources of funding and state support coupled with changes in the global economic environment is now pushing social enterprises along this new trajectory.

### ***Focus on the structural positionality***

Although social enterprises have emerged in the context of political, economic and social change as discussed above, they are corporate bodies and therefore suitable for analysis like commercial firms, seeking to be competitive in the market. The continued growth of social enterprise is underpinned by an acceptance of the market, society and state as interdependent spheres that create specific operational

environments. The IPE's focus on economic development and transformation and strategic considerations makes it a suitable lens to provide some insight into the relationship between social enterprises and other stakeholders in the extraction and delivery of value. In addition, the forms of legal status acquired by these organisations are based on the need to legitimise their operations and support their social ethos and identity as well as to allow them to extract value beyond the social economy. This development is particularly relevant to the study of social enterprises in South Yorkshire, a key objective of this investigation.

Given the demands facing social enterprises and the need to operate as sustainable businesses, a starting point in developing this research's theoretical approach is to identify and critically analyse a suitable alternative theoretical framework that will guide this investigation. The next chapter focuses on the theory of the firm and some of its key elements in order to further the critical analysis of social enterprise.

## **CHAPTER 3: A FRAMEWORK FOR THE ANALYSIS OF SOCIAL ENTERPRISE**

### **3.1 Introduction**

The preceding discussion in Chapter 2 analysed the development of social enterprise using the IPE framework. The focus was primarily on its emergence, characteristics, evolution and its contested understanding. The IPE approach also provides insight into the contemporary development of social enterprises as competitive firms, highlighting how they are developing new commercially based approaches to tackling socio-economic deprivation through enterprise. The IPE approach, however, tends to focus narrowly on issues of economic determination. It does not illuminate the internal systems, decision making and operations of social enterprise as an evolving business that also needs to adapt to changes in the environment (Ellerman, 1984). Chapter 2 showed that the existing literature dwells largely on practical elements of social enterprise and provides little intellectual discussion on how this emerging concept might be further developed. This chapter therefore seeks to establish ways in which the theoretical framing of the concept of social enterprise can be improved by focussing on the internal dynamics of social enterprise.

Using the Behavioural Theory of the Firm (BTF), an extension of the neoclassical theory of the firm and its contractual elements, this chapter scrutinises the development of social enterprises, focussing on key internal operational issues. Specifically, this includes critically analysing the governance and legal structures of social enterprises and how they influence the organisations' outcomes. The selected contractual elements of the theory of the firm that will guide the analysis of the internal governance and management of social enterprises are; Agency Theory (AT), Stewardship Theory (ST) and Resource Dependency Theory (RDT).

Crucially, work done under the BTF framework suggests that the ideological significance of social enterprise cannot be divorced from the functional elements of a capitalist economy (Commons 1931). The chapter is divided into four parts. The first part discusses the conventional neoclassical firm and summarises its key aspects and implications for social enterprise. It is important to discuss the conventional, neoclassical theory of the firm since the BTF emerged as an extension of this

theoretical approach. The second part introduces and critically analyses the BTF approach and also highlights its implication for social enterprise. The third part discusses the internal governance structures of social enterprises and how these impact on their operations. The chapter concludes by discussing the selected theoretical frameworks that will underpin this research.

Since this chapter starts by focussing on the neoclassical theory of the firm, Table 3.1 below shows a comparison of the characteristics of this approach and the behavioural theory of the firm. These theoretical frameworks will form the basis of the analysis and understanding of social enterprises in this part of the thesis.

**Table 3.1; Neoclassical theory of the firm and the behavioural theory of the firm**

Theory	Managerial Rationality	Underlying Logic	Definition of a Firm	Goals of the Firm
Conventional/ Neoclassical Theory of the Firm(TF)	Rational behaviour	Profit maximisation	Black box	Singular
Behavioural Theory of the Firm (BTF)	Bounded rationality	Satisficing Value creation Social behaviour of firms	Adaptive coalition of individuals Learning organisation	Multiple and conflicting

Table 3.1 based on Cyert and March (1992) Jensen and Meckling (1976) and Bowen (2007)

The next section focuses on the neoclassical theory of the firm.

### 3.2 The Theory of the Firm

Work done using the neoclassical theory of the firm is drawn mostly from the field of economics and is credited to researchers such as Veblen (1924), Commons (1931) and Coase (1960) and their attempts to explore institutional phenomena. Veblen (1924), in particular, welcomed the emergence of the modern corporation as a way of ensuring efficiency in the way firms operate. Coase's seminal 1937 article, 'The Nature of the Firm', is widely regarded as the foundation of the modern theory of the firm (Foss and Klein, 2005). In contemporary discourse, the expansion of the neoclassical theory of the firm is associated with the works of Cyert and March (1992), Foss and Klein (2005), Williamson, (1964) and Alchian and Demsetz (1972).

The modern theory of the firm is considered to be part of the new institutional economics that gained prominence in the 1970s (Foss and Klein, 2005; Furubotn and Richter, 2008; Williamson, 1964; Kudlak, 2007). The theory of the firm is common in



economic literature but Jensen and Meckling (1976) argue that themes and materials subsumed under this theory refer in fact to the theory of the market, in which the firm plays a central role. Researchers who have used aspects of the neoclassical theory of the firm as an analytical tool for scrutinising social enterprises include Moulaert and Nussbaumer (2005), de Kam (2005) and Borzaga (2007). Their analyses focus on the need for social enterprises to be innovative and seek ways of operating in competitive markets.

As a theoretical perspective, the generally accepted theory of the firm conceptualises an organisation that seeks to maximise its net revenue, profits or expected profits (Williamson, 2002; Cyert and March, 1992; Cohen and Cyert, 1965; Mahoney, 2005). Underpinning this theory is the argument that the price mechanism efficiently allocates resources in the market and enables the firm to achieve its objectives (Kim and Mahoney, 2005; Demsetz, 1983). Cyert and March (1992) argue that, in essence, the theory of the firm is the theory of the market. In contemporary literature, support for this orthodox view of the firm comes from researchers such as Sundaram and Inkpen (2004) who contend that maximising shareholder values should guide the activities of managers of firms. The firm is therefore conceived as a monolithic 'black box', whose main objective is profit maximisation (Jensen and Meckling, 1976, p. 306). Social and ethical issues within the operation of the firm are considered to be separate activities; the firm's core objective is to maximise profits (Freeman, 1994). Profits are defined as the difference between revenue generated and fixed or variable costs incurred in accruing this revenue (Cyert and March, 1992). This theory also assumes that firms' operations are underpinned by perfect knowledge of their environments and rational behaviour by entrepreneurs and others involved in the firm. This view ignores the potential for conflicts between owners and managers (Berle and Means, 1932; Mahoney, 2005).

The neoclassical theory of the firm argues that there is no difference between firm and markets (Alchian and Demsetz, 1972). The firm is given as exogenous and markets are assumed to exist already. Hence, according to this theory there is no need for an entrepreneur to develop the firm or create or manage markets (which are already in existence) (Spulber, 2008). Researchers such as Freeman and Phillips (2002), however, see firms and markets as essentially different and therefore suggest different concepts should be used to analyse them. Decision making within the neoclassical theory of the firm is assumed to be determined by the market with the internal organisational structure having no impact on the process. Even seminal

works by Coase (1937) considered to be one of the pioneers of the theory of the firm, do not address these key aspects of organisational development. Regarding motivation, the theory regards monetary incentives, sanctions and control as essential in maintaining employees' productivity and motivation (Foss and Klein, 2005). This view has however been questioned by some researchers such as Muth and Donaldson (1989) and Herzberg (1966) who argue that other methods of addressing operational issues in organisations exist.

Moving on from the key constructs of the neoclassical theory of the firm, the next section focuses on the implications of using this theory to analyse social enterprises.

### ***3.2.1 The theory of the firm in social enterprise discourse; profit maximisation***

The normative model offered by the theory of the firm has several drawbacks acknowledged by researchers and academics. These relate to its underlying ideology, focus and applicability to the contemporary organisational dynamics that characterise social enterprise. Firstly, the concept of profit maximisation which underpins the theory of the firm has received significant attention and debate from researchers and academics (Jensen and Meckling, 1976). Even for corporate organisations which emphasise profit maximisation, this concept is under scrutiny. Cyert and March (1992) and Cohen and Cyert (1963) argue that when the actual behaviour of firms is analysed, profit maximisation is revealed as just one of the many goals they seek to achieve. Indeed, for some firms, it might not even feature among their goals. These authors argue instead that the firm's operations are not underpinned by the desire to maximise profits, but by satisficing behaviour (Cyert and March, 1963, p. 330) which is further explained under the behavioural theory of the firm in Section 3.7. Other researchers, such as Muller (1986) and Baumol (1965), agree that while profit is a key commercial objective of the firm it remains ambiguous, particularly around the relationship between performance, goals and resource allocation.

Relating this to social enterprise requires focussing on two critical aspects of their operations, namely their objectives and internal governance. In terms of their objectives, Chapter 2 showed that the ideology behind social enterprise is centred on surplus or value creation rather than profit and reconciling the achievement of financial goals with social goals to achieve a triple bottom line of economic, social and environmental objectives (Stutt, 2004; CASE, 2003). Profit maximisation is not

an overriding imperative for them as its pursuit might compromise the mission which is central to their identity (Newstart, 2005; Warrell, 2007c; Etchart and Davis, 2003). Social enterprises are therefore businesses that reject profit as their only goal. Instead they seek to maximise social value (Barker, 2002a; Thompson and Manson, 2010; McBrearty, 2007). They therefore tend to substitute profit maximisation with surplus or value maximisation, highlighting their aversion to capital accumulation or gain. Any surpluses produced are reinvested back into the social enterprise to develop its capacity to deliver services or products (Dees, 2001; DTI, 2002). This resonates with Hawkins (1973) who argues that profit, as a motive in the traditional theory of the firm, is too narrow because firms in general can realise utility from other sources. These views are supported by Jensen (2001) and Freeman et al (2004) who consider value creation and stakeholder relationships to be key defining characteristics of firms' operations, a perspective which fits perfectly with the underlying ideology of social enterprise. This alternative view of the firm (value creation) thus rejects the idea that a firm's economic activities can be separated from its ethical and social values. Freeman et al (2004), in their analysis of stakeholder theory, refer to this as the 'separation' thesis i.e. separation from the neoclassical theory of the firm and other proponents of the notion that a firm exists only to maximise profits. This is important for understanding social enterprises, since their activities are underpinned by a strong social ethos despite their mission to succeed as competitive firms (Dees, 1998; Pearce, 2003; Chell, 2007; Doherty et al, 2009; Peattie and Morley, 2008). From this discussion, it is evident that the theory of the firm does not allow us to adequately analyse social enterprise.

The next section focuses on the theory of the firm and its implications for the analysis of the internal systems of social enterprise.

### ***3.2.2. Internal organisational analysis and social enterprise***

The preceding discussion of the conventional theory of the firm has demonstrated that there are aspects of the behaviour of the firm which are not fully captured by this theoretical approach (Garrouste and Saussier, 2005; Hawkins, 1973; Foss, 1996). For example, the theory of the firm does not focus on the firm's internal organisational systems and processes (Cyert and March, 1963). Given that social enterprises are value led organisations owned by the community, their internal organisational analysis is crucial in understanding how they make decisions and develop sustainable trading strategies. The above discussion shows that the theory

of the firm considers it to be a 'black box' whose main function is to process inputs into outputs with profit maximisation being the key driver for performance (Williamson, 2002). This is inconsistent with social enterprise, as the discussion in Chapter 2 reveals that social enterprises have democratic governance models that promote inclusiveness and solidarity. As organisations embedded in the communities they serve, their decision making process is predicated upon the need to address social objectives rather than maximise profits. The theory of the firm therefore fails to provide a framework to analyse the different ownership, governance and control structures associated with social enterprises. It also has little to say about how resources are allocated within the firm itself or the importance of managerial and governance roles in managing these resources (Cyert and March, 1992; Casson, 1997; Foss and Klein, 2005). These issues are particularly important for social enterprises since their impact has become increasingly prominent in contemporary discourse of the theory of the firm (Cyert and March, 1992; Jensen and Meckling, 1976). They are also key to understanding social enterprises, which have multiple goals and multiple stakeholders to manage and satisfy.

The above discussion highlights the limitations of the conventional theory of the firm in illuminating the nature and operations of social enterprises. Its focus on profit maximisation rather than understanding the internal dynamics of firms makes this framework unsuitable for analysing the operational behaviour of social enterprises. For example there is no insight into how the conflicting objectives of individuals and stakeholders can be resolved (Jensen and Meckling, 1976). In addition, its focus on separating social and economic goals makes it ill equipped to critically analyse the behaviour of hybrid firms such as social enterprises (Bowen, 2007). Hence the emergence of the behavioural approach, a theoretical framework discussed in the next section.

### **3.3 Behavioural theory of the firm (BFT)**

The discussion on the development of social enterprise using the IPE approach and the conventional theory of the firm shows that these theoretical approaches are too limited to allow us to fully analyse the internal systems and operations of the firm and specifically the social enterprise. We therefore need to consider complementary theories of the firm that scrutinise internal systems and processes and their impact on the firm's development (Milgrom and Roberts, 1998). The BTF approach, which is an extension of the theory of the firm, enables further scrutiny of the development of

social enterprises, focussing on key operational issues and the challenges they face. Specifically, this includes the governance, management and legal structures of social enterprises and how these influence their operational effectiveness. BFT makes it possible to critically analyse the social behaviours of the firm as Table 3.1 indicates. This is contrary to the narrow assumptions concerning the purpose and nature of the firm embodied in the conventional theory of the firm (Bowen, 2007). Mason et al (2006) support this view by suggesting that the BTF goes beyond the mechanics of business by also analysing the impact of culture and norms on the operations of the organisation. This approach modifies or stretches neo-classical economic theory to take into account economic theories of non-market social relations (ISNIE, 2006; North, 1989). The BTF approach acknowledges that a firm's responsibility to society is not necessarily to maximise profits and the role of governance is not necessarily to provide corporate control (Korac-Kakabade et al, 2001). Hence the BTF approach has been described as one of the most dramatic new perspectives to extend and develop the theory of the firm (Hawkins, 1973).

The BTF approach has been selected as a suitable theoretical framework to analyse the internal dynamics of social enterprises in this investigation. Researchers and academics who have used aspects of this type of analytical tool in scrutinising non-profit organisations and social enterprises include Furubotn and Richter (2008), Moulaert and Nussbaumer (2005) and de Kam (2005). Their work focuses on the need for social enterprises to be innovative in order to achieve both social and economic objectives in demanding economic environments. Economic dimensions and innovation are among the theoretical premises of the BTF approach. It is also important, however, to note that this approach, as an analytical tool, has attracted criticism from other researchers. For example, Day (1967) criticises the BTF's approach's assumptions about the relationship between rational choice and behavioural principles saying that these do not clearly articulate the complexity of organisational dynamics. In this investigation however, the behavioural theory of the firm (BTF) approach makes it possible to do the following.

1. Analyse social enterprises as evolving hybrid firms with multiple goals. The firm is therefore not a monolith and needs to adapt to changes in the environment to achieve its objectives. Contrary to the neoclassical theory of the firm, the BTF approach makes it possible to incorporate the social objectives of the firm which is essential to understanding social enterprise (Bowen, 2007; Cyert and March, 1963) .

2. Scrutinise internal dynamics such as governance and decision making. This is critical in understanding the evolution of social enterprises over time and how they seek to adapt to internal and external changes in their environment. This is consistent with Cyert and March (1963) and Bowen (2007)'s argument that the ability to respond and adapt to changes in the economic environment has become a key operational issue for contemporary businesses.

These two elements above will guide this investigation's analysis of the internal governance and legal structures of social enterprise and how they influence their operations. The analysis of the governance and management structures of social enterprises is a key objective of this research. The next section focuses on the emergence of the BTF approach particularly in terms of the two elements above

### **3.4 Emergence of the behavioural theory of the firm**

The behavioural theory of the firm (BTF) is a recent development in the field of microeconomics (Day, 1967) and is mainly associated with the work of Cyert and March (1963 and 1992). Other researchers, such as Rubin (1978), Langlos and Roberston (1995) and Demsetz (1967), have also written extensively on this theoretical approach. These authors have extended the neoclassical theory of the firm to analyse internal organisation and decision making in firms, aspects which were not previously adequately addressed, hence the emergence of the BTF (Bowen 2007). They argue that in order to gain insight into contemporary economic decision making processes of firms, it is also important to scrutinise internal operations such as incentives and property rights and how these impact on organisational structure and outcomes. These views contradict the conventional theory of the firm, which does not acknowledge the relevance of the internal organisational structure of the firm to its decision making process as discussed earlier. The BTF approach represents an extension in organisational economics and therefore supplements the conventional neoclassical theory of the firm (Cohen and Cyert, 1965; Mahoney, 2005).

Cohen and Cyert (1965) argue that the BTF approach seeks to address the limitations of the theory of the firm particularly in regard to decision making. They suggest that the theory seeks to answer two important questions:

1. How does the firm allocate resources?
2. How do the objectives of the firm change over time?

These two questions show that the BFT's focus is primarily on how a firm operates and makes decisions to ensure sustainable development in a multi-actor environment (Cyert and March, 1992). In addition, the firm is constrained by environmental pressures and therefore needs to adapt to achieve its multiple goals (Cyert and March, 1963). At the heart of the theory therefore is the understanding that the firm is not static but needs to be aware of changes in the environment as well as stakeholders' needs and expectations and then adapt accordingly (Augier, 2004). This adaptive behaviour is a response to failures in performance or challenges emanating from the broader environment. It necessitates innovativeness on the part of the firm and making the necessary changes in its strategy and internal systems and processes to achieve its objectives (Cyert and March, 1963). Cyert and March (1963) also argue that, in addition to decision making, the choice and expectations of goals are key components of the behavioural theory of the firm.

Regarding goal formulation in particular, the authors suggest that there must be consensus among all those involved with the firm. The BTF approach therefore acknowledges that those involved in the firm may have different aspirations and interests that do not always converge. Hence Cyert and March (1963) and other proponents of the behavioural approach are opposed to the view that the firm is a monolith, but consider it instead a coalition of individuals and groups, a coalition that includes customers, stockholders and managers. The firm therefore becomes a complex organisation, with multiple objectives and not necessarily reliant on a single decision maker (Hawkins, 1973). The theory also rejects the singular profit maximisation approach central to the neoclassical theory of the firm. On the contrary, a firm has multiple goals and profit maximisation is not the only objective (Cyert and March, 1963; Berle and Means, 1932). Cohen and Cyert (1965) argue that generally the BTF is more applicable to those organisations whose decision making process is not entirely driven by the market. These include non-profit organisations such as hospitals or unions etc (Cyert and March, 1992). The authors consider such organisations to have relative freedom in developing decision making structures, rules and systems consistent with the various objectives that they might want to achieve. Cyert and March (1963) suggest that individuals or groups or the coalition

involved in a firm tend to 'satisfice'. This means, for example, that in their decision making, managers are most likely to seek goals that are achievable, rather than those that maximise their own utility or profit. Within the BTF approach, managers are not assumed to be rationally optimising separate social and economic goals of the firm. These underlying aspects of the BTF approach are also relevant to social enterprises as discussed below.

### ***3.4.1 Behavioural theory of the firm and social enterprise***

The preceding discussion has shown that social enterprises are firms that seek to be financially sustainable and competitive in the market. They combine market activity with philanthropic capital and entrepreneurial drive and seek to reduce reliance on grant funding (Low, 2006; Arbor, 2005). Social enterprises are thus not primarily motivated by maximising profits or return on capital. Instead they are driven by the desire to maximise value through a combination of social and economic goals that can be achieved or satisfied at the same time (DTI, 2002; Dees, 1988; Marshall and Lovatt, 2004; Martin and Thompson, 2010; Barker, 2003; Freeman et al, 2004; Pestoff, 1998). Such maximisation of value is consistent with the views of contemporary behavioural theorists such as (Jensen (2001) as discussed earlier in Section 3.5.1. The governance of social enterprises is characterised by social ownership, which includes various stakeholders such as trustees, volunteers, directors drawn from the community and other external organisations, with no individual ownership of the project idea or claim to assets (Barker, 2002b; SEL, 2003; Doherty et al, 2009). In addition, the global economic trends discussed in preceding sections have resulted in a gradual shift towards such hybrid models of social enterprise, focusing on achieving both social and economic objectives in a multi sectoral approach (CCSE, 2001). What this implies is that a social enterprise seeks to achieve multiple objectives involving a wider constituent base (Simons, 2000). As such, social enterprises are increasingly regarded as 'a multi goal, multi-stakeholder and multiple resource enterprise' (Borzaga and Defourny, 2001). This view is supported by Pestoff (1998) and Gonzales (2008) who consider that their multi stakeholder approach and commitment to democratic principles of governance allows social enterprises to pursue several goals at the same time to address several agendas. These are some of the key constructs of the BTF approach. This new orientation is significantly different from the welfare approach discussed in Chapter 2 in which the objectives of non-profit organisations were considered to be purely social.



Due to constraints arising from lack of access to funding and investments, social enterprises are increasingly looking beyond the social economy to mobilise resources. The matrix of private, public and civil sectors has become critical for the growth of the social enterprise sector (Gentile, 2002), contradicting the widely accepted view that capitalism and social conscience are not natural bedfellows (Akwagyiram, 2008). This collaboration with the private sector means that social enterprises are adapting to the demands of the external environment and seeking to benefit from the a bi- directional flow of value with the private sector (Fox and Shearer, 1997; Gutierrez, 2005; Stutt, 2004; Martinson, 2007). This new direction may require social enterprises to modify not only their organisational culture but also their internal structures and processes (Anderson et al, 1996). This collaborative and multi-goal strategy resonates with Cyert and March (1992)'s description of a firm as a 'coalition of diverse subgroups'. It is also clear that social enterprises seek to achieve social and economic goals simultaneously, contrary to the theory of the firm which regards these as separate activities and objectives.

The above discussion shows that the BTF approach is an appropriate theoretical lens for the analysis of social enterprise. The following sections discuss the internal governance and management of social enterprises using selected elements of the theory of the firm.

### **3.5 Governance and social enterprise**

We have previously argued that the IPE and BTF approaches are suitable frameworks for understanding social enterprise. While the IPE focus offers a historical and contemporary perspective, the BTF approach is crucial in critically analysing social enterprises as multi-stakeholder and multiple goal firms. Our discussion has also noted that one of the key constructs of the BTF approach is its internal analysis of the firm with particular focus on governance and management structures. Given that the IPE and the neoclassical theory of the firm do not incorporate behavioural models that can assist in understanding the internal dynamics of organisations and their interface with the environment, additional theoretical perspectives are required. The following sections therefore use selected elements of the BTF theoretical approach to critically analyse the internal governance and operations of social enterprises. These elements are Agency theory (AT), Stewardship Theory (ST) and Resource Dependency theory (RDT all of which are

theoretical approaches in their own right. They are all significant approaches associated with corporate governance and have been drawn from the fields of both economics and sociology. It is also important to note that the governance of social enterprise is still theoretically underdeveloped (Mason et al, 2006). However over the years researchers such as Abzug and Galaskiewicz (2001), Child and Rodrigues, 2004 and, most recently, Low and Chinnock (2008) have undertaken insightful empirical work on social enterprise governance. The next section first discusses governance theory, followed by different theoretical approaches to governance and where social enterprises fit in. The discussion then moves on to the selected theoretical framework that will guide this thesis's analysis of the governance structures of social enterprise.

### **3.6 Governance theory**

The governance of firms, and particularly the role of the board and its impact on performance, continues to attract the interest of researchers (Nicholson, 2004). Monks and Minow (1995, p.1) describe corporate governance as 'the relationship among various participants in determining the direction and performance of a corporation'. Corporate governance emerged from the disciplines of law and economics (Grant, 2003). The board, according to Daily et al (2003), is the locus of the internal governance of a corporation and performs several key roles which will be discussed in depth under relevant theoretical frameworks in succeeding sections. These include performing the strategic role of making key decisions and providing the necessary direction and strategic focus required for the organisation to achieve its objectives (Low, 2006, Bridge et al, 2009, Nicholson and Kiel, 2004; Zahra and Pearce, 1989). The board can also be a link to the firm's external environment, providing the infrastructure to access the resources and advice required to achieve its objectives. This particular function is associated with the resource dependency approach (Daily et al, 2003; Dalton et al, 1998; Hung, 1998). Several researchers, amongst them Daily et al (2003), Mason et al (2006), Muth and Donaldson (1998) and Hillman and Dalziel (2003), argue that the board can also act as an agent of its stakeholders such as shareholders and investors and perform the task of monitoring and controlling management activities on their behalf. This particular role is associated with agency theorists. The board of directors also recruits, appoints and holds accountable the top management of the firm responsible for operational issues (Cohen and Cyert, 1965). Zahra and Pearce (1989) summarise the above functions or roles of the board as service, control and strategic. Muth and Donaldson (1998)

however summarise the primary roles of the board as managerial control, co-optation and empowerment through the AT, RDT and ST approaches respectively. These theoretical approaches are analysed in the following sections. Ownership is a key determinant of the operations of the modern firm. Parkinson (2003) states that shareholders are considered to be the legal owners of the organisation's assets and that the purpose of governance is to uphold and protect this right of ownership. The theory of the firm defines ownership as the possession of residual rights of control (Foss , 1996; Burns, 2007). This essentially refers to the control, use and allocation rights of a firm's assets (Williamson, 1964). Grossman and Hart (1986), argue that these allocation rights can affect the behaviour and resource allocation processes in firms. For example, potential investors might be reluctant to commit resources if ownership is not guaranteed.

The next section critically analyses the selected approaches to understanding the internal governance of firms and their implications for social enterprise, as indicated in Table 3.2 below

**Table 3.2: Understanding the internal governance of firms**

TYPE OF GOVERNANCE THEORY	CHARACTERISTICS		
	Underlying objectives	Motivation of Executives	Board Functions
<b>Agency</b>	Firm performance enhanced by reducing agency costs	Extrinsic rewards  Self serving and opportunistic	1. Monitor and control  2. Separation of ownership and control
<b>Resource Dependency</b>	Exchange relationship between the firm and its external environment	Financial and non-financial	1. Co-optation of resources through high level links with external environment  2. Boundary spanning
<b>Stewardship</b>	Shareholders have claim on assets.  Protection of rights of ownership and intellectual property.	Non-financial e.g. Need for achievement, recognition  Maximise organisational performance	1. Empowering governance structure. Provides e.g. autonomy and authority  2. Ensures individuals work in the best interests of the organisation.  3. Separation of ownership from control.

Table 3.2: based on Davis et al (1997), Hillman and Dalziel (2003), Pfeffer and Salancik (1978) (2006), Bridge et al (2009), NCVO (2007) and SEL (2001).

### **3.6.1 Agency theory (AT)**

The emergence of the modern corporation resulted in the ownership and control of resources being separated (Berle and Means, 1932; Machold and Vasudevan, 2004) and this separation is one of the dominant themes of the economic theory of the firm (Demsetz, 1983). Cohen and Cyert (1965) suggest that the reason for this separation might be the owners' or stockholders' reluctance to get involved in the day to day

operations of the firm. They therefore appoint a board of directors to shape the firm's strategic direction and development. Berle and Means (1932) argue that the separation of ownership and control can result in a divergence of interests between owners of firms and managers. For example, managers have the potential to pursue their own interests if they have effective control of the firm's resources (Cohen and Cyert, 1965). Furthermore, the owners of the business stock can lose control over their resources if ownership becomes spread across a number of shareholders. This may provide autonomy for managers in the utilisation of resources and increase the likelihood of them pursuing their own interests (Berle and Means, 1932; Demsetz, 1983). This separation of power and control in modern corporate forms gives rise to the principle-agent problem which is discussed below (Berle and Means, 1932).

Agency theory, which is grounded in the fields of economics and financial research, is considered one of the dominant theoretical perspectives in the literature on corporate governance (Daily et al, 2003; Muth and Donaldson, 1998; Zahra and Pearce, 1983). These authors suggest that the popularity of this theoretical perspective arises from the following;

1. AT is a simple theory which allows one to regard an organisation as having two key constituents i.e. managers and shareholders.
2. Historically, it is well known and widely accepted that human beings by nature seek to be involved in activities that serve or reinforce their self interest.

While Jensen and Meckling (1976) regard agency theory as a key characteristic of the operations of the public corporation, the theory has been applied to different organisational phenomena and academic disciplines. These include companies (Eisenhardt, 1989), ownership and financial structures within organisations (Jensen and Meckling, 1976) and sociology (Eccles, 1985). Agency theory is underpinned by the 'model of man' which assumes that shareholders will lose control as the firm grows and that managers will prioritise their own interests above those of the organisation (Donaldson and Davis, 1991; Muth and Donaldson, 1998). As a firm develops and expands, it is not uncommon for the owners or stockholders to delegate responsibility and authority to managers (agents) to run the firm on their behalf (Davis et al, 1997). The key concern for owners of the organisations has always been the amount of control that managers should have (Jensen and Meckling, 1976). Agency theory therefore, in its paradigmatic form, analyses the

relationship between the principal (stockholder) and the agent, who is responsible for implementing the tasks delegated by the principal (Eisenhardt, 1989). Agency theory seeks to address two issues:

1. Conflicts or agency problems emanating from the divergence of goals of principals and agents
2. When there are high costs associated with verifying or ascertaining what the agent is doing (Eisenhardt, 1989).

Agency theory concerns itself with the problems that arise when principals and agents both wish to maximise their own utility and are motivated by prospects for personal gain (Davis et al, 1997; Berle and Means, 1932). Stockholders or owners become principals when they contract executives to manage their firms on their behalf. If there was no divergence of goals between principals and agents, then there would be no agency costs but in reality this is not possible. Hence principals will put in place mechanisms to control managers' activities (Williamson, 1985; Jensen and Meckling, 1976). The AT approach therefore assumes that, unless there are appropriate controls in place to manage the decision making process of the managers (agents), they are likely to maximise their utility at the expense of the stockholders (the principals) (Muth and Donaldson, 1998). This is the crux of agency theory Davis et al (1997). Control mechanisms are required to reduce agency costs (Eisenhardt, 1989; Hillman and Dalziel, 2003; Jensen and Meckling, 1976). Walsh and Seward (1990) argue that these mechanisms should be internal, rather than external to the organisation. They include financial rewards and governance structures that allow principals to monitor the activities of agents through audits and performance appraisals. Financial rewards are predicated on the work that assists principals in maximising shareholder value or from equity shares that allow agents to be part of the organisation's ownership (Jensen and Meckling, 1976; Donaldson and Davis, 1991). Such an approach to governance acts as a deterrent to self serving activities. Davis et al, (1997) argue that rewarding agents financially is a desirable strategy, particularly when they have more information than principals about the operations of the firm. Eisenhardt (1989) suggests, however, that agency theory treats information as a commodity that can be bought. This information asymmetry between principal and agent can also give the former a tool to address the agents' potential to undertake self-serving activities. Agency theory therefore focuses primarily on divergence of interest between principal and agent. But the theory is also

criticised for this. For example, Davis et al (1997) argue that it would be useful if it explained how the divergent interests of principals and agents could be reconciled.

The AT approach assumes that shareholders in ownership positions are more highly motivated to monitor their managers against 'opportunism' and to exert influence to bring about the changes they desire (Daily et al, 2003). Another way of controlling managerial opportunism is through an independent board of directors which can put in place the requisite control and monitoring mechanisms, on the shareholders' behalf (Donaldson and Davies, 1991, p.50; Hillman and Dalziel, 2003). Central to the AT approach is an independent board, free from management influence (Muth and Donaldson, 1998). Since, according to the theory, managers cannot be trusted, an independent board of directors ensures that their activities are monitored and controlled (Eisenhardt, 1989; Muth and Donaldson, 1998). The independence of the board is achieved by separating the initiation and implementation of decisions and strategies i.e. the separation of the board from the CEO. Agency theory considers such independence to ensure greater efficiency, than would be the case with a board compromised by management influence (Muth and Donaldson, 1998). This approach is therefore suitable for organisations with hierarchical structures where decision making is the preserve of top management (Mudambi and Pedersen, 2007). The board's monitoring role, according to Jensen and Meckling (1976) is consistent with the view that the separation of ownership from control can create an environment conducive to managerial opportunism. While an independent board of directors can benefit shareholders, Shleifer and Vishny (1997) argue that research suggests otherwise. Instead, agency control tends to force agents to be compliant, rather than increase the wealth of principals, a view shared by Davis et al (1997).

The next section focuses on the AT approach and its implications for the governance of social enterprises.

### ***Agency theory and governance of social enterprise***

Agency theory has been criticised for its underlying economic assumptions. Doucouliagos (1994) argues that there is a need to consider non-economic motivations when analysing human behaviour in firms, a view supported by Perrow, (1986) one of the staunchest critics of agency theory. Jensen and Meckling (1976) agree that agency theory takes an over simplistic approach to analysing corporate and human behaviour which is actually much more complex and influenced by a

wider range of factors. They also criticise the theory for failing to consider and analyse managers' competence and training needs. Davis et al (1997) consider these omissions to constitute a major weakness of the theory. The applicability of the AT approach to analysing social enterprise governance has therefore been debated. Given that a social enterprise has no shareholders, Abzug and Galaskiewicz (2001) argue that it is difficult to identify the principal and the agent. In addition, since the governance of social enterprise is underpinned by democratic and participatory principles, it is highly unlikely that senior managers of such enterprises would engage in self serving activities (Mason et al, 2006). Despite these criticisms, Callen et al (2009) believe the AT approach is still relevant to the critical analysis of how social enterprises operate, because it focuses on some relevant aspects of non-profit operations such as the relationship between the board and the performance of the firm. This relationship is associated with the AT's principal agent approach characterised by the separation of ownership and control of assets (Daily et al, 2003; Hillman and Dalziel, 2003). Callen et al (2009) argue that this aspect of the AT approach i.e. control of assets, makes it possible to scrutinise how boards of social enterprises operate.

Firstly, it is important to understand how most social enterprises are governed. Section 2.5.3 discussed the democratic model of social enterprise, one of the most common governance models in the non-profit sector. This type of governance emphasises the value of participation and stakeholder involvement rather than personal ownership and surplus distribution (SEL, 2003; Iecovich, 2005; Pearce, 2003; Chell, 2007; Birkhoelzer et al, 1992). It is evident that this type of governance contradicts the AT approach, at the core of which is an independent board free from managerial influence (Muth and Donaldson, 1998). Furthermore, McNulty and Pettigrew (1999) note that a lack of clear separation of powers between the executive and operational staff in non-profits can create a minimalist board and negatively affect efficiency. This type of board tends to be run by an individual or dominated by strong founder members, with little or no conflict, challenge or dissent occurring either amongst themselves or from external stakeholders (Spear et al, 2007). Such situations are inconsistent with the AT approach that advocates for a clear separation of roles between the board and the executive to ensure efficiency (Muth and Donaldson, 1998).

Social enterprises do not have shareholders or stockholders in a commercial sense (Low and Chinnock, 2008). Unlike for-profit organisations the board is regarded as a



'tool of democratic participation' (Low, p.4 .2006). Non-profit organisations are thus controlled by the elected directors or trustees on behalf of the community rather than by share holders ( Pearce ,2003;DTI,2003c) .The function of the board is to represent the interests of this community as well as the interests of various constituents and groups and to ensure that enterprise's assets are not abused (Iecovich, 2005). Callen et al (2009) and Miller-Millensen (2003) argue therefore that the AT approach is relevant to non-profits citing specifically the role that the board plays in protecting the organisation's assets and controlling the activities of managers so as to maintain costs and prevent misallocation of resources. Barker (2002b) concurs, noting that there is evidence of independent boards of nonprofits developing mechanisms to control the activities of their senior managers in order to ensure that their actions and interests are in tandem with those of the social enterprises (Barker, 2002b).This view is supported by Fama and Jensen (1983) who suggest that mechanisms to control assets and monitor activities and staff of non-profits are essential, since these organisations do not normally possess residual assets.

The next section considers an additional theory that goes beyond economics to explain and analyse human behaviour in firms. The following discussion considers the efficacy of Resource Dependency Theory (RDT) as a theoretical foundation for understanding the relationship between a firm and its environment.

### ***3.6.2 Resource dependency theory***

Given the importance of the board of directors' role in corporate governance, extant literature does not sufficiently reveal the relationship between board independence and the financial performance of firms (Dalton et al, 1998; Hillman and Dalziel, 2003). Agency theory has limitations with regards to illustrating the directors' resource mobilisation and strategic management roles (Daily et al, 2003).Whilst it focuses on the board's monitoring and controlling role, other theoretical perspectives are required to explain how directors ensure that their organizations access the resources they need.(Daily et al, 2003). Resource dependency is one such approach to corporate governance. This relatively underexplored approach focuses on the exchange relationship between the firm and its external environment (Davis and Cobb, 2009; Corcoran and Shackman, 2007). In order to ensure its long term survival, the firm co-ops scarce resources key to achieving this objective (Muth and Donaldson, 1998). Work from this theoretical perspective is mainly associated with Pfeffer and Salancik (1978). Other authors who have written extensively on this

concept include Daily et al (2003) and Hillman and Dalziel (2003). However, despite its increasing prominence in the literature on governance there is very little empirical work based on RDT (Davis and Cobb, 2009; Mudambi and Pedersen, 2007).

Bazerman and Schoorman (1983) suggest that the Resource Dependency Theory approach has four benefits in that it focuses on network connections among directors, horizontal coordination, vertical coordination and expertise and reputation. Hillman and Dalziel (2003) refer to these collectively as board capital, consisting of both human and relational capital necessary in assisting an organisation to mobilise key resources. What influences a firm's level of dependence on a resource has also generated debate. Pfeffer and Salancik (1978), for example, identify three key factors that, they argue, influence the level of dependency of a firm on a resource. These are; the importance of the resource to the firm; the scarcity of the resource and competition among organisations to exert control over the resource

Within this theory success is defined largely as the extent to which the organisation maximises its power in the environment (Ulrich and Barney, 1984). Pfeffer and Salancik (1978, p.7) define success as the 'creation of acceptable outcomes'. Those environments with an abundance of resources are considered less hostile and therefore competition is less intense (Pfeffer and Salancik, 1978). What underpins the RDT is the notion that the external environment is the source of scarce resources that the organisation requires for survival and access to these resources is competitive (Pfeffer and Salancik, 1978; Dwyer et al, 1987). The greatest challenge for organisations comes from their inability to exert any form of control over this environment and its negative effect on managerial discretion. Pfeffer and Salancik, (1978) and Scott (1998) argue that this creates uncertainty and dependency for organisations and so provides the impetus for them to develop creative strategies to exploit these resources and therefore minimise this dependency and uncertainty (Pfeffer and Salancik, 1978). The RDT approach provides a useful lens that allows a firm to identify key resources needed to achieve its objectives.

Pfeffer and Salancik (1978) argue therefore that firms need either to develop internal mechanisms to minimise resource dependency or to adapt to the demands of the external environment. They suggest ways in which an organisation can reduce its increasing resource dependency. These include mergers and diversifications and the use of legal, political and social interventions (Pfeffer and Salancik, 1978). Heide

(1994) emphasises formal and informal links with other firms as one way in which resource dependency challenges can be addressed

The role of the board under the RDT approach is then to establish links with external organisations in order to extract and co-opt the resources needed to survive in competitive environments (Pfeffer and Salancik, 1978). A board is successful from an RDT perspective when its ability to raise necessary resources is strengthened (Callen et al, 2009). Pfeffer and Salancik (1978) further argue that the RDT approach brings four benefits to an organisation, namely access to scarce resources, legitimacy, access to channels of information and access to information through advice from key experienced board members.

The literature on RDT does not, however, provide insight on customer satisfaction and values. In addition, while this theory acknowledges multiple dependencies, Hillman et al, (2009,) argue that RDT does not explicitly outline how a firm prioritises them.

The next discussion focuses on the resource dependency approach's implications for social enterprise.

### ***Resource dependency and social enterprise***

RDT is relevant to the social enterprise sector because boards on nonprofits are keen to increase the flow of resources from external constituencies. Indeed having difficulty in raising capital is a chronic problem in the social enterprise sector (Callen et al, 2009). Social enterprises are increasingly looking for innovative ways to mobilise resources and expertise beyond the social economy (O'Regan and Oster, 2005; Barker, 2003). Strategies include recruiting directors on the basis of their ability to positively influence the outside world to the advantage of their organisations (Callen et al, 2009). This approach is particularly useful to social enterprises as they tend to rely on human and social capital rather than material resources. The board therefore acts as a link to the external environment, which can facilitate access to resources. Pfeffer (1973), in his research on the governance of hospitals in the USA, discovered that boards tended to co-opt well known community leaders as a fundraising strategy. Researchers such as Iecovich (2005), Provan (1980) and Muth and Donaldson (1998) refer to this type of strategy as 'boundary spanning'. It is evident that this is consistent with the RDT approach. For social enterprises RDT can

be associated with legal structures such as company limited by guarantee or share capital companies. Barker's (2002b) work in this area focused on social enterprises with limited by guarantee status. He observes that some of these organisations deliberately target specific individuals for recruitment to their boards, based on their potential to assist the social enterprise in gaining access to specific resources or technical expertise.

The next section focuses on Stewardship Theory (ST) and its implications for social enterprise.

### **3.6.3 *Stewardship model***

Doucouliaos (1994) argues that agency theory, as discussed in Section 3.8.2, is limited in that it acknowledges only a small part of the motivation for human behaviour in firms. Stewardship Theory (ST), a relatively new approach to corporate governance (Davis et al, 1997), offers an alternative perspective in which managerial motivation can be more comprehensively critiqued and analysed. This theory is associated with the work of researchers such as Muth and Donaldson (1998), Donaldson and Davis(1991) , Nicholson (2004), Davis et al (1997). Whereas agency theory emerged from the field of economics, stewardship theory emerged from the fields of sociology and psychology (Davis et al, 1997). This theory, though new in corporate governance literature, has also proved open to different interpretations (Eisenhardt, 1989).

The ST approach presents a different perspective on the structure and role of the board and its relationship with the senior executives of the firm. Under this model, which is typical in for-profit organisations, the role of the board of directors is that of an adviser and strategy formulator (Nicholson, 2004; Silk, 2004). The role of the manager is that of a 'steward' rather than an individual seeking to maximise his/her own utility as agency theory assumes (Muth and Donaldson, 1998, p.5). The motivation of senior managers in the corporation is not a matter of concern under this theory. They are assumed to be essentially trustworthy and pro-organisation and their role is to ensure that the resources of the organisation are efficiently employed to attain financial sustainability (Donaldson and Davis, 1991; Jenkins et al, 2007). In contrast, as previously discussed, the AT approach assumes that agents are motivated by extrinsic factors such as remuneration and perquisites (Jenkins et al, 2007). Stewardship theory acknowledges the importance of non-financial

motivational factors for management. These include intrinsic factors such as the need for achievement, affiliation, recognition, autonomy and authority (Muth and Donaldson, 1989).

The ST approach assumes that there is no conflict between shareholders and management as the latter's interests are assumed to be isomorphic with those of the former (Pfeffer and Salancik, 1978; Davis et al, 1992). It is taken as read that, as managers (stewards) work towards the maximisation of shareholders wealth through high performance, their own utility functions are simultaneously maximised (Low, 2006, Donaldson and Davis, 1991; Davis et al, 1997). Executives are therefore empowered by the board and provided with what they need to perform their duties efficiently and ensure that the financial objectives of the organisation are met. Essential to achieving this objective are flexible organisational structures which empower senior managers to make executive decisions and exploit opportunities for the organisation to attain its objectives efficiently. These include governance structures that provide autonomy in decision making rather than those that monitor and control (Donaldson and Davis, 1991; Donaldson, 1985). Such governance structures can, for example, allow the Chief Executive Officer (CEO) of the firm to chair the board of directors, a situation that would not occur under the AT approach due to its insistence on the separation of ownership and control (Donaldson and Davis, 1991).

This shift of corporate control from stockholders to operational managers or executives can be regarded as a significant improvement on agency theory. It may be an effective way of managing complex firms since it has the potential to facilitate and expedite transfer of the expertise, knowledge and commitment of the board members to the firm (Muth and Donaldson, 1998). It should also be noted that under the ST approach, managers are assumed to have needs they need to satisfy. It is therefore crucial that, for example, a steward receives an income to sustain his /her own livelihood (Donaldson and Davis, 1991). What underpins the ST approach is the assumption that, although managers require remuneration, their activities are aimed at achieving organisational rather than individual objectives.

However, recent high profile corporate failures in such huge organisations as Enron, Worldcom and Parmalat challenge this assumption and therefore also the ability of the stewardship model to ensure accountability and efficiency in firms (Guthrie and Turnbull, 2002; Doherty et al, 2009; Low 2006). The ST approach is still a relatively

new concept in corporate governance and researchers agree that more empirical work is required to deepen our understanding of its underlying assumptions and mechanisms (Donaldson and Davis, 1991).

The next section focuses on the implications of the ST approach for social enterprise.

### ***Stewardship theory and social enterprise***

There is little literature on stewardship theory in the non-profit and social enterprise sectors. However, over the past 15 years there has been an upsurge of interest in the governance of social enterprises. Extensive analytical scrutiny of their internal governance and management includes the work of Mason et al (2006), Low (2006), Moulaert and Nussbaumer (2005), Callen et al,(2009), Fama and Jensen (1983), De La Luz Fernandez and Llamas-Sanchez (2008), Batra (1996) and Barker (2003). Researchers such as Pfeffer and Salancik, (1978), O'Regan and Oster (2005), Miller and Millensen (2003) and Iecovich (2005) have written extensively on the nature of non-profit governance and how this affects their outcomes. There is evidence that researchers and academics within the social enterprise sector are increasingly exploring stewardship theory as an alternative approach to enabling social enterprises to operate competitively in the market (Low, 2006). Van Slyke (2000)'s findings in his study on social enterprises involved in public sector contracting support this contention. His findings showed that the stewardship model is becoming a viable alternative for social enterprises seeking to be competitive in a hostile economic environment.

The effects of changes in the broader macro environment, particularly increased competition for resources has made it imperative for social enterprises to consider other forms of economic relations (Douglas, 1994; Palmaas ,2002). In addition, dwindling public and philanthropic support has exposed weaknesses in institutional forms of traditional social enterprises in terms of their capacity to acquire additional resources (Etchart and Davis, 2003). Low (2006) argues that such economic developments may force social enterprises to move from democratic to stewardship models of governance in order to attract the investments essential for their growth. In support of this view, Cornforth (1988) stresses that the social or democratic type of ownership is not attractive to venture capitalists. Given that social enterprises are hybrids, pursuing both commercial and social objectives, their boards and management need to have the autonomy necessary to operate and generate value

for the organisation and the communities it serves. Research has revealed, however, that more often than not trustees of organisations with democratic governance lack the commitment or business acumen required for social enterprises to operate in competitive markets (Lloyd, 2006).

The development of social enterprise governance also appears to be drifting towards a stewardship model because of the complexities of trading associated with democratic governance models as discussed in Section 2.73 (Low, 2006; Dart, 2004). Although the traditional democratic governance structures of social enterprises are still relevant within the social economy, several researchers such as Batra, (1996); Etchart and Davis (2003), Barker (2003), Ridley-Duff (2002b) and influential support organisations in the social economy such as Social Enterprise London (SEL, 2001b) have questioned their effectiveness given the current economic competitive environment facing social enterprises. They argue that organisations with independent, predominantly voluntary boards are incapable of managing their commercial activities effectively and transparently, hence the increasing interest in the stewardship model of governance. Traditional governance models of social enterprises, as discussed in Chapter 2, are generally characterised by a lack of macro -perspective to guide decision making, resulting in what LRS (2002) refers to as 'the nodding donkey syndrome'. In addition the lack of clear separation of powers between the executive and operational staff can create what McNulty and Pettigrew (1999) call a 'minimalist board', run largely by an individual or dominated by strong founder members, with little or no conflict, challenge or dissent amongst themselves (Spear et al, 2007; McGee et al, 2005).

Cornforth (1988) also argues that governance models characterised by social ownership are among the main obstacles preventing social enterprises from acquiring financial resources from venture capitalists. Mason et al (2006, p.290) agree, arguing that despite its for-profit orientation, the stewardship model is consistent with the ethos of social enterprises and in particular, the 'psychological and social profile of its managers'. For example they argue that the model regards managers as entrepreneurs and members of the community that the enterprise serves, which is entirely consistent with social enterprises. As more opportunities for social enterprises emerge, particularly in public service delivery, they are likely to engage more with external stakeholders including suppliers, investors and the community (Lewis et al, 2004; Low, 2006; Salamon and Anheier, 1996). Ridley-Duff (2002b) and Barker (2003) argue that this type of broader, multi-stakeholder model of

social enterprise governance is required to enhance their capacity for growth and sustainability. These developments and views strongly suggest a multi-disciplinary and more inclusive approach to management and decision making for social enterprise so that they can exploit opportunities as they arise (OECD, 1999a; Batra, 1996).

A move towards the stewardship model reinforces Bubb's (2007) point that social enterprise governance models should be fit for purpose in the twenty first century. Leadbeater (2002) regards this as the single most necessary innovation for social enterprises' success. Such an objective would be difficult to achieve with democratic models of governance given their lack of mechanisms to allow personal ownership of the business or protection of intellectual property. Indeed such mechanisms are traditionally considered alien to the social enterprise sector (West, 2005; Birkhoelzer et al, 1992). Stewardship governance models are therefore more likely to be driven by share capital legal structures that offer a legal mechanism to allow ownership and profit distribution.

Nevertheless, researchers and academics urge caution in this drift towards the stewardship model. It has implications for the fit between strategy and structure as well as social enterprises' decision making abilities, observations made by Sweeney and Hardaker (1994) in their analysis of the East Germany economy. For example, Spear et al (2007) argue that the expansion of social enterprises' thematic activities inevitably raises concerns about their ability to manage entrepreneurial activities without compromising their social ethos. An additional challenge for social enterprises is to move away from the 'delegate' syndrome, where stakeholders prioritise their interests over those of the organisation (Spear et al, 2007, p.11). Low (2006) also believes that this new orientation on governance requires further exploration in terms of its applicability to social enterprise. Barker (2002b), though a critic of the democratic model, does not dismiss it outright, arguing that it is still relevant but only in cases where the stewardship of public finance overrides the imperative of income generation.

Callen et al (2009) and Borzaga and Tortia (2006) argue that it is important to note that the economic environment of non-profits is complex and heterogeneous compared to that of the commercial sector. The ways that the characteristics of the board influence how a social enterprise operates is highly contextual, given the diversity of such organisations' activities. This investigation bases its arguments and



viewpoint on the stewardship model for social enterprise, particularly its for-profit shareholder approach. The model, though untested, provides social enterprises with the flexibility to operate in increasingly competitive environments. Spear et al (2007) and Barker (2002b) argue that this type of governance requires the drive and commitment of social entrepreneurs backed by appropriate legal structures to enable social enterprises to become more professional and competitive. The researcher is aware that there are other governance models that could be considered for the analysis of social enterprise such as the Stakeholder and Carver models. These however are deemed to be unsuitable in analysing institutional innovation in the non-profit organisations that this study seeks to understand. For example, stakeholder theory does not fully clarify accountability in organisations (Sternberg, 1997).

### **3.7 Chapter summary**

Two key elements emerge from the review of the literature in this chapter.

Firstly, there are different approaches to analysing the evolution and growth of social enterprises using suitable frameworks of analysis. These analytical models made it possible to focus on key social enterprise characteristics and attributes from different angles, thus providing a holistic picture of the enterprises' development and transformation. These frameworks are summarised in Section 3.10 below.

Secondly, just as it is for the corporate sector, corporate governance is important for nonprofits. The literature review however shows that despite its importance, the governance of social enterprise is an under-researched area. The governance of social enterprises has implications for how they can mobilise resources beyond the social economy, given the pressure to compete in the market. This is reflected in the increasing interest in the stewardship form of governance in the social enterprise sector.

The next section summarises and discusses key emerging issues from the literature reviews in Chapters 2 and 3.

### **3.8 Key emerging issues from literature reviews**

The two literature review chapters discussed the emergence of social enterprise as a tool to augment state efforts in welfare provision through two key conceptual frameworks. From these discussions, the following issues emerge.

1. Social enterprise is an emerging concept and still suffers from largely unresolved conceptual and definitional issues. There is evidence however that social enterprise has the potential to augment state interventions in welfare provision.
2. There are still significant gaps in our understanding and knowledge of operational issues affecting social enterprise. There has been little scrutiny, scholarly research or attention given to certain key issues and their influence on the operational efficiency of social enterprises in competitive markets. For example, the extant literature is largely superficial with regards to governance as well as the nature, type and determinants of legal structures, factors which are essential in the development of such enterprises. It is this gap in knowledge in the literature that this thesis intends to address.
3. From a theoretical point of view social enterprise suffers from insufficient information and underdeveloped theory. There are still too few explanatory or prescriptive theoretical approaches to understanding social enterprise. One of the key tasks in reviewing the literature on social enterprises in this investigation was to identify suitable theoretical frameworks to act as a guide to the work that follows.
4. Evidence from the literature review suggests that social enterprises in South Yorkshire require appropriate functional governance and legal structures to enable them to enhance their prospects of achieving financial sustainability. The emergence of share capital legal structures indicates that there are other constitutional models for social enterprise that have not yet been fully explored. This is an important area of contemporary social enterprise development, where there are significant gaps in knowledge and understanding.

### **3.9 Towards a framework for analysing social enterprises in South Yorkshire**

Based on the discussions in the literature review it is clear that there is no single framework or approach capable of adequately exploring the complexity of social enterprise. Each of the frameworks of analysis used in this investigation addresses particular specific issues in the development and growth of social enterprises.

By using the IPE framework of analysis it was possible to gain insight into the historical development and transformation of social enterprises as independent sustainable firms. The model also allowed us to analyse social enterprise development from an institutional welfare approach. This enabled us to strengthen our knowledge of the role and capacity of self-governing institutions in providing sustainable welfare interventions. The IPE framework is thus a suitable model to analyse the development of the social economy and social enterprises from a historical and contemporary perspective, in particular their legal set up and relationship with markets. However, its narrow focus on profit maximisation, and focus on close state involvement does not make it a suitable instrument to analyse the internal development of contemporary social enterprises.

The Behavioural Theory of the Firm (BTF) approach made it possible to critically analyse and understand social enterprises as autonomous, dynamic businesses competing in the market to create value for communities they serve. Although this approach has its foundation in neo-classical economic theory (which is also a source of criticism) its use in this thesis made it possible to merge economic and social dimensions of contemporary social enterprises (Laville et al, 2004). Crucially, despite being a broad theory, the BTF approach becomes a suitable theoretical lens to critically analyse the internal governance of social enterprises and how they can address threats arising from external economic dynamics. This enabled us to capture the dilemmas of social enterprises as they undergo institutional changes in order to remain viable. A key characteristic of the BTF which is not shared by the IPE approach is its ability to analyse the internal processes and structures of an organisation. This is essential for this analysis of social enterprises in South Yorkshire, since it is the main objective of this study.

### 3.10 Hybrid framework for analysing social enterprises

As noted above, it is clear that there is no single framework or approach that can adequately explore the complexity of social enterprise. Each of the frameworks of analysis used in this investigation addresses particular specific issues in the development and growth of social enterprises. This thesis therefore adopts a hybrid framework of analysis comprising the Institutional Political Economy (IPE) together with the Behavioural Theory of the Firm (BTF). Figure 3.1 below shows this framework created from key elements gleaned from these two approaches to analysing social enterprises.

**Figure 3.1: Hybrid framework for analysis of social enterprises**

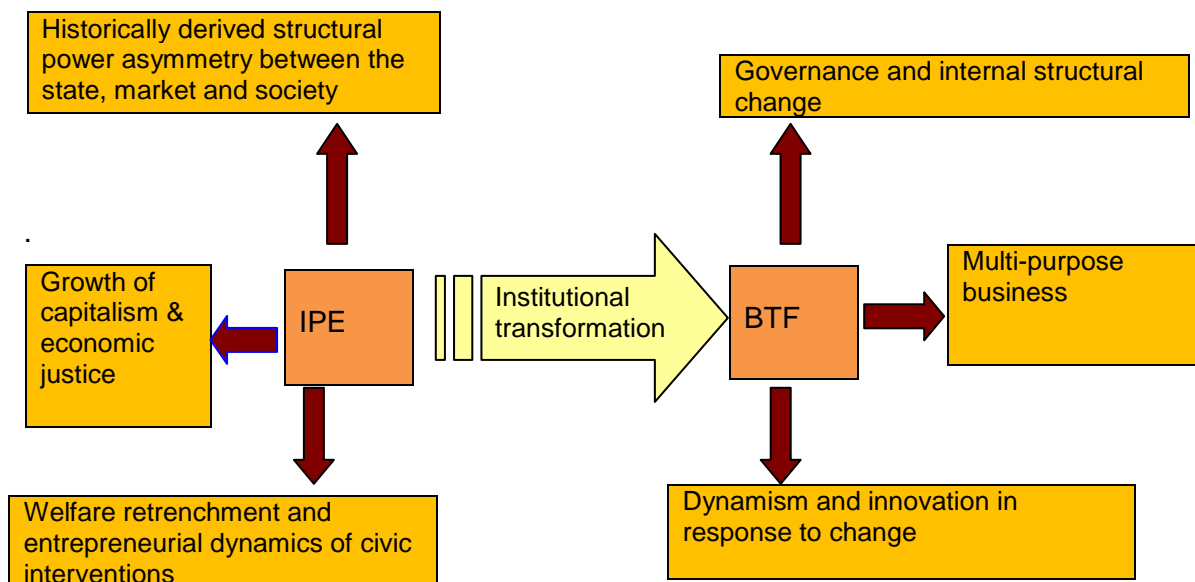


Figure 3.1: Based on Gonzales (2008), Chang (2002), Nyssens (2005)

In this investigation, the hybrid framework makes it possible to:

- (i) Understand the historicity and positionality of social enterprises within the matrix of the market, state and society. As the literature review shows, social enterprise emerged from the social economy, which lies between the state and the markets. The social economy itself developed from the adverse effects of markets and capitalism on society. Analysis of the socio political context of social enterprise is crucial in understanding its contribution and ability to augment the state in welfare provision and perhaps, ultimately, to replace it.
- (ii) Understand key objectives and motivations of social enterprise. Despite their philanthropic history, social enterprises seek to be viable businesses so that they can

compete autonomously in the market in order to maximise delivery of value. Given the external social demands and increasing economic pressure on social enterprises to successfully compete in the market, their need for institutional transformation to operate effectively as commercial firms has become more pressing.

(iii) Analyse internal governance and legal frameworks .A key driver of institutional transformation is the need for social enterprises to respond to changes in the economic environment and to access resources beyond the social economy to further their aims. Achieving this, and therefore being in a stronger position to exploit opportunities, may require adjustments and reconsiderations of their internal organisational systems.

The next chapter discusses the methods used to collect the evidence used in this investigation in order to answer the research questions shown in Chapter 1.

## **CHAPTER 4: METHODOLOGY**

### **4.1 Introduction**

The purpose of this chapter is to discuss and clarify how evidence in this thesis was gathered and analysed in line with the research questions specified in Chapter 1. The chapter is divided into four parts. The first discusses previous and current research undertaken in the field of social enterprise and identifies opportunities and challenges associated with researching social enterprise. The second provides an insight into, and rationale for, the structure of the research design and methodology used in the investigation and how findings were arrived at. Links between the methodology and frameworks of analysis identified in Chapter 2 are also illustrated and discussed. The third focuses on the data collection methods used in the investigation including their limitations. Validity, a key consideration in social science research, is also discussed in this section. The last part discusses the constraints and challenges faced in the investigation and how these were addressed.

### **4.2 Researching social enterprise**

The concept of social enterprise is relatively new and under researched in the UK and indeed worldwide (BRASS, 2006; Weerawardena and Sullivan, 2006; Smallbone et al, 2001). This emerging field is generally underdeveloped and lacks the critical mass needed to fully understand it (Peattie and Morley, 2008; Thompson, 2002; Urban, 2007). Despite various scoping exercises in the UK there is still no definitive baseline illustrating the nature of social enterprises in the country (Haugh, 2005). The scoping exercises also reveal significant gaps in knowledge and information on the development of social enterprises. For example, Lyon et al (2002) note that the reports from these exercises highlight the current lack of robust empirical evidence of the impact of social enterprises in deprived areas, despite this having been a key policy objective of the UK government. The situation is no different in the South Yorkshire region, which is the geographic focus of this investigation.

#### ***4.2.1 The South Yorkshire perspective***

Geographically, the South Yorkshire region is spread across the unitary boroughs that constitute it, namely Sheffield, Rotherham, Doncaster and Barnsley. One of the key tasks of this research was to gain an understanding of the nature of social enterprises in the region and the state of their development. Despite a number of mapping exercises, the number of organisations describing themselves as social

enterprises operating in the region and their scope and character is difficult to ascertain (DTI, 2003a). For example, Sheffield Community Enterprise Development Unit (SCEDU) commissioned a social enterprise mapping exercise in 2003. This piece of unpublished work was restricted to Sheffield and therefore could not give a true picture of the regional social enterprise development (SCEDU, 2003b). In 1997, the Regional Development Agency for Yorkshire and the Humber, Yorkshire Forward, commissioned a study of social enterprises across the region. To date, however the results of this exercise have not been made publicly available. It is in this context that this research was undertaken.

Chapters 2 and 3 of this investigation show that the relative lack of research on social enterprise can be explained in part by its paradigmatic positionality between the private sector and the voluntary sector (Doherty et al, 2009; Salamon, 1994). From a methodological perspective the main implication of this is, as seen in Chapter 2, that theoretical frameworks used to analyse social enterprises tend to derive from either the private or voluntary sector with most so far tending to come from the latter. Since this work has adopted a hybrid framework incorporating the Institutional Political Economy theoretical approach and elements of the Behavioural Theory of the Firm, the design and methodological approach is necessarily influenced by this.

The next section looks at the duration of the research before discussing and analysing the research design.

### **4.3 Duration of the study**

The data collection and analysis in this study was conducted over a period of two and a half years, stretching from June 2005 to December 2007. The time line of the investigation indicating the time taken to complete each component is shown below in Table 4.1. The author of this report, Walter Mswaka, carried out the study as a part-time research student. The research design and methodology employed in the course of the study is discussed below.

**Table 4.1: Research time line**

	<i>From</i>	<i>To</i>
Questionnaire survey	June 2005	September 2005
Interview of support organisations 1	June 2005	September 2005
Interview of support organisations 2	December 2006	July 2007
Case study interviews	January 2007	April 2007
Case study analysis	May 2007	September 2007
Archival Research	May 2005	December 2007

The next section looks at the research design before discussing the data collection methods used.

#### **4.4 Researching social enterprises: the research design**

In any research, it is essential to have a robust framework that allows the researcher to gather and analyse data to provide answers to the research questions. The hybrid framework of analysis comprising elements of the IPE and BTF approaches, as discussed in Chapter 3, was central to developing the research strategy for this work. It is evident that the BTF approach involves understanding the motivations of the firm as well as its internal governance and how this influences its outcomes. The IPE approach makes it possible to understand the historicity of organisations and their relationship with the market and the state.

Bryman and Bell (2003) as well as Ghauri and Gronhaug (2005) refer to the development of such a framework or plan as the research design. Trochim (2006) conceptualises the research design as the 'glue' that holds together the key elements of the research process. He identifies three types of research design. Firstly, if a random assignment is employed then the design is normally referred to as a randomised or true experiment. Secondly, if the research design makes use of multiple groups or waves of measurements, then the design is described as quasi-experimental. Thirdly, if the design uses neither of the above, then it is referred to as a non-experimental design. His model is shown below.



**Figure 4.1: Classification of research designs**

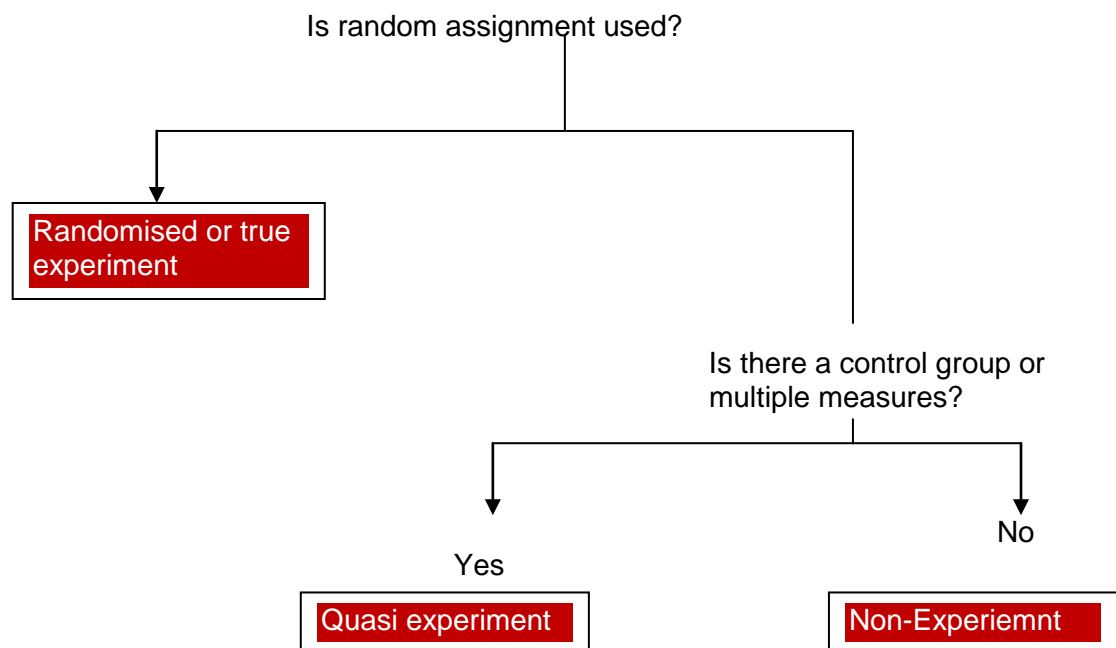


Figure 4.1 based on Trochim (2006)

Since this design makes use of mixed methods to extract required data then, according to Trochim's (2006) model, this is a quasi-experimental research design. The mixed methods approach is discussed in Section 4.5.

In order to capture a comprehensive picture of social enterprise development and support in the region, the research design involved a two- pronged approach, focusing on two specific target populations. These were organisations that described themselves as social enterprises and those who considered themselves to be social enterprise support organisations. A two-pronged approach was preferred for the following reasons. Firstly the focus on social enterprises enabled the researcher to understand the nature and patterns of development of these organisations across the region. Secondly, this technique allowed the researcher an opportunity to analyse different stakeholders within the social economy and their influence on social enterprises. These stakeholders include funders, employees and public sector institutions. It should be noted that researchers such as Lyon et al (2002) have carried out research in this field and used similar techniques to obtain a rich set of data from key informants in the sector. The research design also involved a case study approach explained in Section 4.9. This technique further explores results

arising out of the analysis of questionnaire returns from informants across South Yorkshire.

Therefore the structure of the research design involved multiple investigations of individual social enterprises supplemented by parallel research on social enterprise support organisations and selected case studies within the study area as explained below.

#### ***(a) Social enterprises***

In order to answer the research questions outlined in Chapter 1, it was necessary to investigate the individual social enterprises across the region. This would make it possible to understand their historical background, distribution, characteristics and, particularly, the nature and form of their governance and legal structures. These are key constructs of the IPE approach. Section 4.2.illustrated the dearth of information and statistics on social enterprises across South Yorkshire, despite the importance attached to them in the region. Where information existed, it was either too little or inconclusive. Therefore gathering vital information on the scale of social enterprises in South Yorkshire was a key component of the research design of this investigation.

#### ***(b) Social enterprise support organisations***

The research on social enterprise support organisations sought to identify and analyse infrastructural support for social enterprises in the region. We have seen that social enterprises exist in an environment characterised by a number of stakeholders who influence their operations directly and indirectly. Therefore it was important to identify and analyse support organisations for this sector and ascertain their impact on developing social enterprise across the region. It was also important to elicit and analyse the perceptions of these support organisations on various components of social enterprise development, such as their governance. Section 4.11 analyses in detail how the support organisations were identified and interviewed.

#### ***(c) Case study analysis***

This method allowed the researcher to pursue emerging themes emanating from the quantitative research using real life examples of organisations in their natural setting (Oates, 2006). The case study approach was structured around key areas of the

operations of social enterprises under scrutiny. These included determinants of their legal structures as well as their internal governance and financial performance in line with the hybrid framework used in this study. The case study method also enabled the researcher to use complementary data collection methods such as interviews and direct observation to enrich the data gathered. This approach is discussed in detail in the data collection method section of this chapter.

The research design in this investigation therefore comprised three components, namely an investigation of social enterprises and of support organisations and a case study approach, the rationale for which has been discussed above.

#### ***4.4.1 The research sample and sampling techniques***

Correctly defining the target universe of a study population is an essential element of any research (Heath, 1997). Having identified the target populations of this research, as shown above, it was then necessary to consider how representative samples could be constructed. Current research statistics suggest that there are 55,000 social enterprises and support organisations in the UK (SEC, 2007). It was not possible to investigate all these social enterprises, hence the need for a representative sample. In this investigation, self-defined social enterprises operating in South Yorkshire were the representative sample. However, as previously mentioned, information on the definitive number of social enterprises in the region was unavailable. Using current knowledge and experience and the extrapolation of figures from information held by sub-regional social enterprise support organisations, it was possible to estimate the number of social enterprises in the region as not more than 400. A large sample was necessary to reduce the likelihood of sampling errors (Graziano and Michael, 2004). The research sample was drawn from self-defined social enterprises with legal structures falling into the following most common categories:

- Company limited by guarantee
- Company limited by shares
- Unincorporated associations
- Industrial and Provident Societies/Cooperatives

At the time the research was undertaken, the new social enterprise legal structure, the CIC, had not been launched.

In order to capture a comprehensive picture of social enterprise development across the region, parallel research on dedicated social enterprise support organisations was also undertaken. Based on current knowledge the number of such organisations across the region was estimated as not more than ten. Therefore the researcher considered all these organisations as a sample for the investigation. Empirical research relies on a sample that accurately represents a target population (Heath, 1997). In research, the population refers to the subjects being studied (Ramchander, 2004). This investigation covered a very large geographical area of around 1,560 sq km (National Statistics, 2003). Therefore it was critical to obtain a sample that was large enough to be representative of the target population. Selection of an appropriate sample or target population is important because any study's level of accuracy depends to a large extent on its sample size (SRI, 2002). The larger the sample, the more accurately it will reflect the general population (Nesbary, 2000).

The selection of informants for this study was done using a random stratified sample of social enterprises and organisations operating in South Yorkshire. Ghauri and Gronhaug (2005, p. 150) describe a stratified sample as a probability sample whose 'parent population is divided into mutually exclusive and exhaustive subsets'. They assert that a researcher using this method is able to independently pick a random sample of units. The stratifying criterion used in this sample was based on the differentiation of research subjects as either a social enterprise or support organisation. This means that two strata were formed namely, a population consisting of individual social enterprises and another of social enterprise support organisations, both in South Yorkshire. This distinction was important because the researcher was cognisant of the fact that these two strata required different approaches to data collection. The rationale behind the use of the stratified sampling technique was the need to avoid bias and obtain a clear representation of the total population within reasonable margins of error (Taylor-Powell et al, 2003).

Having discussed the research design and sampling technique, the following section looks at the data collection methods used in this investigation.

#### **4.5 Research methods and techniques**

Research is 'a viable approach to a problem only when there are data to support it', (Leedy and Ormrod, 2001). It was therefore necessary to ensure that appropriate and

adequate data were gathered to address the research questions identified in Chapter 1, namely;

1. What are the different types of legal structures of social enterprises in South Yorkshire?
2. What are the key determinants of social enterprises' legal structures?
3. In what ways does the nature and type of legal structure influence the outcomes of social enterprises?

Addressing these three questions required a robust methodology that could compare salient features of social enterprises as they evolve over time.

Social science researchers have an array of data collection methods to use in the research process. There are three distinct approaches to collecting data (McNeal, 1985). These are qualitative, quantitative and mixed methods techniques (Ramchander, 2004). Quantitative methodologies are concerned with measurement i.e. quantifying the association between two or more variables usually in a statistical manner (Livesey, 2005). Researchers using this method tend to remain relatively detached from the target population and to use quantitative research instruments such as structured questionnaires and surveys to gather data from informants. This is referred to as unobtrusive research (Miles and Huberman, 1994) and is grounded in positivism (Creswell, 1994). In the domain of the social economy this technique allowed the researcher to obtain measurable information on social enterprises that could be statistically analysed (Veal, 1997).

Qualitative data collection methods attempt to specify the quality of the relationship between two or more issues as well as to understand the meanings and interpretations that people ascribe to things (Livesey, 2005). Hence Ramchander (2004 p.104) argues that this type of data collection methodology is grounded in 'the interpretive social sciences paradigm'. The researcher becomes closely associated with the target population during the research using qualitative techniques such as in-depth semi-structured interviews and observation (Jennings, 2001). Qualitative data collection methods address aspects of reality that are difficult, if not impossible, to measure (Miles and Huberman, 1994; Creswell and Clark, 2007). Proponents of this type of approach argue that it is only through qualitative methods that 'the world can be studied through the eyes of the people that are being studied' (Bryman and Bell 2003, p .469).The mixed method approach combines both qualitative and

quantitative approaches and may be viewed as located in the middle of the continuum as it incorporates elements of both qualitative and quantitative methodologies (Creswell, 2003). Table 4.2 below shows the salient features of the three approaches.

**Table 4.2: Approaches to data collection**

<i><b>Qualitative</b></i>	<i><b>Quantitative</b></i>	<i><b>Mixed methods</b></i>
Interview, observation, document and audiovisual data Open ended questions Emerging methods	Instrument based questions Statistical analysis Predetermined Performance, observation and census data	Predetermined and emerging methods Open and closed questions Multiple forms/sources of data Statistical and text analysis

Table 4.2 based on Creswell (2003)

In this study a mixed methods approach was considered ideal in researching the social economy as it includes a variety of institutions and individuals who need to be communicated with at different levels. The use of a mixed method approach has some distinct advantages. It makes it possible to strengthen conclusions from the data collected through triangulation (Webb et al, 1996). It makes it possible to investigate a wider variety of aspects of social enterprise development, necessary given the current scarcity of information. The data collection methods used in this investigation are discussed in detail in Section 4.6, below. An important component of the data collection methods was field work, which is a key aspect of the research process in social sciences. One of the main advantages of field work is that it allows the researcher to gain and develop strong local knowledge (Thomas et al, 1998). The researcher undertook extensive field work which involved administering questionnaires and carrying out face-to-face and telephone interviews with key informants. Of particular benefit was the ability to visit informants' business premises and to verify information provided to ensure its quality and validity.

The next section focuses on the data collection methods used in the investigation.

#### 4.6 Data collection methods

The preferred methodological approach in this study was a mixed method approach which had four components. These were surveys undertaken by means of postal questionnaires, semi-structured interviews, archival research and case study analysis. Archival research was an on-going exercise throughout the investigation as shown previously in Table 4.1. The continuous evolution of social enterprise coupled with policy changes meant that the researcher had to re-visit archival information on several occasions to update it. Figure 4.2 below provides an overview of the four components of the data collection methodology.

**Figure 4.2: Components of the study**

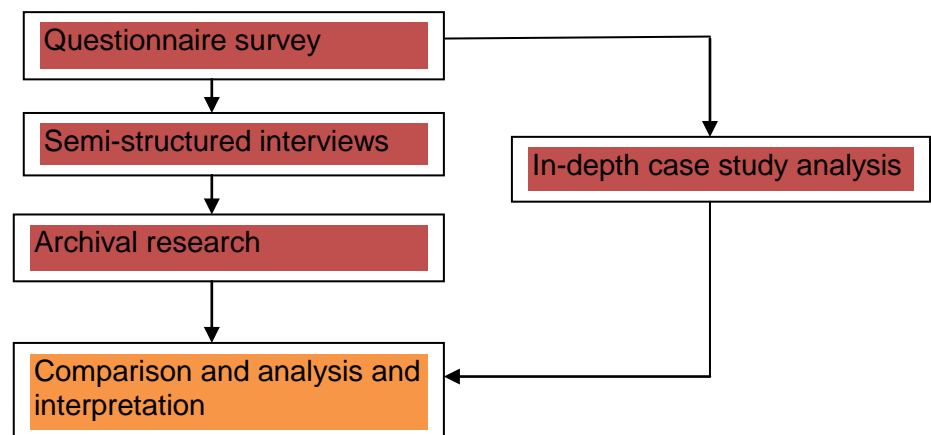


Figure 4.2: Author's construct

Figure 4.2 above shows that a questionnaire survey was the first stage of this investigation. The next section therefore focuses on the questionnaire survey.

#### 4.7 The questionnaire survey

In Section 4.2 it was argued that the paucity of reliable data makes it difficult to characterise social enterprises, let alone identify and target them. This necessitated a survey targeting organisations that called themselves social enterprises. In Section 4.4.1. the number of social enterprises in South Yorkshire was estimated to be around 400. The questionnaire survey technique allowed the researcher to identify and analyse relationships and patterns between the various types of social enterprises as well as organisational design issues. The South Yorkshire region

covers an area of approximately 1,560 sq km and consists of four unitary boroughs. Because of the geographical area to be covered, postal questionnaires were preferred to face-to-face interview techniques (Denscombe, 2003; Ghauri and Gronhaug, 2005). Using postal questionnaires was generally a less expensive way of obtaining significant amounts of data from a large number of potential respondents. It also allowed the researcher to simultaneously capture the required data as well as identify emerging patterns of social enterprise development across the region.

#### ***4.7.1. Accessing respondents***

Getting access to respondents is often a difficult challenge for researchers. This investigation was no exception, given the limited amount of information on social enterprises available across the region.

Before postal questionnaires could be sent out, a data base of social enterprises in South Yorkshire was needed so that contact addresses could be extracted and the researcher could get an idea of the number of social enterprises in the region (Hair et al, 2007). However, this information was virtually non-existent as there has been no official census of social enterprises in South Yorkshire, except an informal survey carried out by Sheffield Community Enterprise Development Unit (SCEDU) in 2003. (SCEDU is a sub-regional social enterprise support organisation funded under contract to support the development of social enterprises in Sheffield.) This survey put the number of social enterprises in Sheffield at 44 (SCEDU, 2003). However there was no information on the number of social enterprises in the other boroughs (Barnsley, Rotherham and Doncaster), that make up South Yorkshire. The researcher was employed by SCEDU as a social enterprise business adviser during this period of the investigation. He was therefore able to utilise his social capital to obtain information from the additional boroughs.

The overall objective of this information gathering exercise was twofold. Firstly the researcher wanted to identify contact addresses particularly for those social enterprises that had been in contact and registered with sub-regional support organisations. Secondly the researcher wanted to identify organisations that described themselves as social enterprises and were either starting out or at an advanced stage of development. The advantage of this approach was that it would be easier to follow up information and cross check evidence.



Contact addresses of social enterprises were obtained from current and updated sub-regional social enterprise support organisations' databases in South Yorkshire as well as from published information and the archives of other independent organisations in the region. Gathering the information was not easy since the sub-regional organisations either had no information or were uncooperative. These methodological problems are discussed in detail in Section 4.15.

#### ***4.7.2 .Design and administration of questionnaires***

One of the advantages of using a structured postal questionnaire is its adaptability (Malhotra, 1996; Douglas, 2000). For example, the design and structure of the postal questionnaire used in this investigation made it possible to obtain some elements of qualitative data as well as the usual quantitative data (Proctor and Renfrew, 2000). As a result a significant amount of useful qualitative information which enriched the data was obtained in a cost effective manner. The questionnaire used in this investigation is attached as Appendix 1.

When designing a questionnaire it is important to be aware that it may be the only opportunity to interact with informants (Hair et al, 2007). Developing a questionnaire and its constituent questions requires a systematic approach. Saunders et al (2009) argue that in developing individual questions, researchers can either adopt or adapt questions used by other researchers or can develop their own. In this research, the researcher developed his own questions. It was important to first clarify the research objective and related questions and then to define the target population and sampling frame (Bryman and Bell, 2003). There is no value in asking questions that do not relate to the research objective; hence the data a researcher wishes to collect influences the design of the questionnaire (Saunders et al, 2009). The target population for the questionnaire survey consisted of self-defined social enterprises. The research objectives and the researcher's knowledge of the social enterprise sector therefore guided his thought process in developing draft questions. These were then evaluated from a respondent's perspective to ascertain whether they could be understood and answered and, in the light of this evaluation, re-drafted in order to avoid ambiguity, access the required sample and maximise response rates (Hair et al, 2007; Bryman and Bell, 2003).

The questionnaire contained two sections. Section A focussed on the patterns and characteristics of social enterprises in South Yorkshire. This included opening

questions as well as those specifically aimed at topics relevant to the research questions. Section B focussed on aspects that assisted the researcher in understanding the results better. Hair et al (2007) refer to these as classification questions. For example the questionnaire has open ended questions that allow respondents to answer freely using their own words (Bryman and Bell, 2003). A disadvantage of this type of question is that the answers require coding and this can be time consuming in the analysis stage.

Once contact addresses were obtained, a total of 218 postal questionnaires were sent, in early June 2005, to self-defined social enterprises in the boroughs within the area of study. By the initial deadline of the end of August 2005, 80 completed questionnaires had been returned. Reminders, with copies of questionnaires attached, were sent to non-respondents in September. A further 22 questionnaires were received in response to these reminders. Therefore the overall result was a sample of 102 completed questionnaires from 218 active social enterprises that were surveyed. Postal questionnaires are usually associated with low response rates (Lee, 1998; Alreck and Settle, 1995). Indeed, in contemporary social sciences research involving postal questionnaires, response rates of less than 10% are not uncommon (Oates, 2006). Therefore the overall return rate of 46% that was achieved seems to be well within reasonable expectations of a postal survey. The return rates per borough surveyed are shown below in Table 4. 3. Note that the responses came from organisations that described themselves as social enterprises.

**Table 4.3: Questionnaire returns**

<i><b>Town/borough</b></i>	<i><b>Qns sent out</b></i>	<i><b>Qns returned</b></i>	<i><b>% return</b></i>
Sheffield	115	65	57%
Barnsley	30	12	40%
Rotherham	33	11	33%
Doncaster	40	14	32.5%
<b>Total</b>	<b>218</b>	<b>102</b>	<b>46%</b>

The respondents came from a wide spectrum of organisations describing themselves as social enterprises across South Yorkshire. The thematic representation revealed by the 102 respondents is shown below in Table 4.4. These thematic areas include childcare, training and development and other activities. The term 'Regeneration Catalyst' is used as an umbrella term to cover social enterprises involved in a number of initiatives, trading and non-trading, in pursuit of achieving socio-economic and environmental objectives. For example one respondent's social enterprise is

involved in environmental consultancy, providing support to disabled people, the provision of managed workspace, the delivery of Learn Direct Courses and providing childcare facilities, all under one roof!

**Table 4.4: Thematic activities of social enterprises in South Yorkshire**

<b>Thematic Activity</b>	<b>Number of organisations</b>
Manufacturing	1
Arts and new media	11
Environmental	6
Catering	1
Childcare	3
Managed workspace	4
Transport services	2
Training and education	22
Health and well being	5
Regeneration catalyst	20
Employment services	9
Information technology	2
Retail	4
Banking and financial products	3
Advocacy	1
Language promotion and development	3
Commercial cleaning services	1
Communications	1
Security equipment installation	2
Broadcasting services	1
<b>Total</b>	<b>102</b>

Table 4.4: Created from results of questionnaire survey

#### **4.7.3. Data analysis of questionnaire returns**

Prior to the advent of computer software, quantitative data analysis was done manually (Saunders et al, 2009; Hair et al, 2007). This was often a laborious and time consuming exercise leading to inconclusive or flawed research results. In order to prevent this, a computer-based statistical analysis tool, SPSS, was used to analyse the data. It was also selected because of the empirical nature and size of the sample that had been obtained. SPSS made it possible to define independent variables and conduct cross tabulations and descriptive statistical analysis of the data (SRI, 2002; Saunders et al, 2009). It was possible to explore key dimensions in order to understand the rationale of social enterprises. Some of the information emanating from the descriptive statistical analysis of the data is presented in Chapter 6.

#### **4.8 Qualitative data collection: support organisations**

From his current knowledge and experience, the researcher knew that the number of social enterprise support organisations in South Yorkshire was not huge. A qualitative research technique was therefore deemed an appropriate methodology to obtain data from informants. Quantitative research is, as discussed above, important in identifying patterns of phenomena. However, the researcher felt that a qualitative research technique would provide a deeper understanding of the complex processes associated with the operations of social enterprise support organisations. This technique allowed the researcher to interact with key informants on a conversational basis and to explore other themes relevant to the research (Ramchander, 2004). While quantitative research is efficient, it may miss the contextual detail that can be captured by qualitative techniques (Miles and Huberman, 1994). In addition, data alone do not tell the whole story as Thomas et al (1998) argue. The qualitative techniques used in the study include a mixture of semi- structured face-to-face open-ended interviews using an interview guide and direct observation. These enabled the researcher to capture the respondents' attitudes and perceptions of various issues connected with the research questions (Saunders et al, 2009; Hair et al, 2007). The interview guide is attached as Appendix 2.

#### **4.8.1 Administration of support organisations' interviews**

The scrutiny of support organisations was done in stages. The first ten organisations interviewed are all based in South Yorkshire. The interviews took place during the same period that postal questionnaires were sent to individual social enterprises across the region. The second group of support organisations that were interviewed included a mixture of both South Yorkshire based and national organisations. This dual approach was necessary to facilitate the verification and corroboration of patterns emerging from questionnaire returns in the region. It was also important to construct a holistic picture of social enterprise support organisations across the region to identify the range and nature of support packages available. Contact information for the social enterprise support organisations was obtained from both regional and sub-regional social enterprise support databases in South Yorkshire. These organisations are shown below in Table 4. 5.

**Table 4.5 Social enterprise support organisations in South Yorkshire**

- Sheffield Community Enterprise development Unit (SCEDU)
- Social Enterprise Barnsley (SEB)
- South Yorkshire Open forum ( SYOF)
- Sheffield Co-operative Development Group (SCDG)
- South Yorkshire Key Fund for Social Economy (SYKFSE)
- Business Link South Yorkshire
- Community Enterprise Doncaster/Doncaster CVS
- Phoenix Enterprises Rotherham Social Enterprise Unit
- South Yorkshire Open Forum
- In My Backyard (IMBY), regional representative of Social firms UK
- Open Forum For Economic Regeneration (OFFER)

The second group of social enterprise support organisations interviewed and the reasons for their selection is shown below in Table 4.6. This group contains organisations in and outside the South Yorkshire region. Their selection was largely driven by the need to understand the policy context within which social enterprises were operating from both a regional and national perspective. Understanding this allowed the researcher to analyse the institutional drivers of social enterprise as well as the future of the phenomenon. Key organisations contacted include the Office of the Third Sector (OTS), which is the government office responsible for social enterprises and the voluntary sector organisations and the Social Enterprise Coalition (SEC), which is the umbrella body for social enterprises. From these organisations,

the researcher was able to gain insight into policy formulation and implementation as well as implications for social enterprises from a national perspective. Emails and the telephone were used to secure interviews with key informants from these organisations. Contact addresses were obtained from their websites and published information. The researcher also used his contacts from working within the sector to secure interviews with regional support organisations such as banks and solicitors. These interviews took place between December 2006 and April 2007.

Blumer (1969) argues that it is every researcher's wish to extract information from informants who are well informed. In order to obtain a rich and reliable set of data, it was necessary to contact and interview senior staff from the social enterprise support organisations shown in Table 4.6. Though selection of informants was otherwise random, requests by email, letter or telephone were aimed at securing interviews with senior managers, directors or chief operating officers.

**Table 4.6: Key regional and national social enterprise support organisations**

<b>Support organisation</b>	<b>Location &amp; position of interviewee &amp; date</b>	<b>Reason for selection</b>
Yorkshire Forward: RDA for Yorkshire and the Humber	<b>Leeds:</b> North Yorkshire Henry Rigg; Enterprise Development Officer (1 December 2006)	To ascertain current policy and future of social enterprise development in South Yorkshire after expiry of European Funding.
HSBC bank	<b>Sheffield Branch</b> Syed Taaudi; Commercial Manager- South Asian Baking (February 2007)	To investigate private sector financial support for social enterprises.
Unity Trust Bank :Ethical Bank	<b>Sheffield</b> Yvonne Bramall; Regional Manager (28 January 2007)	To analyse financial support for charities, voluntary sector organisations and social enterprises from ethical banks.
Office of the Third Sector	<b>London</b> Veronica Johnson; Social Enterprise Unit (21 March 2007)	To investigate social enterprise policy formulation and implications at national level.
HLW solicitors	<b>Sheffield</b> Keith Arrowsmith; Senior Partner (31 January 2007)	One of the key architects of the NEWCO – share capital model for social enterprises.
Bates ,Wells & Braithwaite solicitors	London Abbie Rumbold; Senior partner (11 April 2007)	The architects of the Community Interest Company (CIC).
Sheffield City Council Regeneration department.	<b>Sheffield</b> Phil Reid; Inclusion & Diversity Manager (22 February 2007)	To analyse policy formulation and implications at local level.
Social Enterprise Coalition	Nic Buckley; Office Manager (19 March 2007)	To analyse social enterprise policy formulation and advocacy.

A total of eighteen social enterprise support organisations across South Yorkshire, and beyond were surveyed. The support organisations were divided into four categories for ease of investigation as illustrated in Table 4.7 below. This categorisation was useful because the support these organisations provide has different implications for social enterprise development. In addition, the researcher was aware that some of these organisations needed slightly different interview questions to obtain the required data.

**Table 4.7: Categorisation of social enterprise support organisations**

<i><b>Funders</b></i>	<i><b>Sub-regional social enterprise support organisations</b></i>	<i><b>Regional policy formulation and policy organisations</b></i>	<i><b>National policy formulation and advocacy organisations</b></i>
1.HSBC bank	1. Sheffield Community Enterprise Development Unit (SCEDU).	1.Yorkshire Forward	1.Office of the Third Sector
2. Unity Trust Bank		2.Sheffield City Council	2.Social Enterprise Coalition
3. Key Fund for Social Economy (SYKFSE)	2. Social Enterprise Barnsley (SEB).	3.Open Forum For Economic Regeneration (OFFER)	3.Bates Wells & Braithwaite solicitors
4. Sheffield Co-operative Development Group (SCDG)	3. Community Enterprise Doncaster/Doncaster CVS.	4.In My Backyard(IMBY) regional representative of Social firms UK	
5. South Yorkshire Business Link	4. Phoenix Enterprises Rotherham Social Enterprise Unit.	5.South Yorkshire Open Forum (SYOF)	
	5. HLW solicitors.		

Table 4.7: Created from secondary data information

The interview guide is attached as Appendix 3.

#### **4.8.2 Analysis of support organisations' data**

The analysis of the interview transcripts from the social enterprise support organisations was done manually, identifying key themes that were central to answering the research questions, as explained in Section 4.11. This was because



the sample was too small to warrant the use of analytical software. The analysis involved going through each interview transcript, coding information and identifying key themes that emerged, which were then compared to those emerging from other transcripts. (Saunders et al, 2009). This gave the researcher a general picture of key issues that were emerging and their implications for social enterprise growth.

#### **4.9 Detailed case study analysis (January - April 2007)**

The previous discussion focussed on the quantitative and qualitative research undertaken in an attempt to gain a deeper understanding of the nature and character of social enterprises in South Yorkshire. The descriptive statistics that emerged provided a platform for a more detailed analysis of social enterprises in the region. Further investigation was carried out using a multiple case study approach in line with the research questions outlined in Chapter 1. Table 4.12 provides a summary of how the case study method was used to answer the key research questions and complement the quantitative research discussed in preceding sections.

In social science research the use of case study methodology is gaining prominence despite not being listed in major research texts in this discipline (Tellis, 1997). The increased use of this method has resulted in an extensive body of knowledge dedicated to its development and refinement (Kohn, 1997; Yin, 2003; Tellis, 1997; Stake, 1995). Kohn (1997) in particular argues that the use of the case study research method is gaining ascendancy because of the shortcomings of other data collection methods in providing answers to important questions researchers are asking. The case study approach is subject to many definitions. Cutler (2004, p.367) defines it as an approach to exploring and carrying out in-depth analyses of complex processes 'that cannot be easily separated from the social context' within which they occur. Other advocates of its use such as Stake (1995) and Tellis (1997) consider that the case study approach makes it possible to understand more than what is obvious to an observer. Stake (1995) in particular emphasises that a case study research method is multi-perspective. It allows a researcher to focus both on the target of the investigation and on other relevant stakeholders and how they interact with the research object. Tellis (1997) concurs that this is a key characteristic of the case study approach that distinguishes it from other methods of data collection. Thomas et al (1998, p. 307) consider the case study research method to be 'a framework for investigation' rather than a specific method, adding that with such a framework it is possible to use several additional methods of collecting data such as

semi-structured interviews and direct observation. Towill (2006) notes that the use of a multi-method approach also makes it easier for a researcher to achieve validity by triangulating different sources of evidence and theory. For this reason the case study approach is also known as a triangulated research strategy. Yin (1994a, p. 23) regards the case study approach as an empirical enquiry used to 'investigate contemporary phenomenon with real life context'. With reference to research objectives and outcomes Yin (1993) classifies case studies as shown in Table 4.8 below, emphasising that the boundaries between these classifications are not sharply defined.

**Table 4.8: Case study classification**

<i>Type of case study</i>	<i>Objective</i>
<b>Explanatory</b>	Focuses on causal processes and seeks to explain how and why specific events occur. Seeks to examine how research findings might be explained by theory.
<b>Exploratory</b>	Mainly used as a pilot exercise prior to launching a full scale investigation. Usually used to define research questions and hypothesis.
<b>Descriptive</b>	Describes a phenomenon within its context and requires prior formulation of cause and effect hypothesis.

Table 4.8: Adapted from Yin (1993)

The purpose of this investigation is to understand the nature of social enterprises' legal structures and how they influence their outcomes. Therefore, cognisant of Yin's (1993) model above, the explanatory case study approach is considered the most appropriate strategy for this investigation.

The above definitions of case studies, particularly Yin's (1993) model, strongly support choosing the case-study approach to address the objectives of this research. We have seen that social enterprises in South Yorkshire exist within a broader environment characterised by a plurality of actors. Therefore a case study approach allows the researcher to analyse relevant stakeholders and their influence on each others' activities. This includes analysis of social enterprise infrastructure organisations and the funders and staff of social enterprises. The value of a case study approach is that it increases the experience and improves the understanding of

the influence of the organisational and environmental context of social processes, especially in exploring new or emerging processes and phenomena (Yin 2003; Stake, 1995; Hartley, 2006). The case study method also enables the researcher to investigate overarching issues such as the location and history of the organisation under scrutiny. In view of the complexity of researching social enterprises and the scarcity of information on legal structures, a case study approach was selected as a suitably robust analytical model.

#### **4.9.1 Method of case study approach**

Within social science research there are ongoing debates on the significance of the use of single or multiple case study analysis. In the single case study approach the objective is to explain *how* and *why* a phenomenon occurs (Thomas et al, 1998). This is done through a detailed examination of the interrelationships in the internal operation of the case study. The use of multiple case studies enables the researcher to explore new areas and themes where there is very little theory available to explain a phenomenon (Kohn, 1997). The use of multiple case studies facilitates the process of replication, which allows a researcher to critically analyse themes across a number of case studies. When using a case study approach, the concern has always been to gain an insight into how the causal processes work in either one or a number of case studies (Thomas et al, 1998). A case study method makes it possible to investigate causality by enabling the researcher to develop an in-depth analysis of how some causal processes work out in either a single or number of case studies.

Due to the diversity in types and thematic activities of social enterprises, a multiple case study approach was considered appropriate for this investigation. Four case studies were selected as explained in Section 4.9.2 below. This approach allowed the researcher to present a balanced analysis while at the same time gaining a wider appreciation of how different types of legal structures influence social enterprises' activities. The focus was on the identification of the following key issues;

(a) Motivations behind social enterprises' choice of legal structure.

(b) Governance and operational challenges resulting from balancing social and economic objectives in a competitive economic environment.

These objectives entailed a data collection and analysis method in which the researcher would gather evidence from real life examples. The multiple case study approach was preferred in this investigation precisely for this reason and also because it facilitates the comparison of case study results to produce what Yin (1994) refers to as 'replication logic', a method of analysing themes across case studies to gain a deeper understanding of a phenomenon.

The next section focuses on how the case studies in this investigation were selected.

#### **4.9.2 Case study selection**

Selecting case studies for scrutiny has always generated debate among researchers. The selection process often raises issues of internal and external validity (Kohn, 1997). There is consensus however that case study based research is different from sampling research (Tellis, 1997). The process of case study selection needs to be carried out in a way that maximises learning. Therefore the selection of case studies for this investigation was based on the need to illustrate the diversity, representativeness, nature and character of the social enterprises under scrutiny (Pharaoh et al, 2004).

Given the diversity and complexity of the social enterprise sector, it was important to select case studies that maximise our knowledge of the area under study (Tellis, 1997). The objective therefore was to select case studies with different legal structures, but operating in more or less similar thematic activities. For example case studies 1 and 4, though operating under different legal structures are involved in delivering training, at different levels. Similarly, case studies 2 and 3, though differentiated by their type of legal structure, are involved in delivering environmental improvement interventions. One of the proponents of this type of case study selection technique is Kohn (1997). He argues that heterogeneity among case studies selected for scrutiny enhances generalisability.

The case study analysis therefore involved a comparative analysis of four case studies, two for each legal structure being investigated as shown below in Table 4.9. The two legal structures are company limited by guarantee (CLG) and company limited by shares (CLS). Two examples of the latter were selected from Sheffield since current knowledge and evidence from the mapping exercise indicated that such structures currently only exist in Sheffield. It is important to note that at the time of

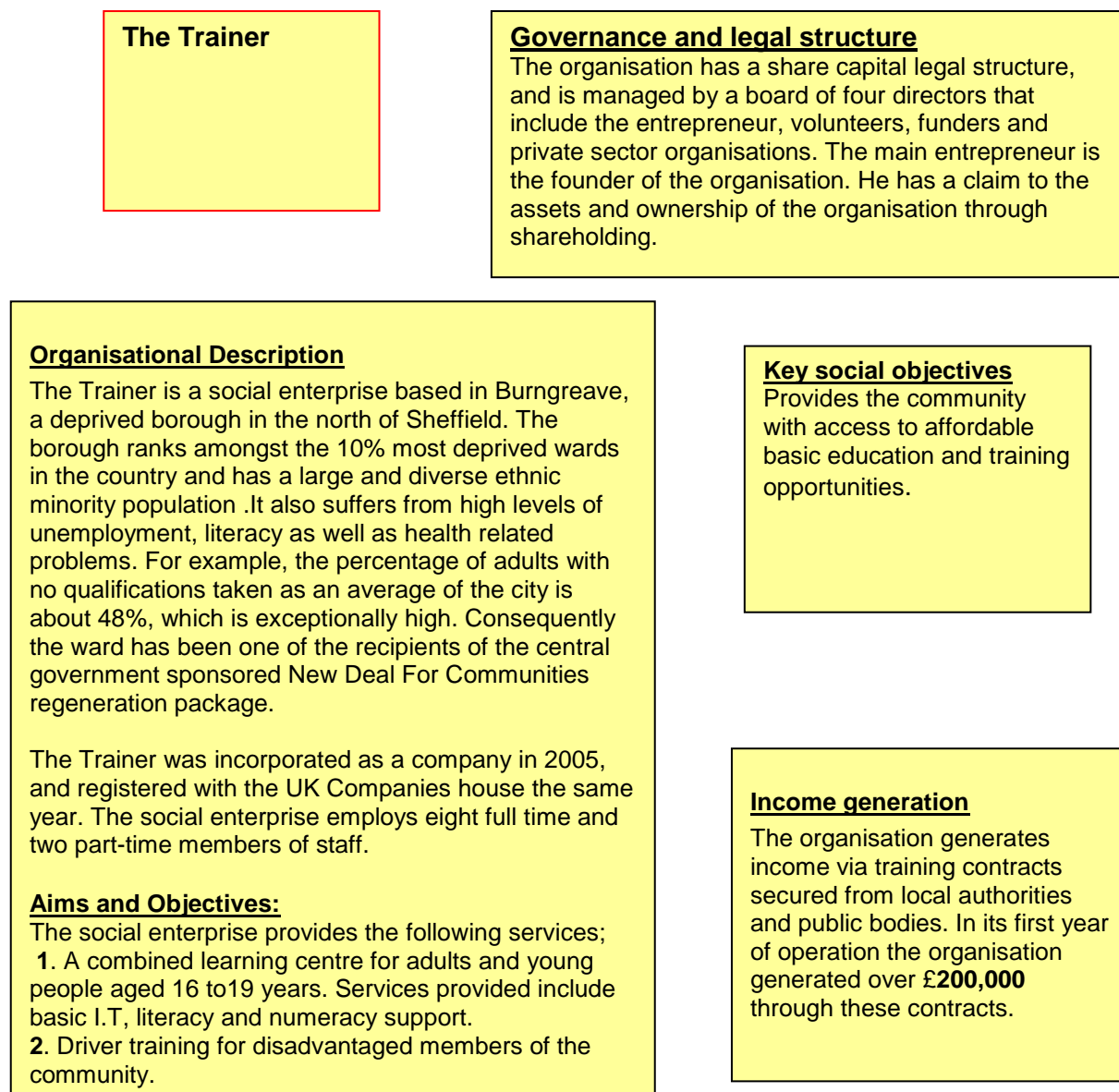
investigation, the Community Interest Company (CIC), which has a share capital variant, mentioned in Chapter 4, had just been unveiled and no social enterprises had yet adopted it. The share capital model under analysis in this study preceded the CIC and was developed and pioneered in Sheffield as explained in Chapter 3. Social enterprises with IPS cooperative legal structures were not considered despite this being a common structure for social economy organisations. There is already a large body of knowledge on cooperatives whose history can be traced back to the early nineteenth century as discussed in Chapter 2. Social enterprises with CLG legal status represent an area requiring further exploration to increase our knowledge on social enterprise development (Low, 2006).

**Table 4.9: Case studies under investigation**

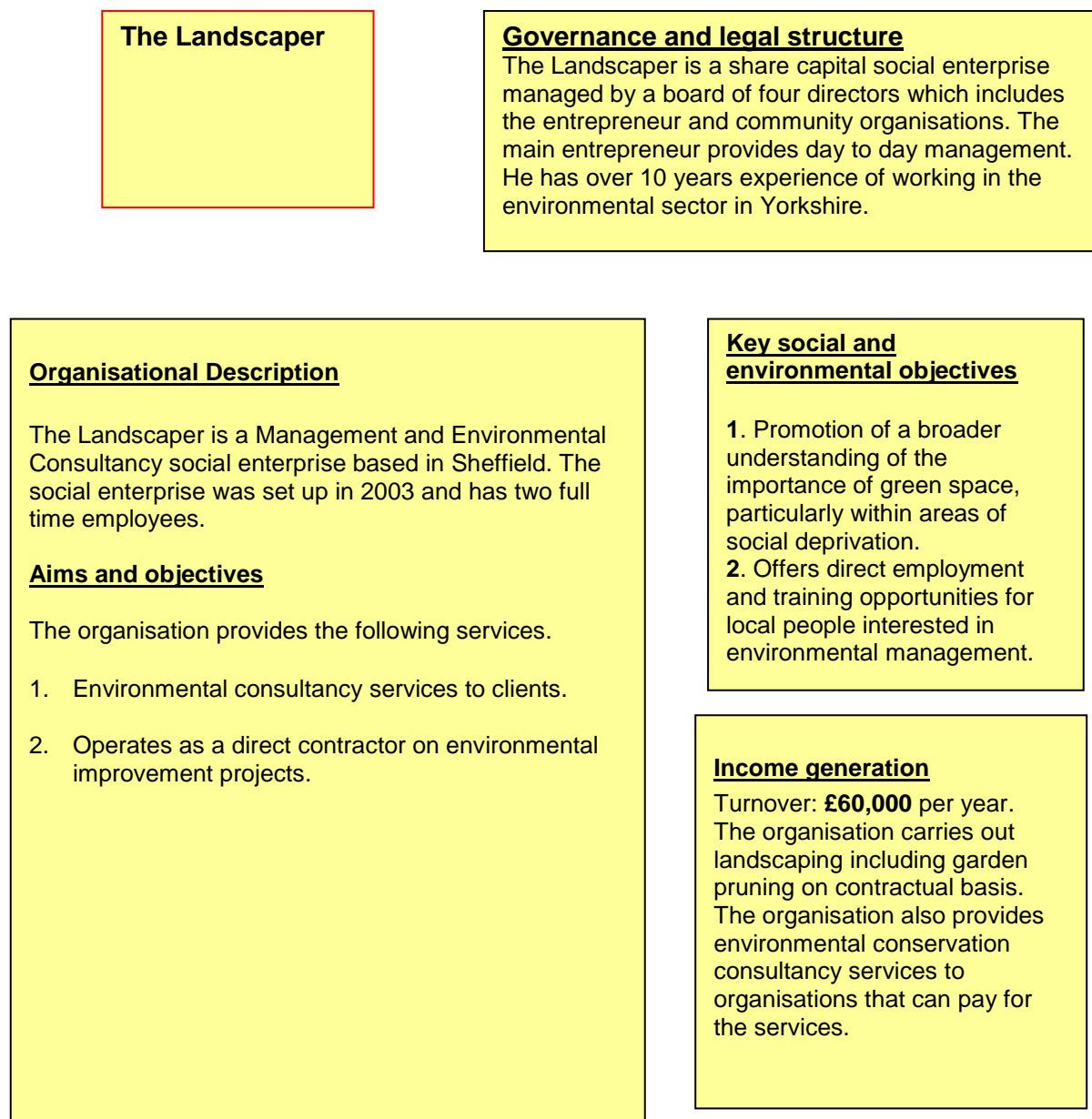
<b><i>Organisation</i></b>	<b><i>Type of legal structure</i></b>
The Trainer	Share capital (CLS)
The Landscaper	Share Capital (CLS)
The Cafe	Company Limited By Guarantee (CLG)
The Community Champion	Company Limited By Guarantee (CLG)

Figures 4.3 to 4.6 below provide descriptions of the selected case studies, showing their geographical location as well as the thematic activities they are involved in. The anonymity of the case studies has been protected and fictitious names used to identify them.

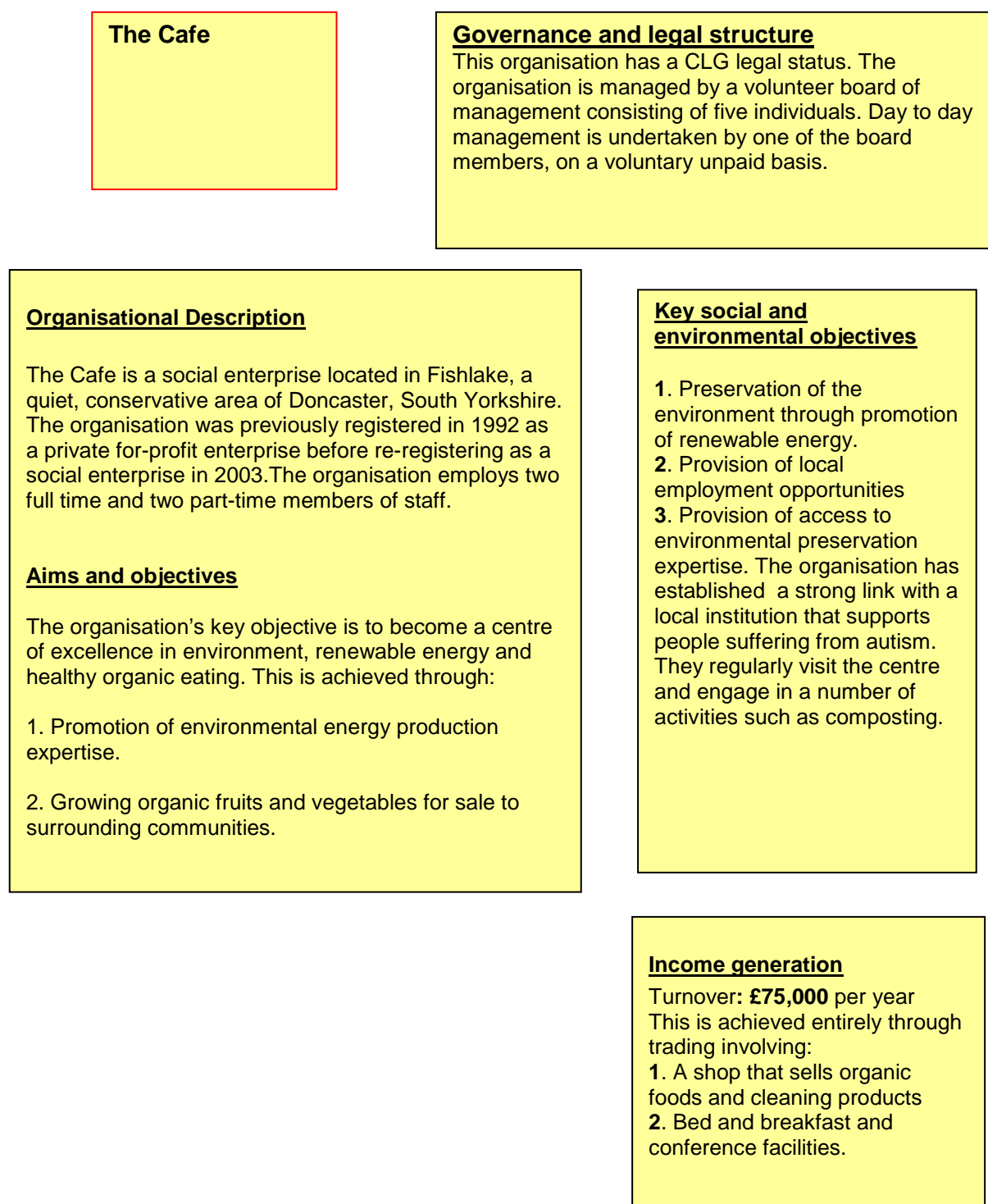
**Figure 4.3: The Trainer**



**Figure 4.4: The Landscaper**



**Figure 4.5: The Cafe**





**Figure 4.6: The Community Champion**

**The Community Champion**

**Governance and legal structure**

The Community Champion has a company limited by guarantee legal status with charitable status. It has a board of six directors led by the founder member who is the chairman of the organisation. The organisation is managed by a volunteer board of directors who provide both strategic and operational management.

**Organisational Description**

Case study 4 is a Doncaster based social enterprise that provides a supportive environment for people with disabilities or who are unemployed. The organisation was established in 1987 initially focussing on people recovering from serious illness who intended to get back to work. Its work later extended to local unemployed people who were interested in gaining training in arts and craft. The organisation has five part-time employees whose posts are funded externally.

**Aims and Objectives**

The organisation is a vehicle that local people can use to gain work experience before moving to future suitable employment. The services provided by case study 4 include:

1. Training in arts and crafts.
2. Handyman service for the elderly in Doncaster.

**Key social objectives**

Supporting disadvantaged members of the community with significant employment barriers to gain skills that can make them employable.

**Income generation**

Turnover: **£80,000** per year, based on current audited accounts.

There is a heavy focus on funding rather than generated income. Current income consists of grant funding.

Negligible amount of trading income earned through 'Home Services', a handyman service for the elderly in Doncaster.

The next section discusses how the data required for this investigation were collected in the case studies.

#### **4.9.3 Case study data collection**

It is not uncommon for researchers to use both quantitative and qualitative methods in case studies (Kohn, 1997; Alreck and Settle, 1995). Yin (1994a) argues that a case study approach requires a comprehensive and robust research strategy comprising a number of data collection methods. Such an approach generates richer data than would be obtained using a single data collection method. Therefore in this investigation, the case study approach involved the use of complementary data collection methods (Thomas et al 1998). The methods used in the case study analysis were as follows:

- **Qualitative research in the form of face to face interviews.**

Sadava and McCreary (1997) argue that qualitative or naturalistic research can be conducted in three ways namely, in-depth open-ended interviews, direct observation and review of the organisation. This study used a mixture of semi structured face-to-face open-ended interviews and direct observation. Much case study analysis involves the use of detailed interviews (Tellis, 1997; Thomas et al, 1998). One of the main advantages of such interviews is that the researcher can capture respondents' attitudes to and perceptions of a variety of issues (Bryman and Bell, 2003). A semi-structured interview or topic guide outlining the main issues under investigation was used and is attached as Appendix 4. This instrument enabled the researcher to include other themes that arose in the interviews without being constrained by a rigid approach (Saunders et al, 2009). This approach made it easier to discuss complex issues such as legal structures and their implications for the survival of the organisations under study. The researcher was also able to capture the opinions and feelings of respondents and how they interpreted their experiences in specific areas of interest (Graziano and Michael, 2004). When face-to-face interviews could not be undertaken or repeated, telephone interviews were conducted, as illustrated in Table 4.15 below. Appointments were made by phone or email with key informants prior to the interviews. Each interview lasted between one and three hours. Care was taken to ensure that respondents were not inconvenienced by long interviews. Probes, as Ramchander (2004) notes, are useful tools in clarifying concepts. The use of face-to-face interviews allowed the researcher to prompt responses from informants in a less structured way (Frissen and Punie, 1998). Consequently it was possible to gain a

deeper understanding of the respondents' perceptions on various issues affecting the social enterprises sector and their own organisations.

The researcher conducted four face to face interviews with key informants from the organisations. The case study selection, interviews and analysis took place between November 2006 and July 2007. Table 4.10 below shows the four case studies that were analysed and the key informants who were interviewed.

**Table 4.10: Schedule of case study interviews**

<u><b>Interviewee(s)</b></u>	<u><b>Interview dates</b></u>	<u><b>Length of interview</b></u>
<b>Case Study 1</b> (Sheffield)	1. Director and owner of organisation	1 <sup>st</sup> Interview 3/01/07 2 hours
	2. Manager of organisation	2 <sup>nd</sup> Interview- 29/01/07 2 hour
	3. Funder	9/02/07 1.5 hour
	4. Director	Follow-up telephone interviews from 1/02 and 09/02/07 1 hour
<b>Case study 2</b> (Sheffield)	1. Director and owner of organisation	1 <sup>st</sup> Interview 5/01/07 1.5 hours
	2. Funder	Follow up telephone interviews- 1/02/07 and 2/03/07 2 hours
<b>Case study 3</b> (Doncaster)	1. Manager	1 <sup>st</sup> Interview 10/01/07 2. hours
	2. Staff Member	18/1/2007 30 minutes
	3. Manager	2 <sup>nd</sup> telephone interview-7/02/07 40 minutes
	3. Funder	1/03/07 1 hour
<b>Case study 4</b> (Doncaster)	1. Chairman Manager Board members Two members of staff	1 <sup>st</sup> Interview 18/01/07 2 .5 hours
	2. Manager	Telephone interview-6/03/07 30 minutes
	3. Funder	18/01/07 30 minutes

Table 4.10 above shows that key informants included owners, senior board members and funders of each organisation, as well as staff members. 'Funders' means organisations providing financial assistance (whether structured as grants or loans) to the social enterprises under investigation. Due to the sensitivity of the issue, interviews with funders were conducted only once consent had been obtained from the key informants. The researcher also used his general knowledge of the funding landscape in the region to access information on various funding packages. This was then used to cross-check the information provided by informants as shown in Table 4.11 below.

Table 4.10 above shows that the researcher made several repeat visits to each case study to obtain information. It became clear that the first visits mainly served to establish rapport with key informants. This was important in ensuring that respondents provided information voluntarily rather than through coercion. An example of an interview is attached as Appendix 5. Initial interviews lasted for at least two hours and follow up interviews lasted at least thirty minutes. Care was also taken to avoid interviewee fatigue by spacing questions and ensuring that informants were relaxed and not under pressure to provide answers.

- ***Participant observation and focus group interview***

The interviews with key informants listed in Table 4.10 above took place at their premises, allowing the researcher to physically verify information such as address, actual existence of the organisation and other physical features such as buildings Tellis (1997). Through face to face interviews, the researcher was able to observe the gestures and body language of respondents. This was particularly useful in case study 4. Having arrived at the organisation's premises an hour early, the researcher was invited to a management committee meeting. There were five people present, comprising three management committee members, a member of staff and a business adviser from Doncaster CVS. The meeting covered a range of issues including administrative issues such as purchase of stationery and business plan preparation. It afforded the researcher an excellent opportunity to observe the body language and gestures of everyone present. The power and authority of the chairman, who is also the founder of the organisation, was evident during the

discussions. Whenever a question was asked those present would wait for him to provide a response before expressing their opinions.

This particular visit also allowed the researcher to conduct a focus group interview after the end of the management meeting. Rarely does a researcher get access to a number of key informants at the same time. Bryman (2001, p. 336) describes the focus group technique as an interviewing method that involves 'more than one, usually at least four interviewees'. Ghauri and Gronhaug (2005) state that focus groups take various forms such as focussed interviews, group interviews and group research. In this investigation, a group interview was conducted. The group being interviewed comprised three members of the management committee and two staff members. The focus group method provided an opportunity to evaluate how informants discussed specific issues and how they interacted within the group (Bryman, 2001). Using a semi-structured interview guide enabled the researcher to extract important information especially on the legal structure of the organisation and the process leading to its selection. For example the researcher asked each interviewee to independently write down why the organisation selected a company limited by guarantee legal structure with charitable status. The researcher was therefore able to get a good view of the impetus behind the organisation's legal structure.

#### **4.10 Archival research**

Documents (found data) are a rich source of information and an alternative to questionnaires, interviews or observation (Oates, 2006). A core component of this study was to undertake detailed archival document research to gain a deeper insight into the concept of social enterprise and the policy behind it. Heath (1997) considers archival research to be a key method of obtaining information on a phenomenon that has already occurred. Of course data that is in the public domain is usually easier to obtain than material that is confidential or sensitive (Oates, 2006). In addition, information that has been recorded will be largely original, thereby increasing validity through triangulation (Hair et al, 2007; Oates 2006). However, it may be difficult to access such data and the researcher has no control over the quality of what is available (Bryman and Bell, 2003; Hair et al, 2007). One of the advantages of using archival research in this investigation was that it permitted developments in social enterprises to be tracked from a historical to a contemporary perspective. It also allowed the researcher to analyse the implications of the development of social

enterprise as a concept for the prevailing government policy towards the sector. Tellis (1997) stresses the need for a researcher to be meticulous in determining the accuracy and origins of documents. Therefore various sources of archival data were interrogated. Key policy documents relating to the development of social enterprises in the UK in general and in South Yorkshire in particular were identified and analysed. (Appendix 6 provides a full list of the documents located and analysed). In order to ascertain how social enterprise policy was perceived and implemented at different levels the document search was split into two components, namely the political/national and the regional context.

#### **4.10. 1 National/ political context**

Chapter 1 described how central government was instrumental in driving forward the social enterprise agenda at national level when Labour came into power in 1997. It was therefore necessary to establish the political context of social enterprise development. Although the concept was embedded in government policy on social reform, this work seeks to discover how the concept evolved from a policy perspective. In addition it was important to find out if contemporary social enterprises are what the government expected them to be when the concept became popular in the late 90s. The researcher's first point of call was to analyse the Labour Party Archives. This was important to ascertain what the party had in mind when it came into power in 1997 and the reason the government immediately embraced the social enterprise theme. Therefore the documents listed below were critically analysed.

- ***Party Manifestos from 1997 to 2005***

The Labour Party manifestos were interrogated so as to gain understanding of the government's plans with regards to social enterprise. The focus of the analysis was on key policy issues of social reform and development and support for businesses. These issues provided an indication of the government's strategy on community development at the core of which lay the social enterprise concept.

- ***Parliamentary select and audit committee reports on social enterprises***

These reports, which included Hansard reviews, were analysed to explore how the social enterprise concept became embedded across the political spectrum in the UK.

It was also important to identify the government's future plans to enable social enterprises to survive independently of state support. Time was also taken to analyse the activities of Think Tanks such as the New Economics Foundation (NEF) and The Institute of Public Policy Research (IPPR) in order to understand their contribution to the development of the social enterprise concept. NEF commissioned a number of reports on social enterprises focussing on their potential to ameliorate deprivation and assist the state in welfare provision. These also included an evaluation of how social enterprises could increase their viability through embracing a more market orientated approach supported by suitable legal structures.

- ***UK Companies House Registry***

The researcher used UK Companies House to access publicly accessible financial documents of the four case studies under scrutiny (Oates, 2006). Accessing this information had three objectives. Firstly, it was helpful in cross checking the financial information provided by informants. Secondly, it was necessary to confirm that these organisations were legally registered. Thirdly, it allowed the researcher to identify and confirm the nature of the organisations' legal structures. The organisations' audited financial statements such as balance sheets, share allocation and profit and loss accounts filed at Companies House were analysed. The results of the financial analysis are discussed in Chapters 7 and 8.

#### ***4.10.2 Local context***

South Yorkshire, as described in Chapter 6, was left economically devastated after the collapse of the coal and steel industries in the 1980s (Thompson et al, 2000). The objective was to gain an understanding of the scale of socio-economic problems affecting the region and how social enterprises were being seen as a potential panacea. A review of existing literature on South Yorkshire as well as other sources of materials on social enterprises was undertaken. Visits were made to local newspaper archives as well as public records to obtain information on the history of South Yorkshire's economy. Other sources of information included the internet, grey literature (unpublished papers on various aspects of social enterprise), as well as academic resources (Hair et al, 2007). Sheffield Community Enterprise Development Unit (SCEDU), provided access to a variety of unpublished information on social enterprises that was relevant to the study. Information from social enterprise mapping

exercises in South Yorkshire, including unpublished information, was also systematically analysed to gain an insight into how social enterprises in the region have evolved.

- ***Visit to Local Regional Development Agency***

The researcher visited the Yorkshire and Humber Regional Development Agency's offices and website to collect information relating to social enterprises. This enabled the researcher to develop a regional perspective on social enterprise establishment and development. Sources of information included brochures and policy statements of the Regional Development Agency on the future of social enterprise within the region. Other sources of information included regional social enterprise strategic plans such as the 2004 Investment Plan for Social Enterprises in Yorkshire and the Humber. Reference to information obtained from these documents is made in Chapters 5 and 6.

- ***Minutes of board meetings***

The researcher managed to gain access to the internal management committee minutes for case studies 1 and 4. The purpose was to gain insight into some of the historic issues relevant to the organisations' operations (Tellis, 1997). The researcher also wanted to find out how the selection and adoption of the legal structure of the organisation was undertaken, particularly if there were any dissenting voices or alternative suggestions during the process.

- ***Memorandum and articles of association***

The researcher obtained copies of the memorandum and articles of association for each of the four organisations. Scrutiny of these governance documents identified the activities that these organisations could legally be involved in. They also showed the type of legal structure that had been adopted and the internal management processes and systems. The implications of the memorandum and articles of association for the organisations' operations are discussed in Chapters 6 and 7.



- ***Newspaper articles and websites***

Newspaper archives were visited to extract relevant information on the four case studies. For example, the researcher contacted the Star, which is the regional paper for South Yorkshire, and gained access to their archives. Here he was able to extract both historical and contemporary information on the case studies, particularly case studies 1, 3 and 4. The results of this archival search are discussed in Chapter 6. This information was also critical in establishing validity of the results of the investigation as shown in Table 4.11.

#### **4.11. Data analysis**

Kohn (1997) points out that in case study analysis it is inevitable that there will be more variables or themes revealed in the course of the analysis than anticipated at the beginning of it. This is precisely what happened in this investigation. Five key emerging themes were identified from the analysis of case studies. These are discussed and analysed in detail in Chapter 6. However, one of the themes (determinants of legal structure) had a further six sub-themes, making it difficult to employ traditional statistical methods of data analysis (Kohn, 1997). Tellis (1997 p, 11) argues that statistical robustness is 'not an absolute necessity in all case studies'. Therefore the method used to analyse the data was replication, which enabled the researcher to critically analyse each case study and manually identify the emerging themes. Comparisons were then made to ascertain if there was a similar pattern across all four case studies that could be generalised, a method recommended by Kohn (1997).

Qualitative data, due to its non-standardised and complex nature, is demanding and difficult to analyse (Saunders et al, 2009; Yin, 2003). Consideration was given to the use of computer aided qualitative data analysis software (CAQADS) packages such as Atlas-ti and NUD.IST to analyse the data. However, after initial trials, particularly with NUD.IST, the researcher concluded that little would be gained from their use, a view shared by Lofland and Lofland (1995). While the researcher was aware that the use of CAQADS can make analysis of qualitative data more efficient, a manual approach, though time consuming was deemed more appropriate. For example, it was difficult to accurately identify emerging themes using NUD.IST, because respondents used different terms to explain the same issue. In addition, the use of electronic qualitative data analysis software is not suitable for information emerging

from focus groups, a data collection method used in this investigation. Catterall and MacLaran (1997) argue that such software may not capture key information from informants. Through manual transcription of responses, the researcher was able to immerse himself in the data and was able to identify key themes emerging from the analysis. Hair et al (2007, p.295) support this approach, arguing that some 'intellectual examination' is still required by a researcher, even with the use of electronic data analysis software. The process undertaken in the investigation to analyse qualitative data is described below.

#### ***4.11.1 Analysis of case study qualitative data***

As discussed above, the greatest challenge faced by the researcher in the qualitative data analysis was the sheer amount of data that was generated. This data also contained information gleaned from observation of informants (Miles and Huberman, 1994; Delamont, 1992; Seidel and Kelle, 1995). Interviews of key informants were recorded and then transcribed, a method recommended by Miles and Huberman (1994) for manual qualitative data analysis. The semi-structured interview guide attached as Appendix 4 was used to collect relevant data. The systematic manual data analysis method used by the researcher is consistent with the work of researchers such as Kohn (1997), Miles and Huberman (1994), Bryman and Bell (2003), Cassell and Symon (2004) and Basit (2003), amongst others.

The method used in this investigation is largely based on the above authors' approach to manual thematic data analysis. The first step was to collect the data using the instruments discussed above. The next step was to transcribe the recordings of the interviews. This involved re-visiting the research objectives outlined in Chapter 1 and the theoretical framework underpinning this investigation, discussed in Chapter 3. This was necessary to assist the researcher to retrieve and organise the data needed to answer the research questions (Basit, 2003). The researcher then used a large piece of paper with five columns, one for each of the four case studies and one for key phrases and emerging themes. Codes were then generated and assigned to key words and phrases relevant to the research questions. The key phrases or variables were derived from the research questions and the literature review (Lofland, 1971; Bogdan and Bilken, 1982). The use of coding in making sense of qualitative data is a common practice (Miles and Huberman, 1994; Agar, 1980; Bryman and Bell, 2003; Basit, 2003; Cassell and Symon, 2004). For example, 'type of legal structure' which is related to the first research question, could prompt

answers such as company limited by guarantee, or co-operative model. These were assigned codes CLG and IPS respectively. Coding therefore made it possible to identify relevant information or construct themes relevant to a specific research question (Bryman and Bell, 2003).

The researcher then examined each transcript, highlighting any words, sentences, illuminative quotes or phrases that related to a specific theme, such as 'type of legal structure' or 'determinants of legal structure'. Further analysis of these highlighted excerpts revealed additional or sub themes, thereby enabling the researcher to organise the data into coherent categories that were interlinked (Agar, 1980; Taylor-Powell and Renner, 2003). For example, the theme 'determinants of legal structure' was revealed to have additional subthemes such as policy environment (code PE) and access to funding (code AF). Further useful themes that were identified this way included 'mission of social enterprise', 'sources of funding' for social enterprise and 'governance' of social enterprise. This method therefore facilitated cross case analysis by 'surfacing common themes and directional processes' (Miles and Huberman, 1994 p.69), a process that Tesch (1990) describes as data distillation.

The frequency of occurrence of each phrase, word or sentence was recorded under each case study's transcript. When these frequencies were compiled at the end of the analysis, they revealed a pattern of themes or an anatomic framework of emerging data (Kaplan, 1964; Basit, 2003; Chen and Meindl, 1991).

The data analysis process is shown diagrammatically below in Figure 4.7

**Figure 4.7: Data analysis process**

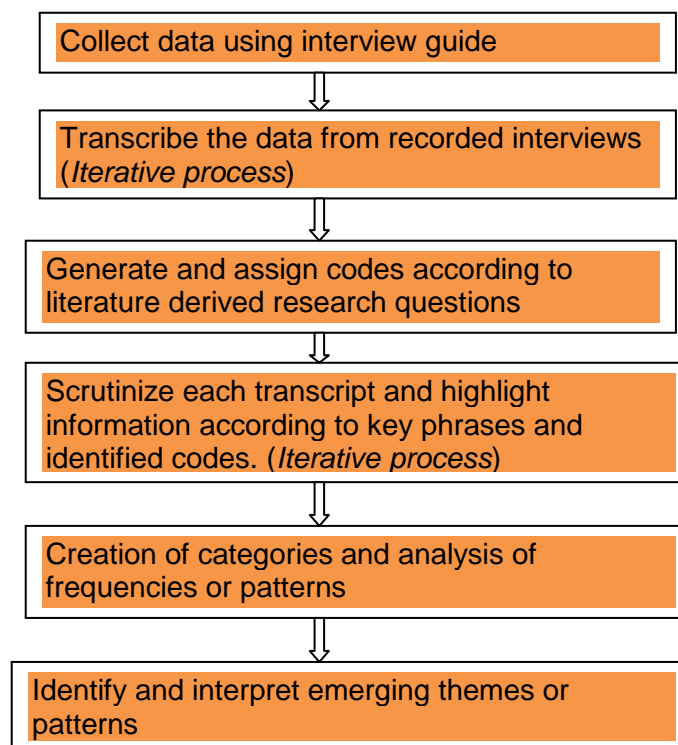


Figure 4.7 based on Miles and Huberman (1994), Bryman and Bell (2003), Cassell and Symon (2004) and Basit (2003)

The process used to analyse the qualitative data was therefore an inductive approach, focussing on textual analysis and then developing themes to assist the researcher in addressing the research questions (Bryman and Bell, 2003; Yin, 2003; Straus and Corbin, 2008).

#### **4.11.2 Analysis of data from documents**

Archival research was a key component of the research design in this investigation. This included scrutiny of various documents as illustrated in Section 4.9. These included magazine and newspaper articles of entrepreneurs and their respective organisations and financial reports of the organisations under scrutiny. The method used to analyse the data emanating from documents, particularly newspaper articles and other published documents, was qualitative content analysis, an approach associated with the work of Dougherty and Kunda (1990) and Chen and Meindl (1991). This involved identifying underlying themes in these documents that were related to the research questions. This method refers particularly to quotations or statements the researcher was able to identify and extract in line with the research

objectives (Turner, 1983). For example, scrutinising memorandum and articles of the case study organisations revealed information on the nature and type of their legal structures and what they allowed them to do, information essential for answering the research questions. The researcher was aware of other document analysis techniques such as semiotics and hermeneutics but these were considered unsuitable for this investigation. Semiotics focuses on the analysis of symbols people use in their daily life as well as making sense of hidden meanings in texts under study. Hermeneutics focuses on the broader social and historical context of a text under scrutiny in order to understand it from the perspective of the person who has created it (Bryman and Bell, 2003).

#### **4.12 Case study quality**

Use of the case study approach has always raised issues about the reliability and validity of findings (Kohn, 1997). A small number of case studies can potentially compromise the reliability of the findings (Soy, 1996). On the other hand, the analysis of even a few case studies generates a lot of information and there is constant danger of data overload. Yin (1994a) suggests the researcher should demonstrate convergence of evidence as well as divergence from a number of sources. As shown in Table 4.11 below, the researcher used a number of techniques to ensure that evidence collection was systematic. Critics of the case study approach have also pointed out that researchers can easily find a case study that provides the evidence that the researcher wants to put across (Thomas et al, 1998). Ethical issues can therefore arise, necessitating triangulation to confirm the validity, reliability and believability of data collected using this method (Tellis, 1997; Yin, 1994b).

##### ***4.12.1 Mixed methods and triangulation***

Stake (1995) describes triangulation as a protocol that researchers utilise to achieve accuracy and also to produce alternative explanations for phenomena. Therefore, triangulation is important in strengthening the validity of the findings through establishing agreement using independent measures (Miles & Huberman, 1994; Schwartz-Shea, 2006). Reinharz (1992) considers triangulation to increase the likelihood of obtaining scientific credibility and research utility (p.197). Woodhouse (1998) and Thomas et al (1998) suggest that triangulation and documentation are key elements of achieving rigour in an investigation involving multiple case studies

and multiple sources of information. To achieve rigour, a researcher needs to provide sufficient evidence to justify the conclusions that are being drawn from the research.

Despite being distinctly different in nature, qualitative and quantitative methods can be used to supplement each other to achieve a well rounded analysis (Jick, 1979). Researchers such as Creswell and Clark (2007) and Saunders et al (2009) agree, arguing that combining quantitative and qualitative datasets provides a better understanding of the phenomenon under scrutiny than if these datasets were used on their own. In this investigation qualitative information from case study analysis was triangulated with information from quantitative surveys. For example, tests of association of emerging themes from case study analysis were made with data from questionnaire returns to achieve internal validity through statistical cross tabulations, or cross -case pattern matching (Riege, 2003). The researcher utilised the robust model shown in Table 4.11 to collect evidence and provide a strong platform for triangulation. The type of triangulation used to achieve validity is what Denzin (1978) calls 'methodological triangulation'. This technique is common in social sciences research and utilises more than one method of collecting evidence. Table 4.11 shows the tests and techniques for establishing validity and reliability used in this investigation.

**Table 4.11: Tests and techniques for establishing validity**

<i>Key stages in case study analysis</i>	<i>Techniques of analysis used</i>	<i>Objective of case study test</i>
<b>Data collection</b>	<p><b>1. Multiple sources of data identified and interrogated (Yin ,1994a)</b></p> <ul style="list-style-type: none"> <li>• Interviews with entrepreneurs leading the four social enterprises under investigation.</li> <li>• Direct observation.</li> <li>• Interviews of members of boards of directors of social enterprises.</li> <li>• Interviews of key informants from social enterprises.</li> <li>• Interviews of key informants from social enterprise support organisations.</li> <li>• Analysis of internal company documents such minutes of board meetings, strategy documents and advertising materials.</li> <li>• Analysis of financial information held by the Companies House UK.</li> <li>• Analysis of information from quantitative surveys.</li> <li>• Archival research.</li> </ul> <p><b>2. Gathering and establishing chain of evidence(Yin ,1994a &amp;b)</b></p> <p>All interviews with key informants were recorded and transcribed using an interview guide. Supporting evidence, such as newspaper articles and financial information was analysed and cross-checked with data already obtained from informants.</p>	<b><u>Construct validity</u></b>
<b><u>Data collection</u></b>	A case-study protocol was developed involving in-depth analysis of selected case studies via semi structured interviews using an interview guide.	<b><u>Reliability</u></b>
<b><u>Analysis of data</u></b>	<p>The data was manually analysed and key emerging themes identified.</p> <p>Identified and tested associations of qualitative data emerging from case study interviews with data from quantitative analysis already undertaken. This was done through cross tabulations.</p>	<b><u>Internal validity</u></b>
<b><u>Research design</u></b>	The research design involved a mixed-method approach incorporating quantitative and qualitative approaches. The theory in multiple case study analysis was also utilised.	<b><u>External validity</u></b>

Table 4.11: Adapted from Yin (2004a) and Yin (2004b)

#### ***(a) Construct validity***

Evidence from the multiple sources shown above was analysed in the context of the research questions outlined in Chapter 1 (Cowley et al, 1999). Appendix 5 provides a breakdown of the sources of evidence collected for each case study. In addition the researcher ensured that there was consistency in the design and application of the instruments used to collect data (Kohn, 1997). This approach facilitated the process of corroborating information such as archival data that had already been collected. It is evident that the data collection was extensive and included both internal and external information on what influenced how these organisations operated.

#### **4.13. Summary of data collection techniques**

Table 4.12 below summarises the data collection methods used in this investigation to address the research questions.



**Table 4.12: Summary of data collection techniques used in the investigation**

<i>Research question</i>	<i>Data required</i>	<i>Method of data collection used</i>
<b>(A) Social Enterprises</b>		
1. Investigate different types of legal structures of social enterprises in South Yorkshire	Social enterprise population and location	<ul style="list-style-type: none"> <li>• Consultation of data bases of sub regional support organisations</li> <li>• Quantitative techniques structured postal questionnaires (with provision for qualitative or functionalist paradigm)</li> <li>• Postal questionnaires</li> </ul>
2 Identify and critically analyse key determinants of legal structures of social enterprises	Operational social enterprises and key legal structure drivers	<ul style="list-style-type: none"> <li>• In depth case study method comprising archival data, quantitative and qualitative techniques</li> </ul>
3. Investigate influence of type of legal structure on outcomes of social enterprises	Internal financial management systems and organisational design	<ul style="list-style-type: none"> <li>• In depth case study method comprising archival data and qualitative techniques</li> </ul>
<b>(B) Social enterprise support organisation</b>		
Types and distribution of support infrastructure for social enterprises	Number of national and sub-regional support organisations and location	<ul style="list-style-type: none"> <li>• Archival research</li> <li>• Document analysis/archival research</li> </ul>
Characteristics of support organisations	Nature and criteria of support	<ul style="list-style-type: none"> <li>• Quantitative and qualitative techniques</li> </ul>
	Individual perceptions and views	<ul style="list-style-type: none"> <li>• Semi-structured interview guide</li> <li>• Open ended interviews</li> <li>• Direct observations</li> </ul>
	Due diligence	<ul style="list-style-type: none"> <li>• Document analysis</li> </ul>

Table 4.12 above shows that this investigation employed a multi-method approach to gathering the evidence required to answer the research questions. The complexity of researching social enterprise is reflected by the multiplicity of the data collection methods.

#### **4.14 Ethical considerations and validity**

One of the key ethical guidelines in research concerns information dissemination and protecting the identity of respondents (McNamara, 1994; Hair et al, 2007; SRI, 2002). In this study all informants were made aware of confidentiality issues and assured

that no information would directly identify a particular informant unless consent was given. It was also considered ethical to ensure potential informants were aware of the reasons behind the study and why their participation was desirable. This was also important in improving response rates (McNamara, 1994).

Ensuring the validity of data is another key consideration in research. It involves ensuring that the process used to gather the required data is efficient and the results are reliable (Welman and Kruger, 2001). In this study, a number of methods were employed to achieve this. Multiple sources of data and triangulation were used to ensure the quality of findings as discussed in Section 4.12.6. The validity of data was enhanced by the emphasis on confidentiality and anonymity, with regards to information provided by informants. Appropriate literature on research design and methodology in the social economy was consulted to ensure the researcher's cognisance of critical issues regarding research in the sector. University-run workshops on data collection methods were attended to consolidate the researcher's knowledge of social science research. In order to maximise data validity, it is important to ensure that the research instruments are appropriate and can assist the researcher in analysing and interpreting the data (Cooper and Emory, 1995). Therefore, all research instruments used in the study had coding systems. These are critical in the organisation and classification of data during analysis (Saunders et al, 2009). Once the objectives of the study had been determined and the instruments justified, ethical approval was obtained from the university before commencing the study (Sadava and McCreary, 1997).

#### **4.15 Constraints and challenges faced**

In the course of carrying out any piece of research, it is normal to encounter challenges or obstacles in accessing data (Hair et al, 2007). The challenges faced by the researcher in this particular study are outlined below. They have been split into three components according to whether they occurred during the questionnaire survey, the support organisation interviews or the case study analysis.

##### ***Postal questionnaire survey***

**(a)** Some of the informants who completed questionnaires were junior operational staff that did not have adequate knowledge of the activities of the organisations they represented. Consequently there were some reservations about the accuracy of the

information provided (Denscombe, 2003). However the number of such informants was very low and any negative impact on the quality of findings was not significant.

**(b)** A few respondents would not divulge all the information requested because they felt that it was confidential. This included sensitive issues such as turnover or the names of organisations approached for funding or support. When respondents wrote their phone numbers on the questionnaire, the researcher made follow-up phone calls. A significant amount of extra useful information was collected in that way.

### ***Support organisations' interviews***

The main problem here was the time taken to contact key informants. Several organisations had gatekeepers whose job seemed to be to frustrate the researcher. Contacting these organisations was a difficult task, especially The Office of the Third Sector and The Social Enterprise Coalition which, incidentally, are key drivers of the social enterprise agenda. Both these organisations periodically insisted that they could not field officers for face to face interviews due to pressure of work and shortage of staff. Innovative attempts to make contact included sending an email to a key informant identified from the organisation's website, then phoning the informant to check if they had received the email. Such methods enabled the researcher to then carry out a telephone interview using a semi structured research guide. Another problem associated with interviewing support organisations was that the fieldwork coincided with local government elections. Therefore it was difficult to pin down officials for interview.

### ***Case study interviews***

The problems encountered during the case study interviews mainly involved logistical problems. Interviews involved travelling to informants' premises during working hours. Luckily, the then employers of the researcher, (SCEDU) generously allowed him to do so, and even met mileage expenses.

## **4.16 Chapter summary**

This investigation made use of a mixed-method research methodology to gather the evidence required to address the research questions. These methods were quantitative, qualitative, archival, direct observation and case study approaches. The

case study approach allowed the researcher to gather and analyse data from informants in their natural setting. The use of a mixed-method approach, given our knowledge of research methodologies previously used in researching social enterprise, was innovative. This method is what Creswell (2003) referred to as a sequential transformative data analysis strategy. By using this method, the researcher was able to construct a robust argument regarding the patterns and processes of social enterprises' development in South Yorkshire, a feat which other studies have so far failed to accomplish. Significantly the methodology enabled the researcher to triangulate evidence as well as cross-check information to ensure that the findings were valid. The methodological lessons gained from undertaking the investigation, lessons which are crucial for future research in this area, are reflected in greater detail in the concluding chapter of this thesis.

The next chapter discusses the context of social enterprise development, focussing on the UK and the South Yorkshire region, which is the location of this research.

## **CHAPTER 5: SOCIAL ENTERPRISES IN SOUTH YORKSHIRE: CONTEXT**

### **5.1 Introduction**

In Chapter 2, it was argued that understanding the socio-economic context is essential in establishing the nature and form of social enterprise development. This is for two reasons. Firstly, understanding the historicity of the social economy makes it possible to understand present dynamics and the extent to which the past has shaped the phenomenon. Secondly, since this work includes case studies, it is important to understand and situate the case work within the broader space of the economy. In pursuit of this, the chapter provides the contextual background of social enterprises in South Yorkshire, with data drawn mostly from secondary sources. This data is necessary to address the second and third research questions, outlined in Chapter 1. The focus of this chapter is therefore to present the socio-economic context of social enterprises in South Yorkshire using preliminary data from quantitative research undertaken in this study. The chapter is divided into three parts. The first part provides the contextual background of social enterprise in the UK. The second focuses on the geographical and historical socio economic context of the South Yorkshire region. The last draws out some key elements of this contextual analysis that emerge from the discussion and are central to understanding the work that follows.

Understanding the UK context of social enterprise is essential in understanding the origins of the government's thinking on social enterprises and how this has influenced their development in South Yorkshire. In addition, it is important to set the geographical context of the investigation. The next section therefore looks at the nature of contemporary social enterprises in the UK.

### **5.2 Nature of contemporary social enterprises in the United Kingdom**

While the use of the term social economy might be relatively recent, Conaty and McGeehan (2000) argue that the history of social enterprises is much longer than that of the corporate sector in the UK. Historically they have been part of the organisational landscape of enterprises in the country, dating back to the eighteenth

century mutual societies, cooperatives and settlement movements (BRASS, 2004; BASSAC, 2002b). The history of cooperatives and other community organisations spans centuries but social enterprises have become prominent over the past twenty years (Peattie and Morley, 2008). There are about 62,000 social enterprises in the UK, with a combined turnover of £27 billion per year. They constitute 5% of the UK national business base, making the sector as a whole larger than the agricultural sector (Jones 2010). The social enterprise sector is growing, employing about 1.3 million people (3.4% of the UK working population) (Filou, 2008). The third sector as a whole contributes nearly £9 billion a year to the UK economy (PriceWaterhouse Coopers, 2009). The growth of social enterprise is expected to continue as 5.8 % of the UK working population is engaged in some form of early stage entrepreneurship and at least 230,000 of them are keen to start a business with social objectives (Filou, 2008). This development is congruent with some of the government's objectives of reforming the welfare system, such as tackling the dependency culture (The Economist, 2008). Their main objective is to encourage people to move from welfare to work, with promotion of self employment through enterprise high on the agenda (West, 2004). The UK has a vibrant social enterprise sector with some of the best known being The Big Issue, which addresses homelessness through enterprise, Jamie Oliver's 15, giving disadvantaged young people a chance to learn a trade and Ealing Community Transport which provides innovative solutions to community transport problems and has grown and diversified into other activities.

Social enterprise continues to be a national strategy, central to the government's policy of tackling exclusion and deprivation (Po-Hi, 2003). The Labour government, before being ousted by the Conservative/Liberal Democrat coalition, unveiled various plans to make the sector financially self sufficient and economically viable. This included a commitment to provide the necessary technical and financial support packages (HM Treasury, 2006). These developments were evidence that the government viewed globalisation as an immutable reality and that its economic policy formulation was driven by the need to adjust and adapt, accepting the primacy of markets over politics (Clift, 2000). This policy has been continued by the new coalition government with their promotion of the 'Big Society'. This policy thrust regards social enterprise as a mechanism to tackle deprivation and exclusion through sustainable enterprise activities. They are keen to transfer ownership and management of local assets to social enterprises (Schwartz, 2010). The success of this strategy, however, is threatened by the current severe public spending cuts announced by the same government under its Comprehensive Spending Review

Programme (Hampson, 2010). Social enterprise support organisations fear that these cuts will force public sector organisations to transfer assets to the private sector rather than to social enterprise as they streamline their operations. There is an argument therefore that transfer of assets should be 'locked' in to social enterprises to enable them to continue delivering public services (Jones, 2010).

The next section discusses and analyses the challenges facing contemporary social enterprises in the UK and the strategies they are taking to remain viable in view of the reduction of institutional financial state support.

### **5.3 Challenges facing contemporary social enterprise in the UK**

Despite the popularity and growth of social enterprise in the UK, the sector still faces significant challenges (DTI, 2004; Alter, 2006; Bank of England, 2003; Martin and Thompson, 2010). Buttenheim (2002) argues that merely supporting a good cause does not guarantee funding or generate income (Buttenheim, 2002). It has also become clear that pervasiveness of social problems cannot be adequately addressed by philanthropy and state funding (Tropman Report 2003; Edwards, 2008). In addition, globalisation, scarcity of resources, declining philanthropic support, increasing competition and, recently, the economic recession are pushing social enterprises to search for new ways to augment their budgets (CCSE, 2001; Heaney, 2010). This requires a review of social enterprises' legal and institutional capacity to extract the resources necessary to achieve economic sustainability (Foster and Bradach, 1994; Conaty and McGeehan, 2000; Cox, 2000; Etchart and Davis, 2003).

#### ***5.3.1 Achieving financial sustainability***

Achieving 'financial sustainability' has always been a thorny issue within the social economy and UK social enterprises are no exception (Barriaux, 2006; Bank of England, 2003). The term is a catch all phrase packed with a wide variety of ideas and conflicting perceptions (Eade and Williams, 1995; Holdren et al, 1995). In the commercial world the term implies that the core purpose of business is to generate profits for share holders and to sustain operations and growth (Dyllick and Hockerts, 2002; Friedman, 1958). For social enterprise, this translates as successfully achieving their economic and social objectives. Following the reduction of institutional financial support, there is consensus that the sector needs to generate more income from trading activities or access capital from sources beyond the social

economy as Figure 5.1 below shows (Heaney, 2010; Grenier, 2003; Case, 2005; Conaty and McGeehan, 2000; Doherty et al, 2009). By being more entrepreneurial, they can build their capacity to be financially self reliant. A renewed social enterprise sector with the ability to attract non-traditional funding such as private sector resources is necessary if the sector is to grow (Conaty and McGeehan, 2000). The ability to interact with stakeholders outside the social economy becomes a significant factor of success and, contrary to how it has been viewed in the past, the private sector is now a key stakeholder. It is an increasingly important source of resources and technical expertise that can help social enterprises increase their capacity to deliver value (Barker, 2002b). As discussed in Chapter 2, the main challenge has been making social enterprises attractive to private investors, particularly given the lack of suitable infrastructure to facilitate this collaboration (Heaney, 2010). Social enterprises require the capacity and resources (human and financial) to make their interaction with organisations beyond the social economy financially rewarding (McGee et al, 2005; Brown, 2007; Richter, 1992).

**Figure 5.1: The Locus of Social Enterprise**

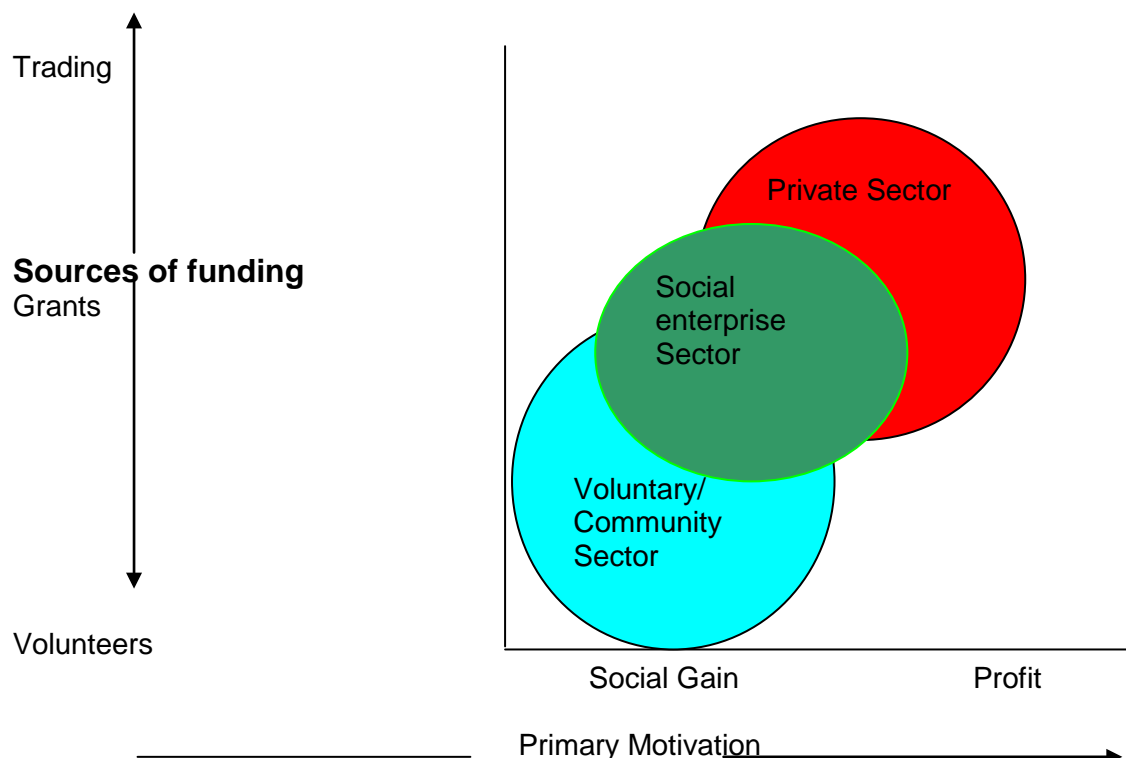


Figure 5.1: MSEI, First Interim Evaluation, Amion Consulting (2001)

### **5.3.2 Access to funding and investments**



Undercapitalisation is a chronic problem affecting the development and sustainability of contemporary social enterprises in the UK (Alter, 2004; LRS, 2002). Such organisations require different forms of investment at different stages of their development (Emerson, 2000). They are usually funded by a mixture of grant packages and trading income (Grenier, 2003) as discussed in Chapter 2. As Chapter 1 noted, a number of traditional grant support programmes have come to an end in the UK, forcing social enterprises to look for alternative funding sources (Arradon and Wyler, 2008). The decrease in public funding such as the Single Regeneration Budget (SRB) and European Structural Fund (ESF), which used to be the main source of finance for UK social enterprises, has caused concern over the sustainability of social enterprises and their interventions (Johnson, 2000; Flockhart, 2005; Heaney, 2010). In a survey undertaken within the voluntary sector by the Directory of Social Change (DSC) in the UK, 65% of respondents stated that it is now more difficult for social enterprises to mobilise financial resources because of these changes (DSC, 2006). In addition, contemporary social enterprises face even greater threats to their resource mobilisation strategies, given the current financial crisis and cuts in public spending, the most dramatic since the 1970s (Dearden-Phillips, 2009).

Analysis of the UK context of social enterprise highlights the following issues:

1. The end of European grant financial assistance programmes for social enterprises left a majority of these organisations undercapitalised and unable to continue with their activities. Development of viable trading operations became a realistic alternative to generate surpluses to support their objectives. The government is therefore keen to support social enterprises so that they become self reliant, viable businesses that contribute to the mainstream economy. In that way they will become less reliant on institutional support. The current coalition government's intention to offload public assets to social enterprises is evidence of this.
2. Social enterprise in the UK is facing significant challenges to remain viable following the onset of the economic recession and the subsequent cuts in spending. These organisations are now competing with the private sector to deliver public contracts, markets which had been previously ring-fenced for social enterprises. This exposure has highlighted operational challenges such as suitable frameworks to attract investments.

Having discussed and analysed the national context of UK social enterprises, the next section focuses specifically on South Yorkshire. The South Yorkshire context is important because firstly, it is the focus of this investigation and secondly, it is necessary to situate social enterprise within the regional political economy of South Yorkshire. Figure 5.2 below situates South Yorkshire and shows its constituent boroughs.

**Figure 5.2: Map of South Yorkshire**



Figure 5.2: Pictures of England.com (2001-2009) and South Yorkshire Investment Fund (2009)

## **5.4 The geography of South Yorkshire**

The South Yorkshire region, formally established in 1979, comprises the four unitary boroughs of Sheffield, Rotherham, Barnsley and Doncaster. Barnsley, Doncaster and Rotherham are also referred to as the coalfield areas of South Yorkshire, due to their coal mining history. South Yorkshire lies roughly in the centre of the United Kingdom (South Yorkshire Partnership, 2004) and about 1,267,288 people currently live there. The region covers an area of approximately 1,560 sq km (National Statistics, 2003). Rotherham, which lies between Sheffield and Doncaster, is a rapidly developing borough, with strong labour and market links, while Barnsley, which lies to the north, is a significant market town (Rotherham Overview, 2006; Yorkshire and Humber Plan, 2005). Sheffield is the largest of the unitary authorities that make up South Yorkshire and is the main economic centre of the region (Yorkshire and Humber Plan, 2005). In fact, Yorkshire Forward, the Government Office for Yorkshire and the Humber, in its Regional Economic strategy 2003-12 paper, identified Sheffield as the 'key driver of economic growth in South Yorkshire'. The city also contains the most deprived communities in Yorkshire (Sheffield City Council, 2003). Doncaster, where a new airport, (Robin Hood International Airport) has recently been commissioned, is poised to become the transport and logistical centre of the region.

South Yorkshire is located on the main 'North to South and Trans Pennine East – West transport corridor' (South Yorkshire Partnership, 2004). While there are good north – south rail and road links, there is a need to improve the other transport links within the region. Most of the transport related problems emanate from the region's transition from a predominantly heavy industrial economy to one which is much more mixed (Yorkshire and Humber Plan, 2005). The region contributes 21.7% of Yorkshire and the Humber Gross Value Added (GVA). It has above average unemployment with 25.7% of the county's population of working age but 26.8% of the county's unemployed (South Yorkshire Partnership, 2004). According to the 1998 Price Waterhouse Coopers report, the region faces an exceptionally difficult set of economic challenges (South Yorkshire Partnership, 2004). Consequently, South Yorkshire has profound weaknesses, reflected by very high levels of deprivation. It is therefore not surprising that recent statistics indicate rising crime figures in the region, particularly gun crime which has risen by 40% (Yorkshire Evening Post, 2006).

Two key issues are worth noting from the above. First is that the region's geographical location away from the core urban conurbation of the UK gives it a distinct economic disadvantage. Secondly, the decline of the region's industrial base of steel manufacturing and coal mining resulted in particularly challenging socio-economic conditions (PriceWaterhouse Coopers, 1998). These challenges are further discussed in the next section.

### **5.5 Economic history and business context in South Yorkshire**

The South Yorkshire region has over 35,720 businesses, with an economically active population of 586,000 in 2003 (National Statistics, 2003; Yorkshire Forward, 2005). Historically, the economy of South Yorkshire was primarily industrial and this dates back to the nineteenth century industrial revolution with coal mining and steel production being the mainstay of the economy (Birch, 2006). The region's economy developed as a dual economy comprising agriculture and heavy industry although coal and steel became dominant (Hey, 1969). At its peak in 1971 coal and steel employed approximately 187,000 people, which represented a quarter of local jobs, but by 1996 60% of these jobs had been lost (Yorkshire and Humber Plan, 2005; IdeasSmiths, 2004). The economic upheavals that plagued the entire region in the early 1980s explain this scenario. The accelerated closures of steel industries and coalmines in South Yorkshire resulted in massive job losses and devastated entire towns (Thompson et al, 2000). Beatty et al (2005) note that by the end of 2004, a further 65,000 jobs had been lost in South Yorkshire. These developments reduced the number of collieries to eight from a peak of 211 in 1981. This in turn created a plethora of socio-economic problems for people across the region (Objective 1, 2004). For example thousands of laid off miners and steel workers needed retraining (Murray et al, 2005). In addition to high levels of unemployment, the economic downturn also resulted in many families requiring welfare support. These developments are central to the socio-economic issues affecting South Yorkshire.

Despite some encouraging signs of economic recovery in 2000, GDP and income levels are still low compared to the EU average (South Yorkshire Partnership, 2004; Ideasmith Consulting Partnership, 2004). Table 5.1 below shows the economic performance of the region based on GDP from 1999, when European financial assistance commenced, to 2010.

**Table 5.1:** South Yorkshire economic performance based on GDP

<i>Period</i>	<i>GDP as % of EU Average</i>
1999	74.4
1999-2001	77.1
2001-2004	84.6
2004-2009	79.1

Table 5.1: Based on Objective 1 (2004) and Yorkshire Forward (2010) economic reviews

There was a marked increase in GD levels between 1999 and 2004 as Table 5.1 above shows. But this was followed by a sharp contraction of around 5.5% due to the decline of the industrial base of the region coupled with the onset of global economic recession (Yorkshire Forward, 2010). Recovery from the decline of the region's economic base has been slow. Econometric analysis across the region show that although GDP rose by 0.5% in 2010, due to the increasing value of home grown products, the overall economic outlook is depressing (South Yorkshire Times, 2010). The industrial activities that have made South Yorkshire famous, such as metal work, coal, engineering and iron and steel are in significant decline as discussed above and many industries have entirely collapsed. The situation has changed dramatically since 2003 when the region experienced strong economic growth (BBC News, 2010). This situation is unlikely to change as unemployment continues to increase by an average of at least 0.2% per year and by the end of 2010, this rate was around 2.2% (Yorkshire Forward, 2010; Sheffield Telegraph, 2010). Recently, one of the largest steel making companies in South Yorkshire, Corus, made over 2,500 workers redundant due to this harsh economic environment (Yahoo News, 2009).

## **5.6 Socio-economic context of social enterprises in South Yorkshire**

As a result of the economic upheaval of the 1980s the South Yorkshire region as a whole contains some of the poorest boroughs in the UK. This picture is captured in Table 5.2 below which shows the severity of the deprivation in comparison to the rest of the UK. The figures offer a valuable insight into the full range of socio-economic and environmental problems plaguing the region. The region benefited from European financial assistance, under the European Regional Development Fund (ERDF) after being designated Objective 1 (the highest category of European support) at the Berlin summit in 1999. The subsequent programme of assistance was launched in July 2000. In 1999 South Yorkshire experienced a significant influx of

European structural support funding through Objective 1, the Single Regeneration Budget (SRB) and the Single Pot (IPSEYH, 2000). This funding was provided to tackle socio-economic deprivation in the poorest areas across the region through the provision of training opportunities, employment and business creation (SYIF, 2003). Objective 1 involved a £1.8 billion investment programme for South Yorkshire, including £700million from the European Union Structural Fund (GOYH, 2001). The development of sustainable social enterprises was considered a key way in which deprivation and exclusion could be tackled in South Yorkshire (IPSEYH, 2004). Objective 1 was also concerned with tackling unemployment in South Yorkshire particularly how the problem of retraining for employment could be addressed (Beatty et al, 2005).

**Table 5.2: Socio-economic deprivation in South Yorkshire**

<i><b>Borough</b></i>	<i><b>No. of wards in the most deprived 20%</b></i>	<i><b>Percentage of wards in the most deprived nationally</b></i>
Barnsley	17	77.3
Doncaster	14	66.7
Rotherham	13	59.1
Sheffield	13	44.8

Table 5.2: Adapted from Regional Economic Strategy Companion Document (2003)

The socio economic deprivation shown in Table 5.2 above has not shown any significant improvement since the onset of European financial support programmes. It is in this context that the development of social enterprises in South Yorkshire is being analysed.

The development of social enterprises in South Yorkshire has been acknowledged as potentially an effective intervention to address socio-economic ills in the region particularly through self employment. An integral part of the Objective 1 programme was an intervention called Community Action Planning that was allocated an amount of £21 million to support the development of locally based business initiatives such as social enterprises (Bache and Chapman, 2008). The feasibility of this intervention is supported by research carried out in 2004 across the region that suggested that 51% of miners who had lost their jobs would consider self employment (Beatty et al, 2005). Despite the region's deep seated economic problems, the social enterprise sector has been growing steadily as indicated by the diversity of thematic areas

shown in Table 4.4. However the current economic climate and the new coalition government's views on social enterprise, discussed in Section 5.3, may affect this growth.

In summary, the decline of the region's industrial base of steel manufacturing and coal mining resulted in particularly challenging socio-economic conditions. These became the focus of regeneration activities across the region, supported by local government and European financial assistance programmes.

The next section focuses on social enterprises in South Yorkshire. It draws information mostly from questionnaire returns and is complemented by data on what we already know about social enterprises drawn from various secondary sources. The social enterprise population in South Yorkshire is considered first in order to understand the impetus behind their establishment, before analysing their periods of existence and the support structures available to them.

## **5.7 Social enterprise history and population in South Yorkshire**

In Chapter 4 it was revealed that the number of organisations purporting to be social enterprises operating in South Yorkshire was difficult to ascertain, although mapping exercises have taken place in all sub regions within the region (DTI, 2003a). Researchers such as Riddley Duff (2002a) and Gordon (2006) have also undertaken assessments of the region's social enterprises and cooperatives, though the results of their scoping exercises are not yet publicly available. From figures gleaned from independent surveys carried out by sub-regional organisations such as SCEDU, we were able to estimate that there were no more than 400 of these organisations operating across the region. There are a relatively small number of organisations that might be classified as social enterprises that were established in the region well before the introduction of European infrastructural and financial support programmes in the 1990s. After this period however, there was a huge expansion of such organisations in the region (Sheffield Star, 2004). Unfortunately the majority of the social enterprises that were established have not been properly documented (SCEDU, 2003b).

There is a paucity of information relating to the emergence and development of social enterprise in South Yorkshire. Historically, organisations that describe themselves as social enterprises can be traced back to nineteenth century self help co-operative

and voluntary organisations. Although the region was characterised by a dual economy (agriculture and coal and steel), it was the latter that was dominant and resulted in exploitation and poverty (Hey, 1969). The resultant self- help interventions were followed by the emergence of the Rochdale Pioneers, who are considered to be the first community owned organisation dedicated to addressing socio-economic deprivation arising out of rapid industrialisation in Yorkshire (Wyller, 2008). Hey (1969) notes that because of the spectre of poverty, communities started turning to craft in order to sustain their livelihoods and this developed into cooperatives and social enterprises as we know them today. The development of these utopian organisations was unsurprising given the massive scale of industrialisation in the region which led to South Yorkshire becoming the Industrial Centre of England (Birch, 2006). The 1970s and 1980s saw a huge increase in cooperatives in across the country including South Yorkshire and some of these could have developed into social enterprises. However, it is important to note that the success of these organisations was minimal due to severe constraints on their viability (Brown, 2002). In the 1990s cooperatives, in the form of worker co-operatives, re-emerged in South Yorkshire, the majority of which were social enterprises. In 2007 they employed nearly 200 people and had a combined turnover of £5 million (Sheffield Co-operative Development Group, 2005). These developments however do not provide adequate information on the numbers and nature of self-defined social enterprises in South Yorkshire. The next section uses data emerging from descriptive statistics to illuminate this issue.

The results of the questionnaire returns shown in Figure 5.3 below provide an indication of the number of self-defined social enterprises operating in South Yorkshire. This information is essential in supporting the historical data available on such enterprises.



**Figure 5.3: The social enterprise population in South Yorkshire**

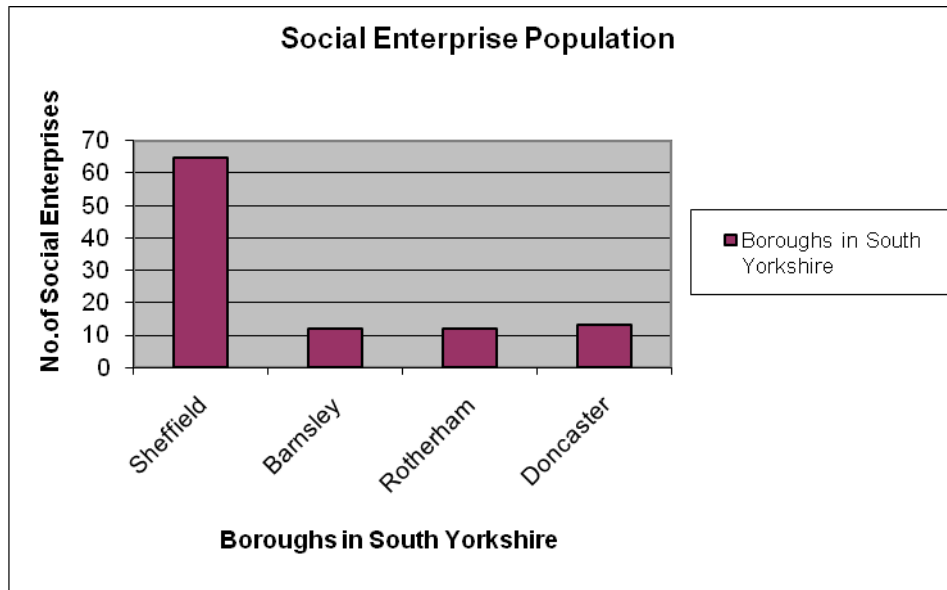


Figure 5.3: Created from questionnaire survey data

Sheffield has the highest number of organisations describing themselves as social enterprises (65) as Figure 5.3 shows. Doncaster was second highest with 13, with the metropolitan boroughs of Barnsley and Rotherham each having 12. All four boroughs are facing severe socio-economic challenges as previously explained. Further investigation is required to find out why Sheffield has a relatively high number of organisations describing themselves as social enterprises. It should be noted that the city underwent strong economic recovery in the early 1990s, a development which, as previously observed, led to Yorkshire Forward identifying it as the 'key driver of economic growth in South Yorkshire'. The city received over £23 Million of ERDF funding that was committed to a number of projects to boost the regeneration of the city (Breakthrough, 2004; SCEDU, 2003b). As a result, Sheffield's social economy was generating an average income of £4 million per year. Whether these developments had an impact on the number of social enterprises currently existing in Sheffield is an issue for further research.

The next section focuses on the period of existence of social enterprises in South Yorkshire

## **5.8 Age of social enterprises in South Yorkshire**

As previously noted, the history of social enterprises in South Yorkshire pre-dates the influx of European financial investments in 1999. Despite the deep seated socio-economic challenges, the region is characterised by a vibrant social enterprise sector, vibrancy reflected in the diversity of thematic activities that social enterprises are involved in as shown in Table 4.5. However, this growth is severely threatened by the current hostile economic environment caused by global recession. The economic upheavals of the 1980s and a steady inflow of European financial resources into the region have had an impact on the development of social enterprises there (Thompson et al, 2000; SYIF, 2003).

EU investment in the economic reconstruction of the region amounted to £1.8 billion over a seven year period from 1999. This included the provision of financial support to four sub-regional social enterprise support organisations (Yorkshire Forward, 2006). It is difficult to accurately determine the number and age of the social enterprises that benefited from European funding because of the likely inclusion of other organisations, particularly from the voluntary and community sector. These could have simply 're-branded' themselves as social enterprises to access support and resources available from designated infrastructural support organizations, thus distorting the true picture of social enterprises in South Yorkshire (GHK, 2005).

There are also a number of self-described social enterprises which were established in the region well before the onset of European infrastructural support programmes and have not been documented (SCEDU, 2003b). Others were simply operating without 'realising' that they were social enterprises (SCEDU, 2003b). Before 1980, only a handful of organisations in the region were classified as social enterprises, but there was a huge expansion, since the onset of EU financial assistance programmes (Sheffield Star, 2004).

Information in Figure 5.4 below, taken from responses to the survey undertaken in 2005, provides an indication of the ages of self-defined social enterprises in South Yorkshire. From the data it appears that European, and other, capital investments in the region do impact on the creation of social enterprises as discussed below.

**Figure 5.4: Ages of social enterprises**

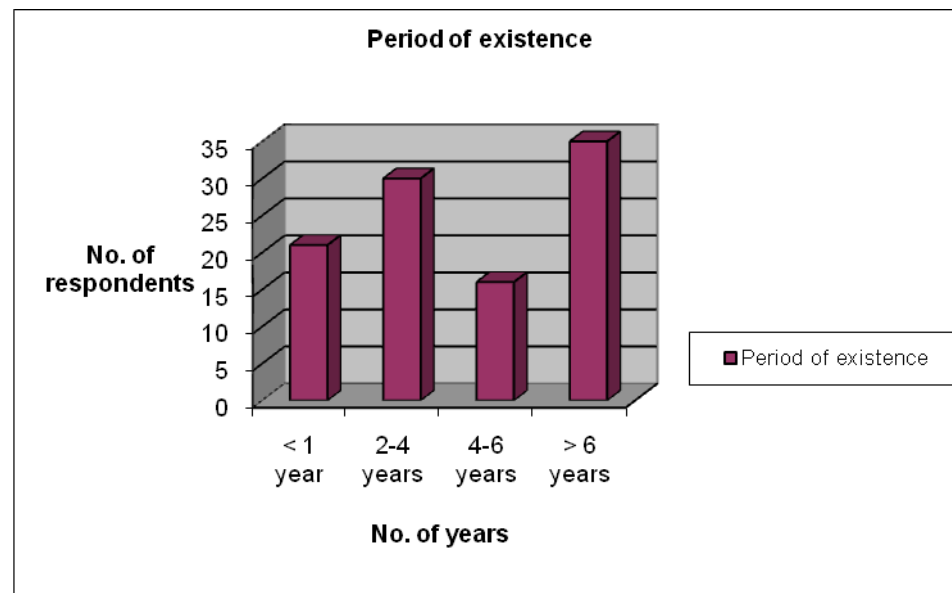


Figure 5.4: Created from questionnaire survey data

Figure 5.4 shows that the most common age for social enterprises is more than six years. This might be because, from 1999, there was a significant influx of European funding in South Yorkshire, through Objective 1, Single Regeneration Budget (SRB) and Single Pot. During this period South Yorkshire received more financial assistance than any other region within the county of Yorkshire and the Humber (SYP, 2004).

The results also reveal an apparent peak in the number of social enterprises aged between two and four years. This might be explained by the launch of the government's Social Enterprise Strategy in 2002, three or four years before the date of this survey.

Further analysis of the ages of self-defined social enterprises reveals that the number of those that have been in existence for less than a year is significantly greater than those that have been in existence for four to six years. The reason for this needs further research although the following factors may be relevant:

- Continuing government support through its social enterprise strategy. This support legitimised this sector and resulted in additional European and government funding as shown above.
- The figures are likely to include some organisations that re-branded themselves as social enterprises as discussed above.

The exact ages of social enterprises in South Yorkshire are therefore difficult to ascertain. What is clear however is that the history of the development of this phenomenon in South Yorkshire predates the introduction of significant European development funds.

Since the establishment of viable social enterprises was one of the objectives of the South Yorkshire Regeneration Programme, it is important to analyse the support structures available for social enterprises. The next section therefore focuses on social enterprise support organizations across the region, using information drawn from secondary sources and from the questionnaire survey.

### **5.9 Social enterprise support organisations in South Yorkshire**

There are a number of support organisations in South Yorkshire which play a pivotal role in supporting the establishment and growth of social enterprises across the region. These organisations offer different types of support to social enterprises including financial investment and business advice and counselling services. The region's social enterprise support infrastructure has been largely funded by grants through the Single Regeneration Budget (SRB) and European structural funds (IPSEYH, 2004). However, for South Yorkshire, these funding streams ended in 2007 when their focus shifted to supporting the economic regeneration of Eastern European countries (Flockhart, 2005). A key component of the Labour Government's policy on social enterprise included the establishment of Regional Development Agencies (RDAs) and regional support organisations. As previously described, this investigation identified and interviewed 18 social enterprise support organisations across South Yorkshire and beyond, some of which are shown below in Table 5.3.

**Table 5.3: Social enterprise support organisations in South Yorkshire**

NAME OF ORGANISATION	TYPE	LOCATION	NATURE OF SUPPORT	AREA OF INFLUENCE	CRITERIA FOR SUPPORT
Sheffield Community Enterprise Development Unit (SCEDU)	Sub regional social enterprise support organisation	Sheffield	1.Business advice and technical support 2. Grant funding packages	Sheffield	1.Viable business idea 2.Recognisable entrepreneur 3.Acceptable social enterprise legal structure 4.Clear socio-economic and environmental goals
South Yorkshire Key Fund For Social Economy	Community Development Finance Institution (CDFI)	Sheffield	1.Loan and grant support out of revolving fund  2.Equity Investment packages	South Yorkshire and Yorkshire and the Humber	1.Viable enterprise idea and model 2.Acceptable social enterprise legal structure 3.Clear socio-economic and environmental goals
Yorkshire Forward	Regional Development Agency	Yorkshire & the Humber	1. Provision of technical and financial support to social enterprises across Yorkshire and the Humber.	South Yorkshire and Yorkshire and the Humber	Regional enterprise support organisation
South Yorkshire Investment Fund (SYIF)	Regional business financial support organisation	Rotherham	1.Provision of mezzanine finance, and equity linked investments	South Yorkshire	Viable business idea and potential for rapid growth
Phoenix Social Enterprises		Rotherham			
South Yorkshire Open Forum		Rotherham	Sign posting and information dissemination	South Yorkshire	No criteria Information dissemination
Open Forum For Economic Regeneration(OFFER)	Community Empowerment	Sheffield		Sheffield	Sheffield based Community enterprises
Social Enterprise Barnsley		Barnsley			
Business Link South Yorkshire (BLSY)	Contract holder (from Yorkshire Forward/Objective 1) for sub regional social enterprise support organisations	Barnsley	Primary channel for funding and support to social enterprises in South Yorkshire	South Yorkshire	Sub regional social enterprise support organisation
In My Backyard (IMBY)	Representative organisation of social firms UK	Sheffield	Stimulate growth and development of social firms	South Yorkshire	1.Viable enterprise Idea 2.Social firm 3.Clear socio-economic and environmental goals
Sheffield Cooperative Development Group (SCDG)	Regional support organisations for social enterprises	Sheffield	Financial and technical support for co-operatives	South Yorkshire	1.Cooperative or working towards 2.Acceptable constitution

Table 5.3: Created from quantitative and qualitative research data

Table 5.3 above shows a wide range of organisations dedicated to supporting social enterprises across South Yorkshire together with their location, the type of support they provide and their criteria for providing grants or loans. Community Development Finance Institutions (CDFIs) within the region such as the South Yorkshire Investment Fund (SYIF) and the South Yorkshire Key Fund for Social Economy (SYKFSE) complement support being provided by the RDA, Yorkshire Forward, (IPSEYH, 2004). The involvement of major agencies such as Business Link and South Yorkshire Investment Fund, (not previously involved with social enterprise), is indicative of government enthusiasm for promoting the financial self-reliance of social enterprises.

In general, support provided to social enterprises in the region tends to be restricted to social enterprises within each borough. For example, in Sheffield, organisations describing themselves as social enterprises would approach local support organisations such as SCEDU or Sheffield Enterprise Clusters (SEC). This is largely due to contractual agreements between the providers of structural funding (Objective 1 and Yorkshire Forward) and borough based support organisations. However, there are support organisations whose remit goes beyond South Yorkshire and the Humber, such as the South Yorkshire Key Fund For Social Economy (SYKFSE). Their support is not restricted by a strict geographical focus.

However, following a review of the social enterprise support programme in 2007, a new consortium of businesses under Yorkshire Forward is responsible for supporting the development of social enterprises in the region. This body now offers support to the sector through a single 'portal' that replaces the sub regional support network that existed prior to 2008 and has been discussed earlier. It is also interesting to note that a recent Yorkshire Forward publication (Business Support Review, 2006) does not mention social enterprise in its proposed new regional economic development outlook. Instead, the focus is on increasing VAT registered businesses across the region, the majority of which are not social enterprises. This brings into question the commitment of the RDA in continuing with support programmes specifically designed for social enterprises.

The significance of this contextual background to this investigation can be seen in the following ways;

1. The region's geographical location away from the core urban conurbation of the UK gives it a distinct disadvantage economically. This has been exacerbated by the expiry of European structural funding in 2007 thereby severing a significant supply line of grant support for social enterprises and other businesses in the region (Regeneration and Renewal, 2005c).
2. The decline of the region's industrial base of steel manufacturing and coal mining resulted in particularly challenging socio-economic conditions discussed above. This saw European Union structural funds being channelled into the region through dedicated regional institutions to support economic regeneration activities including social enterprise.
3. Despite this, and other, financial investment in the region, the social needs of the communities have not been entirely addressed. The economic gains made in the region over the past decade have been negatively affected by the current economic recession. This, coupled with the current coalition government's public spending cuts, has seen a 10-15% reduction in local authority budgets. (BBC News, 2010). Since local authorities have been actively supporting social enterprise it is likely that this will impact negatively on the growth of this sector across the region.

These conditions make South Yorkshire an ideal location to understand the operations of social enterprises in the UK.

### **5.10 Chapter summary**

This summary draws out key elements from the preceding contextual analysis and discussion of social enterprises in South Yorkshire. It highlights three issues specified below, that are key to understanding the work that follows in this thesis.

The history of social enterprise in South Yorkshire is directly and intricately linked to interventions designed to ameliorate deep seated deprivation across the region. It is evident that the socio-economic conditions resulting from the collapse of the region's economic base provided the impetus for the establishment of social enterprises. The availability of EU financial support accelerated the establishment of organisations describing themselves as social enterprises.

The history of social enterprises in South Yorkshire predates the influx of European financial investment into the region in 1999. The region faces serious socio-economic and environmental challenges that have made it a focal point of state interventions to tackle deprivation, poverty and exclusion through the creation of social enterprises. These conditions allow us to understand the way social enterprises operate in South Yorkshire and the constraints and opportunities they face. Despite the deep seated socio-economic challenges, the region is characterised by a vibrant social enterprise sector, as evidenced by the diversity of thematic activities in which social enterprises are involved. However, the sector faces severe threats from the current hostile economic environment caused by global recession.

The state remains a key player in the development of social enterprises in South Yorkshire. This is evident in the current government's efforts to provide an enabling environment for the growth of social enterprises. The support strategy involves the use of regional and sub-regional institutions as conduits of financial and technical support to social enterprises in South Yorkshire. This support plays a key role in stimulating and catalysing the growth of these organisations across the region.

The next chapter pursues key themes identified in this chapter through case studies of four selected social enterprises in South Yorkshire.



# **CHAPTER 6: RESULTS: ORGANISATION AND STRUCTURE OF SOCIAL ENTERPRISES IN SOUTH YORKSHIRE**

## **6.1 Introduction**

The hybrid framework of analysis discussed in Chapter 3, consisting of the IPE and BTF approaches, identifies three key elements on which this investigation focuses as it addresses the research questions outlined in Chapter 1. These are social enterprise's historicity and structural positionality, the motivations behind it and its internal governance. Using the IPE approach to analyse social enterprise's historicity and positionality is fundamental to answering the first two research questions which relate to the types of legal structures that social enterprises have. Chapters 2 and 3 argue that the IPE and BTF approaches help us to understand the motivations of social enterprise and hence are useful guides in providing answers to the second research question which seeks to investigate the determinants of social enterprises' legal structures. Finally, an important element of the hybrid analytical framework is that it allows us, through the BTF and contractual elements of the theory of the firm, to critically analyse organisations' internal systems and to examine how these help shape the nature and form of what they do and how they operate. The literature review also suggests that these issues are currently under researched and therefore require further scrutiny. This analysis addresses the second and third research questions.

This chapter focuses on the detailed analysis of four case studies which were selected from the sample of respondents investigated in the exploratory research. The results are triangulated with questionnaire survey data and qualitative research undertaken in this investigation. The case study analysis focuses primarily on two legal structures, company limited by guarantee (CLG) and company limited by shares (CLS). These were identified in Chapter 2 as the legal structures most commonly found in social enterprises in South Yorkshire. The anonymity of the social enterprises has been protected. They are referred to as The Trainer, The Landscaper, The Cafe and The Community Champion respectively as shown below in Table 6.1.

**Table 6.1: Thematic activities of case studies under investigation**

<b>Organisation</b>	<b>Thematic Activity</b>	<b>Type of legal structure</b>
The Trainer	Provision of basic education and training	Share capital (CLS)
The Landscaper	Environmental management and consultancy	Share Capital (CLS)
The Cafe	Environmental preservation and renewable energy	Company Limited By Guarantee (CLG)
The Community Champion	Provision of non-accredited skills training	Company Limited By Guarantee (CLG)

This chapter is divided into five parts. The first introduces the scope of the case studies under scrutiny, focussing on the themes emerging from the case study content analysis discussed in Section 4.11. and considers how they assist in addressing the research questions. The second critically analyses key emerging themes from qualitative analysis of case studies. This section also links to the relevant descriptive statistics and qualitative data arising out of the exploratory research and the literature review in Chapters 2 and 3. The third part discusses and analyses the internal governance structures of the case studies and their relationship to the type of legal structure. Similarly, the fourth analyses the financial performance of the case studies and its relationship to the type of legal structure. The last section identifies and discusses key emerging issues and their influence on social enterprises.

## **6.2 Scope of the case study analysis**

The in-depth analysis of the case studies described in Chapter 4 identified three major emerging themes, essential in developing a deeper understanding of social enterprises and how their governance and legal structures impact on their operations. These themes (which also had sub themes) are:

1. Determinants of legal structure: This had six sub-themes discussed in detail in Section 6.4. The intention was to understand *why* particular legal structures were chosen, the *type* of legal structure chosen and the social enterprise's mission. The evidence gathered helped address all three research questions

2. Governance structures: The objective was to ascertain the types of governance of social enterprises in South Yorkshire and the legal structures driving them. This helped address the second and third research questions.

3. Sources of funding: The objective was to understand how social enterprises are financed. This included analysing their turnover and how their particular legal structure influenced their ability to mobilise financial resources from different sources. Evidence gathered in this process helped address the third research question.

The next section starts by focussing on the results of the case study case analysis, looking initially at the determinants of legal structure. When respondents were asked to state the reasons behind their choice of legal structure, six key determinants were identified. These were: influence of the policy environment; desire to achieve and uphold social objectives; the need to attain ownership of business and remuneration; access to funding; access to equity investments and availability of business and legal advice.

Before discussing these further, it is important to understand the nature and type of legal structures of self-defined social enterprises in South Yorkshire. This information is drawn from the results of the questionnaire survey.

### **6.3 Legal structures of social enterprises in South Yorkshire**

The IPE approach, as discussed in Chapters 2 and 3, helps us to understand the legal foundations of an economy and therefore facilitates the critical analysis of social enterprises' legal structures. There is no single favoured legal structure for social enterprises in the UK (DTI, 2002). Instead, they use a variety of legal structures under the U.K Companies Act (1985) and Industrial and Provident Society legislation (Leslie, 2002). Researchers also concur that there is no single model for social enterprises and that they cannot be defined solely by their legal status (Alter, 2004; DTI, 2002). These chapters also discussed the new share capital models available for social enterprises in the form of the CIC (share capital variant) and the NEWCO. Chapter 2 revealed that the most prevalent legal structure in the social economy is the company limited by guarantee (Economic Partnerships, 2004; Bank of England, 2003). Descriptive statistics from the questionnaire survey confirm that the CLG is the most common legal structure of self-defined social enterprises in South Yorkshire. These results are shown below in Table 6.2.

**Table 6.2: Types of legal structures of social enterprises in South Yorkshire**

<b><i>Type of legal structure</i></b>	<b><i>Number</i></b>
<b><i>Company limited by guarantee (CLG)</i></b>	73
<b><i>Company limited by shares (CLS)</i></b>	8
<b><i>Co-operative/IPS</i></b>	6
<b><i>Unincorporated association</i></b>	9
<b><i>Trust deed</i></b>	2
<b><i>Not yet constituted</i></b>	4
<b><i>Total</i></b>	102

Table 6.2: created from questionnaire survey data

The figures also reveal that, despite the ubiquity of organisations structured as companies limited by guarantee, traditional cooperatives, unincorporated associations and trusts persist within the social economy. Interestingly, there were eight social enterprises structured as companies limited by shares, (NEWCO), a legal vehicle pioneered in Sheffield. The emergence of share capital legal structures challenges orthodox views as these are not structures historically associated with the social enterprise philosophy. The investigation took place before the CIC, a share capital variant, was launched in 2005, hence its absence from the menu of legal structures shown in Table 6.2.

#### **6.4 Determinants of legal structure**

Social enterprises adopt specific legal structures for a variety of reasons and it tends to be assumed that their needs will determine the structure they will adopt (SEL, 2003). As Chapter 3 discussed however the reasons behind a social enterprise's choice of legal structure are unclear and inconclusive. Despite all the rhetoric on social enterprise development, this issue has continued to elude intellectual engagement and critical analysis. To date there is no consensus on a model or

framework in contemporary academic discourse. What exists in the literature assumes that entrepreneurs are sufficiently knowledgeable to make competent decisions when choosing a legal structure. Emerging work, however, reveals the complexity around this issue. The apparent lack of extensive research, consensus or attention to this phenomenon means there is limited information to guide national policymaking on effective strategies to develop and strengthen the sector.

The next section focuses on the policy environment, which was identified as a key determinant of the legal structure of a social enterprise.

#### **6.4.1 Policy environment**

As previously discussed, one component of the hybrid framework underpinning this investigation, the IPE framework, provides insight into the asymmetric power relations between the state, markets and society (Gonzales, 2008). This also helps in elucidating the role of the state, or public policy in general, as well as social enterprise in welfare provision. In the UK the development of social enterprise remains an important element of central government's policy formulation (Pharaoh et al, 2004). The government is keen to support social enterprises and assist them in becoming less dependent on grant funding and other forms of state support. From a policy perspective, the previous Labour government sought to create an enabling environment to foster the development of social enterprises. The current coalition government also recognises that the establishment of viable social enterprises can be an effective way in which a wide range of socio-economic issues can be tackled cost-effectively. Social enterprises are at the core of the government's efforts to address deprivation and exclusion through enterprise. We also saw that the cessation of European infrastructural funds and the turning of major funders towards loans rather than grant support have dramatically changed the entire funding environment for social enterprises (Buttenheim, 2002). The implication is that the state is now keen to see social enterprises being more professional, shifting away from grant funding and becoming financially sustainable (DTI, 2002; West, 2004). In addition there is growing realisation that an appropriate regulatory framework for social enterprises is critical for their growth and sustainability.

It was evident from the case study analysis that the policy environment plays an important role in influencing social enterprises' choice of legal structure. For the purposes of this investigation, the policy environment is analysed in terms of specific

interventions that the UK government and infrastructural organisations make in order to improve the governance of social enterprises and make them more successful as businesses (SESE, 2002). Such interventions relate specifically to the management and disbursement of the financial and technical resources required to stimulate social enterprises' establishment and development.

### **1. Policy environment and legal structure**

Analysis of the Café and Community Champion case studies shows the influence of prevailing policy on their decisions to select CLG legal structures. CLG status was chosen in order to comply with current policy on accessing support from funders that were disbursing central government and European financial support to social enterprises. As a respondent from the Café, whose social enterprise depends on grant support to cover start-up costs, said *'Some funders clearly wanted the CLG'*. He continued, *'as a social enterprise, (not for profit organisation), it's a good badge to have'*. When questioned further about what he meant by 'good badge', the respondent indicated that the CLG legal structure allowed them to identify themselves as a social enterprise and so access funding and support specifically available for the sector. These responses reveal two significant points. Firstly, the organisation's choice of legal structure has been influenced by funders' preference for a CLG model. Secondly, the organisation regards the CLG legal structure as accurately illustrating the identity they want to portray. This point also came out explicitly from the questionnaire survey undertaken. The need to secure grant funding was the most frequently cited influence (36% of respondents) on social enterprises' decisions to select a CLG legal structure.

Analysis of some of the Community Champion's funding applications also provided an insight into how current funding policy dictated the way social enterprises operated and specifically how they were managed. For example, the application forms required information on the organisation's management structures and in particular, the nature of its ownership. An example of such a form is shown in Appendix 7. Further analysis of this form revealed that funders were more inclined to support an organisation whose legal structure reflected the social ownership of the organisation. Therefore it is reasonable to conclude that these funders were more likely to accept a CLG or IPS as a legal vehicle for a social enterprise, since these are based on a community ownership model. This was confirmed by a respondent who remarked. *'When you require something from the government, it is easier to do*

*what they want. They (the government) clearly want the CLG, and we also agree with this'* (The Community Champion).

From the above, we can see that, while the respondents acknowledged that it was necessary to have a legal structure to access grant funding, the organisations are also compliant with prevailing funding policy. This is consistent with Haberberg and Rieple's (2001) view that governments can dictate non-profit organisations' direction through specific policy interventions.

Further evidence of the policy environment's impact on governance structures can be seen in the analysis of the case studies The Trainer and The Landscaper which are share capital companies. To draw down grant funding support from the European Regional Development Fund (ERDF), they were required to complete application forms, shown as Appendix 8. Part of the form required the applicants to complete a section on 'social enterprise gateway criteria'. This required evidence of the nature of the applicant organisation's governance. Firstly, the applicant was required to stipulate how their organisation's governance reflects social ownership. Secondly, the applicant organisation was required to provide evidence of 'wide membership, with limited provision for capital distribution to individuals' (SCEDU, 2006). Clearly the first option would indicate a legal structure such as a CLG or IPS, while the second would require a share capital legal structure. This was confirmed by the respondent from The 'Landscaper' who said *'I have always wanted a legal structure that allows me to distribute some profit, so the funder's conditions are OK with me'*.

The influence of the funder's requirements on recipient organisations' legal structures is further evidenced by the results of the qualitative interviews of social enterprise support organisations. Table 6.3 below shows the criteria that support organisations in South Yorkshire use prior to providing financial support.

**Table 6.3: Criteria for accessing business support in South Yorkshire**

- 'Viable business model
- A legal structure, CLG,IPS,CLS(*with modifications*)
- Presence of an entrepreneur(s)
- 'Robust governance model ( showing skills and competences of directors)
- Identification of a clear community of benefit

Table 6.3: Created from qualitative interviews of support organisations

Table 6.3 shows that one of the criteria is a legal structure. By insisting that social enterprises have a legal framework before receiving funding, support organisations require legitimacy, accountability and professionalism in the operations of social enterprises. Without a legal structure, it would not be possible for organisations to successfully apply for financial support. This was confirmed by a respondent from Social Enterprise Barnsley (a funder) who said *'we make it clear that we would want to see a suitable legal structure ...if an applicant hasn't got this, we always signpost them to someone who will help them'*.

The government's National Procurement Strategy for Local Government seeks to include social enterprises in a wider, modern, public service delivery. This was an impetus for The Trainer not only to have a legal structure, but also to model it on a share capital basis. As a respondent from this organisation said, *'the government wants to see social enterprises acting like businesses not community organisations.....we needed something like a share capital structure that we have to exploit opportunities coming from the government'*. The organisation was thus able to take advantage of opportunities such as outsourcing, emanating from the government's decentralisation of service delivery. Its business plan and some minutes of meetings clearly showed a conscious and deliberate decision by the organisation to mobilise enough capital to strengthen its capacity to service huge contracts. The initial capital outlay required by this organisation was in excess of £380, 000. Therefore there was a realisation that grant funding alone would be totally inadequate to raise such an amount and assist the organisation to develop sufficient capacity to be 'contract ready' (The Trainer's Plan, 2005). As the respondent remarked *'raising £380k through grant funding was out of the question...it would have taken us a long, long time....'* It was necessary to choose a legal structure that would enable the social enterprise to attract both grant and equity finance. This complies with central government's desire to see social enterprise achieve sustainability and growth through innovative legal structures (DTI, 2003c).

The impact of the policy environment on social enterprises' legal structures is further evidenced by the analysis of some banks that support social enterprises. A representative of The Unity Trust bank, which specialises in providing financial support to charitable organisations and social enterprises, was interviewed in this investigation. According to the respondent, it is a matter of policy that their clients *'need to have some form of legal structure that specify that any profit, surplus or*



*money that they make is actually re-invested back into the organisation*'. This response is a clear indication that an organisation with a share capital legal structure would be unable to secure financial support from the bank.

Evidence from descriptive statistics and qualitative interviews of social enterprise support organisations also revealed the influence of the policy environment on the type of legal structures of social enterprises. As previously noted, the need to secure grant funding was the most frequently cited influence on social enterprises' decisions to select a CLG legal structure. A sizeable number of respondents also cited the need to conform to funding regulations as the reason for selecting their particular legal structure. Table 6.3 above shows that institutional funders prioritise a viable business model and the presence of a legal structure as key criteria for funding. In this regard, funding policy has a bearing on the types of legal structures selected by organisations. This information therefore supports the findings from the case study analysis regarding the role of policy in internal organisational design.

The policy environment, as a determinant of legal structure, can be interpreted in two ways. Firstly, the decision to select a specific legal structure could be attributed to the general characteristics of organisations that the UK government is keen to promote in its broader strategy to tackle deprivation and exclusion. These include common ownership, democratic governance and social objectives. Therefore CLG and other charitable organisations associated with the mutual system become a natural and acceptable form of governance of community- led interventions that the government is committed to support. Arguably we can also detect an element of compliancy to the prevailing policy paradigm, by these social economy organisations.

Secondly, the policy environment provides opportunities for those enterprises that are entrepreneurial and eager to participate in public service delivery and contracting. Participation in such programmes has necessitated that social enterprises widen their sources of income to strengthen their ability to tender. Consequently we have seen the emergence of innovative legal structures such as share capital legal structures previously unknown within the social economy.

The next section discusses 'social objectives' as an additional determinant of legal structure for social enterprise that emerged from the analysis.

### 6.4.2 Social objectives

Chapter 2 uses the IPE theoretical approach to discuss the origins of social enterprises, starting from the interventions that evolved in the nineteenth century to address extreme worker exploitation and poverty. The focus of these interventions was on the provision of social welfare to communities suffering as a result of industrialisation. We also saw that social enterprises evolved from the various organisations set up during this period of economic and social upheaval (West, 2004). The need to achieve social, economic and environmental objectives has continued to be central to the activities of the social economy and in particular social enterprises (Pearce, 2003; Chell, 2007). In the case study analysis, a strong need to preserve a socially useful focus also emerged as a key determinant of legal structure. This is unsurprising, given that maintaining a strong social orientation and promoting economic justice are key attributes of the social economy organisations from which social enterprises have evolved. Social objectives therefore become a key characteristic of social enterprises' identity (Favreau and Levesque, 1997; Peattie and Morley, 2008). Achieving economic objectives, i.e. profit, is not their only objective (Cyert and March, 1963; Berle and Means, 1932).

#### 1. Social objectives and CLG legal structures

This section starts by analysing The Café and The Community Champion that have CLG legal structures. The Café was originally set up as a wholly commercial share capital company before re-registering as a not for profit CLG ten years later. The reason given for this change in legal status was that the organisation felt that a CLG model would allow them to demonstrate their ethical and moral mission. Therefore the share capital structure was considered inappropriate to the organisation's objectives. A respondent from the organisation (with reference to the share capital legal structure) remarked *'there is a lot of cynicism around the objectives....to please share holders'* (The Café). He went on to say *'the share capital model seemed to be wrong at the time'* (Transcript 2, p.5). These statements reveal an aversion to profit distribution, reminiscent of the period when the first philanthropic organisations were created during the industrial revolution. This organisation, as explained in Figure 4.3, uses its expertise on renewable energy and environmental development to support various community development initiatives in Doncaster. The respondent continued by saying *'We basically wanted a legal vehicle that would allow us to strengthen our social ethos in our communities ....we are not guided by making profits'*. In addition

the organisation has a programme dedicated to supporting local disabled people, through various activities such as gardening. The strong social stance of the organisation is also reflected in their banking. The Cafe banks with one of the leading ethical banks in the country. *'We would not bank with any other bank that does not reflect our social and moral stance'*.

This strong social dimension is also demonstrated by The Community Champion which was set up to assist individuals in getting back to work after suffering from the effects of long term unemployment or recovering from illness or physical disabilities. Their advertising brochure from 2006 states that the organisation *'helps to minimise personal misfortune and maximise the person's individual skills'*. This assertion is made more poignant by the work the organisation did in its early days. Archival research unearthed an article in a local newspaper from 1993 (Star, 1993). According to this article the organisation was at the forefront of efforts being made in Doncaster to assist stroke victims to re-shape their lives through a variety of skills based training such as furniture restoration. This objective is typical of the social economy that seeks the protection of the rights of the vulnerable people (Defourny and Delvetere, 1999). A respondent from this organisation confirmed that the organisation would never have considered a share capital legal structure, saying *'we didn't want anything to do with profit...our organisation deals with vulnerable people and so we wanted something that would help us continue with this'* (The Community Champion). The first clause under the objects and aims in the organisation's memorandum and articles of association reinforces its overall social and moral mission. It states;

*'To promote work experience and employment opportunities by therapeutic and rehabilitation services for people with health problems, or who are disadvantaged and or who are long term unemployed'*. (The Community Champion's governing document)

The objects and aims of the Community Champion make no reference to large scale trading activities. This in itself is indicative of its mission to assist deprived members of the communities who have been previously overlooked by mainstream provision.

From the above analysis, we can detect a strong social mission and rejection of large scale commercial activities and profit distribution in both organisations. They opted for CLG legal status as they felt that a share capital legal structure would compromise their social ethos. A respondent from the Community Champion made it

clear that they wanted a legal structure that allowed them to involve the communities they serve in the running of the organisation. He remarked, *'our current legal structure (CLG) allows transparency. We are able to include willing members of the organisation in the running and decision-making of this organisation'*. Similarly, the respondent from The Café said, *'We have a board of voluntary directors whose members are employed elsewhere but who share our vision...So we wanted a legal structure that could allow them to be part of this organisation and contribute the development of our local community.....so the CLG was the one for us'*. Evidence from questionnaire returns also indicates a philanthropic orientation which aims to maximise value rather than profits. This is consistent with the work of Jensen (2001) and Freeman et al (2004) which argues that value maximisation and stakeholder relationships are key components of the operations of the firm.

To further clarify this discussion, Table 6.4 below shows a cross tabulation of type of legal structure and organisations' social objectives. The table shows that the majority of the respondents providing various types of social and welfare interventions have CLG legal structures. This finding is significant, as it confirms that the nature of social enterprises' objectives influences the type of legal structure they adopt. From the above observations, one can generalise that organisations with CLG legal structures are largely dependent on non-traded funding to achieve their outcomes. Therefore we can conclude that it was inevitable that they would select legal structures that reinforced their social ethos. It is also clear that service to the community, rather than trading to generate profits is at the core of the organisations' operations, views shared by Borzaga and Defourny (2001).

Investigating further the perceived advantages and disadvantages associated with the CLG legal structure provides insight into why it was selected. Not surprisingly, being able to demonstrate a social ethos emerged as one of the main reasons for adopting the CLG. A further advantage was that it was easy to apply and understand, a point clearly articulated by the Community Champion respondent. *'It was much better for us to go for something that we could clearly understand'*. This answer is consistent with the literature on why organisations opt for the CLG structure discussed in Chapter 2. This legal structure also allows the social enterprises to reinforce their social ethos and protects them from exposure to risk. CLG legal status allowed The Cafe to have an identity consistent with its social ethos. Neither of the respondents from the social enterprises with CLG legal status identified any disadvantages of their legal structure. They both indicated that, though they

considered other legal structures such as share capital and cooperatives, they felt that these lacked appeal and would compromise their social ethos.

## **2. Social objectives and CLS legal structures**

Moving onto the analysis of The Trainer and the Community Champion, both share capital entities, we can also see clear social objectives. For example, The Trainer's addresses unemployment and educational issues among disadvantaged members of the community in Sheffield. As a respondent said, *'as you know the area we are located in is very deprived and this is the key reason we set up...we are constantly looking at ways in which we can improve the lives of the people in this community'*. This includes equipping them with basic numeracy skills to enhance their chances of employability. The Landscaper was also guided by a strong sense of community development through its provision of employment opportunities, not only for entrepreneurs running organisations, but also for disadvantaged people within the wider community. This objective was clearly stated in the organisations business plan. Furthermore, a respondent said, *'provision of employment is obviously a key objective...our aim is to look at providing work experience and skills training to young people from the community'*.

When the memoranda and articles of association of both were analysed, they revealed clear embedded social objectives in addition to economic ones. One example in the governance document of the Landscaper read *'improving employability of disadvantaged people within the community of benefit'*, reiterating what the respondent had said above. However it was also apparent that, although social objectives were important, they did not appear to have significantly influenced their decisions to opt for share capital legal structures. Evidence from questionnaire returns confirmed that even social enterprises with CLS legal structures have strong social objectives as shown in Table 6.4 below. This finding is significant in that it suggests that, for an organisation to be identified as a social enterprise, it must show evidence of its social mission in its governing documents and share capital social enterprises are no exception. This supports the argument that a social enterprise cannot purely be described by its legal structure, but also by what it does. Such developments reveal how the social enterprise concept is evolving in tandem with market requirements. This point was made clear by a respondent from The Trainer when he said *'although we have strong social aims, we are aware that we need to compete in the market.....to be among the best in our area of business'*.

**Table 6.4: Type of type of legal structure and organisation's social objectives**

<i>organisation's social objectives</i>										
<b>Type of legal structure</b>	Provision of community facilities and resources	Creation of employment and training opportunities	Access to low cost financial products and banking	Improvement of the environment	Support and facilities for disabled and marginalised people	Provision of childcare facilities	Personal skills development	Improvement of health, nutrition and /or social care	Promotion of community languages	Total
Company limited by Guarantee (CLG)	27	24	0	4	10	3	3	1	1	73
Company limited by shares (CLS)	1	4	0	1	1	0	1	0	0	8
Co-operatives (IPS)	2	0	3	0	1	0	0	0	0	6
Unincorporated associations with a constitution	3	2	0	0	1	0	2	1	0	9
Trust deed	0	0	0	1	1	0	0	0		2
Not yet constituted	0	1	0	0	1	1	0	1		4
<b>Total</b>	<b>33</b>	<b>31</b>	<b>3</b>	<b>6</b>	<b>15</b>	<b>4</b>	<b>6</b>	<b>3</b>	<b>1</b>	<b>102</b>

Table 6.4: Created from questionnaire survey data

Overall, it can be seen that all the case studies sought to provide some form of access to opportunities and services to individuals overlooked by mainstream provision. These objectives had an impact on decisions to adopt specific legal structures, especially for those with CLG legal status. The results also show that a social enterprise as a business integrates social and economic objectives in its operations. These are some of the key constructs of the behavioural theory of the firm approach, associated with the work of Bowen (2007) and Cyert and March (1963) discussed in Chapter 3.

The next section discusses and analyses 'ownership' as a key determinant of legal structure.

#### **6.4.3 Ownership of business**

Contemporary discourse on the characteristics of social enterprises, particularly their ownership, continues as discussions in earlier chapters show. In the commercial world, ownership is a key determinant of the operations of the firm as discussed in Chapter 3 under the BTF approach. It is often based on how shares are allocated i.e. ownership of the residual rights of control (Burns, 2007; Parkinson, 2003). However, the concept of ownership within the social economy is not clear cut as Chapter 2 illustrated. Generally it implies social ownership of the organisation and its assets by a group of individuals mandated by members to run the organisation over a certain period of time (DTI, 2002). The general motivation here is expressed as social and philanthropic objectives. However, even within the social enterprise sector, as the discussions under the IPE framework show, different views of ownership have resulted in polarised views on how social enterprises should be governed. One school of thought associated with the work of Birkhoelzer et al (1997) and Pearce (2003) regards personal ownership and profit distribution as alien to the social economy. An opposing school of thought argues that the possibility of personal ownership of the organisation or resources within the social enterprise sector should not be dismissed outright. This view, associated with the work of Barker (2002a) and Dees (1998) amongst others, further argues that social entrepreneurs are no different from commercial entrepreneurs and hence should be rewarded financially for the risks they take. In this investigation, the concept of personal ownership of the business emerged as a key determinant of type of legal structure. In this analysis, ownership is discussed in the context of ownership of business, shareholding and access to surpluses.

Significantly and predictably only respondents from share capital companies stated that ownership and access to equity investments and share of profits were significant in their decisions to select this type of legal vehicle. They considered these attributes to be what attracted them to this type of legal structure, as opposed to others such as CLGs or cooperative models. This point was confirmed by the respondent from the Landscaper who said that the share capital model enabled him *'to keep ownership close to him'*. He commented further that *'I was investing my own money into this, so I wanted to protect that'*. This view is consistent with the arguments of Spulber (2008), in his seminal works on the extension of the theory of the firm. He says that the entrepreneur is a key component of the firm as s/he takes risks in establishing it which is essential for creating markets. The respondent from The Trainer took the same view. However his reasons were based on prior negative experience with a CLG *'I didn't like the CLG because I could not protect my own investments and I couldn't retain ownership... I was voted out of the organisation despite the fact that I was the owner and main entrepreneur'*. It can be seen that both respondents required that ownership of the business enabled them to invest and safeguard their intellectual capital, as well as to access a share of the surpluses generated by the business. This view is supported by Palmaas (2002) and Barker (2002b) who suggest that it is time to introduce new legal structures for social enterprises that recognise both social aims and ownership in order to propagate real entrepreneurship in the sector. We can therefore see some congruency between ownership of the business and rewards for entrepreneurship in social enterprises structured as share capital entities. The respondents from these entities concede that having access to a share of profits was a significant influence in selecting the share capital model. As the respondent from The Trainer said, *'I wanted a constitution that enabled me to gain control of the organisation and also have a share of the profits'*.

From the above analysis, it was clear that a legal structure of the share capital model that guarantees ownership and benefits from capital growth would be attractive to the entrepreneurs behind The Trainer and The Community Champion.

The results from the questionnaire returns shown below in Table 6.5, support this finding. The table shows a cross tabulation of type of legal structure with reasons for adopting it. Almost a third of respondents (32% of the sample) were influenced by the need to retain ownership. This finding is inconsistent with the widely held prejudice within the social economy against profit distribution as exemplified by Pearce (2003).



This analysis of organisations with share capital legal structures indicates that the role that access to profits and ownership play in developing sustainable social enterprises needs to be reviewed.

**Table 6.5: Type of legal structure and reasons for adopting legal structure**

<i>Reasons for adopting legal structure</i>										
<b>Type of legal structure</b>	Ability to attract external equity	Retain ownership/control of organisation	Attract grant funding	Only structure we are aware of	Establish contractual relationships	Protection of directors	To conform with model rules and regulations	Adopted existing and made necessary changes	Cannot answer	<b>Total</b>
Company limited by Guarantee (CLG)	5	23	29	8	1	2	3	2	0	73
Company limited by shares (CLS)	1	6	1		0	0	0	0	0	8
Co-operatives (IPS)	0	1	1	0	0	0	4	0	0	6
Unincorporated associations	0	1	4	0	0	0	1	0	3	9
Trust deed	0	1	1	0		0	0	0		2
Not yet constituted	0	1	1	0	0	0	0	0	2	4
<b>Total</b>	<b>6</b>	<b>33</b>	<b>37</b>	<b>8</b>	<b>1</b>	<b>2</b>	<b>8</b>	<b>2</b>	<b>5</b>	<b>102</b>

Table 6.5: Created from questionnaire survey data

In Table 6.5, it is clear that the majority of those who selected a legal structure consistent with retaining ownership chose the CLG. However, closer scrutiny of the concept of 'ownership' shows that in this instance, it refers to community ownership of resources, assets and organisations, rather than outright ownership through share holding. These are features of the democratic governance model associated with social enterprise, as discussed in Chapter 2. Incidentally, these respondents were also influenced by the need to attract grant funding, thus further complicating the perception of ownership.

A large proportion of the respondents with CLS legal structures shown in Table 6.5 selected this legal vehicle in order to retain ownership of the project idea. It is then assumed that retaining ownership of the organisation also entails having access to a proportion of the surpluses produced. This was revealed by the manager of The Landscaper, when he said, *'perhaps there was an ulterior motive for pushing forward a certain type of legal structure that guaranteed ownership and access to profits'*. More in-depth analysis of both share capital organisations' governing documents however, revealed a much broader meaning of ownership. Although the entrepreneurs leading these organisations retained ownership of the business through the number of shares they held, they also ceded ownership of a part of the business to other stakeholders in return for financial investments. This is acknowledged by Batra (1996), Barker (2003) and Grossman and Hart (1986) who argue that ownership of the business has to be guaranteed to attract investments and that it has become necessary to involve other stakeholders in the governance of a business. The results of qualitative interviews of social enterprise support organisations confirm this view of ownership. There is a general consensus that new share capital legal structures offer a tangible way of ensuring ownership and personal remuneration in the social economy.

Overall, the issues of ownership and remuneration add to the difficulties associated with defining the concept of social enterprise that were discussed in Chapter 2. For example, the findings emerging from the case studies and exploratory research contradict the UK government's own definition of social enterprise which, as previously discussed, clearly precludes personal financial gain and wider stakeholder participation in the governance of social enterprise.

#### **6.4.4 Access to funding**

Social enterprise developed from the social economy associated with philanthropy rather than from market activities. The survival of such organisations depended on grant and voluntary support, a tradition that has continued to this day. Most voluntary and not-for profit organisations continue to rely heavily on grant funding to sustain their operations (Walker, 1995; Shaw and Carter, 2007). This includes even those who have the capacity to generate income since most trade within tightly defined communities that cannot pay market rates for services provided (Simons, 2000; SEL, 2001). Financial support packages structured as loans have not been prevalent within the social enterprise sector (Peattie and Morley, 2008). The DTI (2004) survey reveals that where loans were provided to social enterprises they were provided on similar terms as to mainstream businesses. This may explain the low take up of loans by social enterprises who may struggle to meet the criteria set by providers of these types of financial packages.

The discussion of access to funding in this investigation focuses primarily on the ability of social enterprises to access both grant and loan financial packages from a variety of sources. Chapters 2 and 5 show that lack of access to finance is a constant threat to the viability of social enterprises, exacerbated by the decline in traditional sources of grant funding (Arradon and Wyler, 2008).

Though all respondents from the four organisations concurred that access to funding was a key determinant of type of legal structure, this appeared more significant for those enterprises with CLG legal status. For example when the respondent from The Community Champion was asked why they chose the CLG legal structure, he answered *'we were convinced that people would have greater respect for that.....and there is a possibility that funding would be easier to obtain... The legal structure (CLG) with charitable status would certainly enable the organisation to access funding from the public and other donors'*. When asked if his organisation had considered other legal structures (such as the IPS cooperative model that can also attract grant funding) he replied that *'the cooperative model appeared too complicated and so it was better for us to go for something that we could understand'*. Similarly, a respondent from The Cafe said his organisation selected the CLG legal structure because of the need to access *'grant funding to kick-start our enterprise'*. The respondent went on to confirm that the decision to adopt the CLG legal status was predicated on the need to mobilise grant funding to cover the costs

of delivering social value to the communities they serve. This organisation had considered other legal structures such as the IPS and the CLS but the respondent was critical of these saying, *'they were not suitable because one of our key aims was to draw down funding...and that's what we wanted to do, right from the start'*. This finding makes it clear that grant funding continues to play a major role in the development of non-profit organisations.

The above responses are consistent with the findings from questionnaire returns where 36% of the respondents acknowledged that they opted for CLG legal structure status to facilitate access to grant funding. This is unsurprising, bearing in mind that traditionally, grant funding constitutes a significant portion of the income of social enterprises. Table 6.6 below, showing a cross tabulation between type of legal structure and availability of financial support, reinforces this point.

**Table 6.6: Type of legal structure and availability of financial support**

<i>Availability of financial support</i>							
<b>Type of legal structure</b>	Awareness of funding sources available	Less emphasis on loans for business start-up	Make access to funding less bureaucratic and restrictive	More grant funding for business start-up	No changes necessary	Cannot comment	<b>Total</b>
Company limited by Guarantee (CLG)	19	5	10	12	1	26	73
Company limited by shares (CLS)	5	0	1	1	0	1	8
Co-operatives (IPS)	1	1	1	2	0	1	6
Unincorporated association	2	0	2	2	2	1	9
Trust deed	0	0	1	1	0	0	2
Not yet constituted	1	0	0	3	0	0	4
<b>Total</b>	<b>28</b>	<b>6</b>	<b>15</b>	<b>21</b>	<b>3</b>	<b>29</b>	<b>102</b>

Table 6.6: created from questionnaire survey data

Table 6.6 shows that more than half of the organisations with CLG legal status would like to see more grant funding available to social enterprises. In addition, a significant number of respondents with this type of legal structure would like to see access to funding made easier and less bureaucratic. We have already seen that this type of legal structure makes it easier for social enterprises to access public funding usually in the form of grants (Bank of England, 2003). Unsurprisingly, the above table also shows that social enterprises with CLG legal status make up the majority of those who are opposed to loan financial packages, a fact that reflects their philanthropic orientation. In the case study analysis it was clear that the respondents from The Cafe and The Community Champion were in favour of a legal vehicle that would enable them to access grants from a wider range of sources but were not interested in loans.

It is interesting to note that both share capital social enterprises under investigation managed to acquire grants from various social enterprise infrastructural support organisations. This was made possible by modifications in their governing documents that ensured that social and environmental objectives were upheld, as discussed further in Section 6.5.1 of this chapter. On this issue the respondent from The Landscaper said, *'the funders didn't like us at first because of our structure (CLS) but once they understood it the Key Fund [Funder] gave us the grant'*. This signifies a fundamental shift in how enterprises with legal structures that allow profit distribution are viewed by funders.

Overall, access to funding emerged as a determinant of legal structures in all four case studies. However, this seemed to be a stronger influence in those organisations with CLG status, where operational requirements proved to be a strong impetus behind the selection of this legal vehicle. This could be due to their philanthropic orientation and their desire to achieve social rather than economic objectives. A legal structure such as a CLG was likely to be more effective in allowing them to access funding to cover the costs of delivering the social benefits.

#### **6.4.5 Access to equity investments**

Discussions in Chapters 2 and 5 show that social enterprises are undercapitalised and face a plethora of barriers in their attempts to access external finance. There is also general consensus among researchers and practitioners that grant funding is not always beneficial to social enterprises because 'funding regimes inhibit an

enterprise approach' (DTI, 2002). It has also become increasingly apparent that philanthropy and government funding are insufficient to address the pervasiveness of social problems as the discussions in Chapters 2 and 3 reveal. The decline in traditional sources of funding and increased competition for available resources means that social enterprises need to diversify their income base (Peattie and Morley, 2008). Chapters 2 and 5 also show that access to finance continues to be a significant challenge to the establishment and sustainability of social enterprise (Bank of England, 2003; Alter, 2004; DTI, 2002). In addition several researchers argue that weak or unsuitable legal structures are negatively affecting social enterprises' ability to access different types of financial resources. This is important since a social enterprise is in essence a firm that seeks to compete in the market.

Access to equity investments emerged as a key determinant of type of legal structure for the organisations that had CLS models. The Trainer, for example, had ambitious financial targets when it was being set up. It projected a turnover of £300k in its first year of operations according to its 2006 business plan. Looking at the initial business set up costs and projected turnover, it was apparent that the organisation would need to mobilise a significant amount of capital and assets to meet this target. It therefore needed a legal vehicle that would lever in financial resources so that it could develop its capacity to deliver more value as Section 6.4.1 shows. While acknowledging its social ethos, the entrepreneur behind the activities was aware that grant funding alone would not meet all the financial requirements of the enterprise. Closer scrutiny of the organisation's memorandum and articles of association revealed a legal structure that not only reflected its socio-economic focus, but also a desire to extract value beyond the traditional social enterprises' sources of finance. Clause 5 of the governing document of The Trainer stipulates that;

*The company has 40 equity shares in the form of redeemable preference shares valued at £2500 each (memorandum and articles of association, 2006).*

The above clause shows a deliberate effort to cede part of the organisation to investors in return for much needed financial resources. The respondent from this organisation, when asked why the current legal structure had been selected, said '*we wanted a share capital legal structure that would enable us to issue shares and get financial resources from the private sector*'. On the same note the respondent from The Landscaper said, '*we wanted something (a structure) that would ensure the longevity of our operations by making it possible to acquire other financial products...*



*I mean investments*'. Therefore one can reasonably conclude that the desire to widen sources of financial resources influenced The Trainer's decision to select a share capital legal structure. This decision is consistent with the views of Low (2006), Barker (2003) and Cornforth (1988) who argue that social enterprises might need to embrace innovative legal structures to attract investments. The mention of the private sector is significant in that it reflects the challenges being posed by the reduction of the traditional public, institutional and philanthropic support for the social enterprise sector. This decline has severely affected social enterprises' ability to acquire resources as observed by Etchart and Davis (2003) and Flockhart (2005).

The quantitative data reflects how changes in the funding landscape have impacted on social enterprises' choice of legal structure. Table 6.4, which shows a cross tabulation of type of legal structure and the reasons for adopting it, confirmed this finding. Only those organisations with CLS legal structures selected their legal vehicle with the intention of accessing external equity investments. Though the number of such respondents was small, this is nonetheless indicative of more strategic thinking and a deliberate desire to diversify their income base and access mainstream finance. This to some extent shows that the choice of legal structure is influenced by the needs of the business which in this case include the ability to attract external equity investments (SEL, 2003; Alter, 2003; Barker, 2002b).

Further evidence from the quantitative research supports the finding from the case study analysis that the ability to access equity investments is a determinant of legal structure. Table 6.7 below shows a cross tabulation of type of legal structure and social enterprises' financial objectives. This aids in understanding of the relationship between the type of legal structure and how the organisation employs it to achieve its desired financial objectives

**Table 6.7: Type of legal structure and organisations' financial objectives**

<i>Organisations' financial objectives</i>							
<b>Type of legal structure</b>	Self sustainability	Generate profits and returns to shareholders	Building financial reserves for future investments	Provision of banking facilities for excluded people	None	Cannot comment	Total
Company limited by Guarantee (CLG)	55	0	11	0	2	5	73
Company limited by shares (CLS)	5	3	0	0	0	0	8
Co-operatives (IPS)	3	0	2	1	0	0	6
Unincorporated associations with a constitution	7	0	2	0	0	0	9
Trust deed	2	0	0	0	0	0	2
Not yet constituted	4	0	0	0	0	0	4
<b>Total</b>	<b>76</b>	<b>3</b>	<b>15</b>	<b>1</b>	<b>2</b>	<b>5</b>	<b>102</b>

Table 6.7: Created from questionnaire survey data

Table 6.7 shows that those respondents whose objective is to generate returns and profits for share holders are all structured as CLS models. So it would be reasonable to generalise that this objective would only be achieved through a share capital legal structure as this would attract equity and distribute profit. This point was confirmed by the respondent from The Trainer who said, *'As I told you earlier I have a few people who have invested their monies into this... of course they would be expecting a good return...and that's what we want so that they can invest more'*. It is also important to note that the IPS legal structure discussed in Chapter 3 could achieve this objective, but its share allocation is subject to restrictions (SEL, 2003).

The CLS legal structures of The Trainer and The Landscaper did not always facilitate their access to necessary financial resources as this legal vehicle is not common in the social economy. Predictably therefore, they found access to grant funding, in particular, largely restricted initially. Some funders were clearly ignorant of the existence of social enterprises with CLS legal structures. The difficulties faced by such social enterprises in accessing grant funding is evidenced by the remarks of a respondent from The Trainer; *'Some traditional funders did not understand it [the share capital model], so we did not get the grant funding we needed'*. One of the funders to which The Landscaper was applying for financial support questioned the appropriateness and the ethicality of the organisation's legal structure as shown previously in Section 6.4.3. The funder made it clear that, since the applicant's legal structure was share capital, they would need to be satisfied that the organisation was in fact a social enterprise. The funder in this instance was appalled at the CLS legal structure's potential to reward both entrepreneurs and shareholders financially and insisted that the organisation change its legal structure to a CLG before they invested in it.

This funder's views were inconsistent with the general attitude to share capital legal structures demonstrated by a number of enterprise support organisations in South Yorkshire. Evidence from qualitative interviews shows that, of ten organisations, half were supportive of share capital legal structures for social enterprises. The reason given for this was that such legal structures, though new to the sector, were critical in promoting entrepreneurial vibrancy and financial sustainability of social enterprises. In addition, the informants felt that share capital legal structures were a tangible way of ensuring ownership and personal remuneration. Further evidence from interviews of private sector organisations that support social enterprise shows the potential of the CLS model to mobilise financial resources beyond the social economy. Referring

to the CLS legal structure, a respondent from a firm of solicitors that provides legal advice to social enterprises (Bates, Wells & Braithwaite), said *'It allows equity investments. That is a real driver of commercial growth... just as it [share capital] is a driver of the commercial economy, it should be a driver of the social economy'*. It is important to note however that reservations were expressed about the share capital legal structure of social enterprise. A respondent from IMBY, a social enterprise support organisation, remarked *'Share capital models potentially are a good thing. The problem is that social enterprise is a new sector, it still doesn't know whether to turn to the business side or the social side. Some funders are also reluctant to invest in them'*.

Overall, the emergence and support of share capital legal structures in the social economy has the following implications. Firstly, the concept of social enterprise is constantly evolving as it adapts to changes in the global economic environment. This adaptation may involve consideration of new legal frameworks such as share capital models in order to remain competitive in the market. Adaptation and organisational transformation are key elements of the hybrid framework that underpins this investigation. Secondly, share capital based legal structures, though new, offer an additional mechanism for social enterprises to achieve their objectives. The introduction of the CIC legal structure with a share capital variant, discussed in Chapter 2, reveals political support for this new direction for social enterprise.

#### **6.4.6 Expert advice on legal structures**

The IPE approach, a key component of the hybrid framework used in this investigation, provides insight into the legal frameworks guiding the operations of organisations. Chapter 2 showed that, for social enterprises to successfully compete in the market with other businesses, they require access to high quality business advice and technical support. However, social enterprises have often struggled to access this type of support. There is consensus among social enterprise practitioners that the current and planned constellation of business advice and technical support services for social enterprise needs to improve (Alter, 2006; Barker, 2003). They say that current provision clearly lacks the capacity to adequately nurture new and emerging social enterprises (BASSAC, 2002b). Typically, voluntary groups within the social economy, as discussed in Chapter 2, play a critical role in providing the sector with advice on their legal structures. This service is normally free of charge and quite basic in nature. The social enterprise sector therefore requires an increased level of

advice and support to enable them incorporate suitable legal structures that will help them achieve their objectives. While there are a number of legal structure options available to social enterprises, lack of knowledge of these legal vehicles is chronic across the sector as discussed in Chapter 2.

One of the objectives of the study was to assess the influence of the availability of legal advice on type of legal structure, given its importance as indicated in the literature review. Case study informants were asked if they sought advice before deciding which type of legal structure to adopt. In the analysis it became clear that the availability of expert legal advice played a key role in assisting social enterprises to select an appropriate legal structure. All respondents, while initially, having some idea of the legal structure they wanted, sought legal advice before and after selecting it. For those structured as share capital companies, approaches were made to specific solicitors who were more conversant with this legal vehicle. As previously explained, share capital legal structures are a new and developing phenomenon in the social economy and there is a dearth of individuals or institutions with sufficient knowledge of their application to social enterprises.

The Community Champion's experiences in selecting a suitable legal structure epitomises the general difficulties social enterprises face in this area. Several legal structures were considered, including the cooperative model. A respondent from the organisation confirmed, *'I did some work with an organisation based in Leeds, a co-op.....it struck me that it really wasn't us'*. He went on to add that, despite deciding on the CLG legal structure, the organisation nonetheless sought legal advice which significantly influenced their choice of legal structure. *'We actually met some legal people, who gave us some guidance'*. The Cafe, which used to have a CLS legal structure prior to adopting the CLG, confirmed that expert advice had strongly influenced their decision to change their legal structure. The respondent remarked *'as a management committee, we made that decision to seek legal advice ...as you know, we didn't like the private company one'*. They wanted a legal vehicle that was consistent with their social ethos and specialist advice was important in their decision to select an appropriate legal structure. When these organisations were asked if they would have gone ahead with their choice of legal structure without legal advice, both indicated that they would not have done so. The responses from The Community Champion and The Cafe demonstrate the importance of external expert legal advice, even though the entrepreneurs behind the social enterprise already had some idea of the legal structure they desired

The influence of external, professional legal and business advice on the selection of a legal structure is also evident in the analysis of The Trainer and The Community Champion which have CLS models. For example, central to the needs of these organisations was a legal vehicle that was consistent with their aspirations (ownership and surplus distribution) as well as the ability to raise the amount of capital required to kick-start their operations. Confirmation of these objectives was provided by a respondent from The Trainer when he said, *'Mind you, we didn't understand the structure ourselves at first. All we needed was something that enabled the entrepreneur to be in control and have a share of the profits'*. The respondent from The Landscaper was also concerned by potential loss of ownership and control in his social enterprise and therefore paid for external legal and business advice to allay his fears. He said *'it was important to get the right advice...I mean legally before we started this project'*. He further commented *'I don't think I would have invested my money if these lawyers had not recommended this model'*. These findings raise three significant issues.

Firstly, it suggests that the respondents wanted legal structures that would allow them to achieve both organisational and personal goals. Table 6.5 shows that respondents selected specific legal structures to achieve specific objectives. For example those similar to respondents from the two share capital case studies selected a CLS because of the need to access external equity investments. Secondly, there is a general lack of advice and knowledge on legal structures within the social economy as shown in Table 6.8 below. As the respondent from The Landscaper said *'It took me quite a long time to find a solicitor who understands social enterprise... thanks to SCEDU... they put me in touch with someone who understands share capital models'*. Thirdly, the respondents were acknowledging the role of external sources of advice and support in helping them to select legal structures that were fit for purpose. This contradicts the views of those researchers mentioned in Chapter 2 that social enterprises have the knowledge and competency to make decisions about the type of legal structure they need.

**Table 6.8: Availability of legal and business advice in South Yorkshire**

<b><i>Key issue</i></b>	<b><i>Frequency</i></b>
More sector specific business advice	16
More awareness of sources of business advice	14
A desire to see less competition amongst support organisations	1
Need for improved quality standards of business advice	11
No changes are necessary	5
Cannot comment	55
<b><i>Total</i></b>	<b>102</b>

Table 6.8: Created from questionnaire survey data

Table 6.8 shows that the most frequent comment was that more sector specific business advice for social enterprises is needed. The second most frequent observation was that they were not aware of sources of business advice. In the exploratory quantitative research, one informant demonstrated this when he stated that his organisation did not know what a constitution really involved. They simply purchased a company structured as a CLG off the internet because they believed that funders looked favourably upon this type of legal structure. This deficiency in awareness has also been highlighted by Carter (2003) and Cox (2000). A sizeable number of respondents stated that the quality of available advice was very poor. This investigation however could not establish the identity of organizations that provided the business advice described by these respondents. These results also suggest that information needs to be made more user friendly and sources of advice and funding clearly signposted. As the respondent from The Community Champion stated, *‘information on legal structures is quite technical and you really need a solicitor who can explain this in layman’s terms’*. This was also supported by the respondent from The Café who said *‘we had to travel all the way to Sheffield for legal advice because there was no one here....I mean locally whom we were comfortable with’*.

It was clear from the case study analysis and information from descriptive statistics that:

The current level of provision of business advice to social enterprises is not adequate and needs to be improved. This finding is consistent with the observations of Alter (2006) and BASSAC, 2002b) discussed in Chapter 2.

Expert legal advice is critical in enabling social enterprises to select suitable legal structures that enable them to achieve their objectives.

The case study analysis also confirms that the decision making process involved in selecting an appropriate legal structure is complex and time consuming. Rather than endure this, social enterprises might adopt an uncomplicated legal structure such as CLG, even though it might not be appropriate for their needs. We saw in Chapter 2 that Lawrie (2002) argues that decisions on legal structure should be made and finalised before the project has commenced operations. The findings from case study analysis support this observation. They reveal that consultations and deliberations on legal structure took place before the legal structure was brought into operation.

The next section looks at the mission of social enterprises and its relationship with their legal structures. This emerged as one of the key themes in the analysis of the four case studies under investigation.

## **6.5 Mission and legal structure**

In Chapter 2 we saw that most researchers agree that social enterprises are hybrid organisations and that their mission is to achieve the triple bottom line of social, economic and environmental objectives (Dees et al, 2001; Dart, 2002). Their mission is important for social enterprises because it guides their work and enables them to identify themselves with their communities of benefit. In addition the mission also illustrates the key objectives that the social enterprise seeks to achieve. From the determinants of legal structure discussed above we can see that a strong social ethos and a desire to access funding and equity investments are integral elements of a social enterprise's mission to achieve social and economic goals.



### ***6.5.1 CLS social enterprises and mission***

In the case study analysis, the need to attain financial sustainability featured in all case studies under scrutiny. Results from questionnaire returns shown in Table 6.9 below support this finding with the majority of self-defined social enterprises stating that their main objective is to achieve financial sustainability. What was clear was that even those social enterprises with CLG legal status sought to accumulate or build financial reserves for future investments.

**Table 6.9: Description of organisation and organisations' financial objectives cross tabulation**

<i>Description of organisation</i>	<i>Organisation's financial objectives</i>						Total
	Financial sustainability	Generate profits and returns to shareholders	Building financial reserves for future investments	Provision of banking facilities for excluded people	none	Cannot answer	
Social Enterprise	44	3	8	1	1	1	58
Community organisation	4	1	4	23	2	0	34
Combination of all three			1				1
Co-operatives (IPS)	1	0	0	1	0	0	2
Registered charity				2			2
Development trust				2			2
Social firm constitution	0	0	0	1	0	0	1
Not for profit organisation	0	0	0	1	0	0	1
Self financing unit within a statutory organisation	0	0	0	0	0	1	1
<b>Total</b>	<b>49</b>	<b>4</b>	<b>13</b>	<b>31</b>	<b>3</b>	<b>2</b>	<b>102</b>

Table 6.9: Created from questionnaire survey data

Analysis of the missions of the case studies with CLS legal structures shows a strong desire to achieve economic objectives as discussions in preceding sections show. This is understandable, given that such entities have legal structures that allow them to cede part of their ownership to external investors seeking a financial return. As the respondent from The Trainer remarked, *'as I said before, we have people who have invested in this organisation and want a return'*. Attainment of financial sustainability inevitably becomes top priority in order to generate surpluses to pay entrepreneurs and meet financial expectations of external investors through dividend payments. While CLGs have the same need to provide salaries for entrepreneurs, they do not have financial obligations associated with a wider stakeholder base. Their commercial orientation is clearly visible in clauses 3.1 of both The Trainer and The Landscaper's memorandum and articles of association:

*'To carry on business as a general commercial company', (2005)*

This clause is significant in that it precedes the social and environmental objectives of the two entities. It is a clear statement of the organisations' strong ambitions to be financially sustainable. This is consistent with views of researchers such as Barker (2003) and Stutt (2001) who are of the view that social enterprises, despite their need to achieve social goals, should be more entrepreneurial and strive to operate as sustainable businesses. This is clear in The Trainer's strategies to achieve and maintain sustainability. The respondent from this organisation said *'we are in the process of setting up another trading arm ...a taxi business to increase income sources'*.

However, despite a for-profit orientation there is also an awareness of the need to achieve social and environmental objectives. The Trainer for example is clearly attempting to balance its financial mission with explicitly defined social objectives. The organisation operates in an extremely deprived part of Sheffield, with a diverse ethnic population. In addition to high levels of deprivation, the area also has severe unemployment problems. In its application for grant funding to commission a feasibility study, the social aims of the organisation were apparent when it stated that it *'seeks to develop key skills to enhance employability of individuals currently overlooked by mainstream provision'*.

The Landscaper's mission was clarified when the respondent remarked *'sustainability is the key and I firmly believe in internal growth'*. However the organisation also has

explicit social objectives. These include, according to its business plan, '*provision of local employment opportunities as well as preservation of the environment*'. The latter activity fits well with Pearce's (2003, p. 33) model of a social enterprise where he makes a specific caveat that 'any socially responsible organisation has to be environmentally responsible'.

One of the characteristics of a social enterprise outlined in Chapter 2 involves the management of generated financial surplus. Researchers generally agree that surplus income is ploughed back into the organisation to increase its capacity. This is evident in case study organisations with CLS legal status. For example clause 3.21 of the memorandum and articles of association of both such enterprises say:

*Any surplus income created through trading over and above that required meeting the above objectives, shall either be re-invested to grow the business or to promote the interests of investors (payments of dividends). Such resolutions will be presented by the Board and agreed by other shareholders.*

This clause is significant in that it is consistent with the characteristics of a social enterprise discussed in Chapter 2. The clause also identifies the organisations with CLS legal status as social enterprises, despite their commercial orientation and protestations from researchers such as Chell (2007), Pearce (2003) and Birkhoelzer et al (1992) who are opposed to profit distribution in the social economy.

### **6.5.2 CLG social enterprises and mission**

Comparing the for-profit approach of the above case studies with The Cafe and The Community Champion that are structured as CLG, a completely different picture emerges. While these entities also seek to attain financial sustainability, the attainment of social and environmental objectives is priority. For example, clause 3.1.1 of the memorandum and articles of association of The Community Champion says:

*'To relieve unemployment for the public benefit in such ways as may be thought fit, including assistance to find employment, and in particular (but not exclusively) by providing therapeutic and rehabilitation services ....'*

The above clause does not mention the generation or management of surplus funds in the mission of the organisation. When asked to clarify the aims of the organisation, a respondent from the case study said *'our aims are simply to help people that needed help.....it's as simple as that'*. This position statement is reinforced by evidence of the work the organisations do within the community as described in Figure 4.4. The Community Champion can be regarded as a 'jack of all trades'. *'People come up to me for all sorts of things'*, the chairman of this organisation remarked, *'I have even had a request for a solicitor. I act without legal commitment'*. A colleague of the chairman concurred by saying that he (the chairman) is in fact *'Rossington's or even Doncaster's answer to a Citizen Advice Bureau'*.

The Cafe works closely with disabled people from the surrounding communities. For example residents of the local autistic residential home have been involved in various projects such as composting and gardening at the organisation's premises. Referring to the service the organisation provides for the disabled members of the community, a respondent from The Cafe said *'they wouldn't have anywhere else really to go around here'*. This work is a public declaration that the enterprise exists for the benefit of the people particularly those from disadvantaged backgrounds. Such objectives are in line with Borzaga and Defourny's (2001) arguments that provision of services is central to the goals of a social enterprise.

The analysis in this section reflects the nature of social enterprises in that they are embedded in communities and work at grassroots levels to address gaps in mainstream provision of services.

### **6.5.3 Balancing objectives**

Balancing social and commercial objectives however, is a precarious task, as observed by Akwagyiram (2008). This can clearly be seen in the case study analysis but appears more significant in those with CLG legal status. Although the focus of The Community Champion is on achieving social objectives, there is a realisation that trading activities are also crucial for social enterprises. This position is reflected in clause 4 of the objects of the social enterprise:

*'To become sustainable by carrying out work and providing a service for profit'*

A respondent for the organisation confirmed this objective by saying *'at board level, we have said that we must earn more money...work towards sustainability'*. The analysis of its business plan shows that The Community Champion has engaged in a negligible amount of trading activity. It has expanded the 'Home Services' project that supports the elderly and vulnerable people within the community with services such as garden maintenance, cleaning and small repair works. Unfortunately this activity provides little of the much needed cash flow, an observation also made by the consultants who the organisation commissioned to carry out a feasibility study on potential income generating opportunities. Referring to the Home Services project, the consultants explained *'They have often been delivered for such low fee levels (or often for free) that the organisation's viability has been very marginal'* (Feasibility report, November 2006, page 5). Further analysis of the feasibility report indicated ambitious commercial pursuits which include delivering accredited training in carpentry and wood products manufacturing. An amount of £299,600 is forecasted over three years. What is of concern however is that the organisation's memorandum and articles of association forbids it from full scale taxable trading. Clause 5 (a) says that the organisation;

*'Shall not undertake any substantial permanent trading activities and shall conform to any relevant statutory regulation'.*

It is then difficult to see how the organisation envisages achieving its projected trading income targets given the restrictions in its governing documents.

While The Community Champion is likely to face difficulties with regards to trading, The Cafe's scenario is rather baffling. Despite having a seemingly robust business model and a legal structure that allows unrestricted trading activities, there is no attempt to consolidate and develop income streams. For example, the enterprise does not have any form of promotion, a fact acknowledged by the manager of the organisation. In addition the organisation's website was not functional. When asked about it the manager said *'Yes we have it (website) but it doesn't work really.....we ought to do something about it'*. When asked how the organisation intends to cover the huge capital costs of the planned environmental project shown in its business plan, the respondent indicated that they were going to approach local social enterprise support organisations for grant funding. He continued further by saying *'full scale commercial trading is not something that we have in mind at the moment'*.

These responses indicate either an ignorance of the mechanics of a business, or a complete reluctance to deal or engage with business issues affecting the organisation. They also illustrate the difficulties in changing ingrained assumptions and negative mindset inherent in the social economy (Social Futures Institute, 2004). This way of operating is what Barker (2002a) referred to as a significant drawback associated with social enterprises which are under a democratic or membership type of governance. The generation of trading income does not appear to be integral to the strategic plans of such organisations unlike those with CLS legal structures.

Overall we can see that the missions of the case studies under scrutiny sought to achieve three objectives i.e. financial sustainability, social and environmental objectives. This is consistent with most researchers' view that social enterprises are essentially hybrid models, using enterprise to further socio-economic and environmental issues. This is also consistent with the BTF approach, which regards a firm as having multiple goals and stakeholders (Bowen, 2007; Cyert and March, 1992). We can also see some congruency between mission and legal structure. For example, each case study organisation adopted a legal structure in tandem with its mission. From social enterprises with CLG legal status, one can detect a strong philanthropic stance with an equally strong aversion to personal capital accumulation and distribution. Those with CLS legal structures clearly exhibit a strong mix of both social and economic objectives. There is however; a strong desire to consolidate commercial activities to achieve financial sustainability. Practically the analysis shows the difficulties in balancing the achievement of the social, environmental and economic objectives of the organisations under investigation (Etchart and Davis, 2003).

The next section summarises the findings on the determinants of legal structures of social enterprises in South Yorkshire.

## **6.6 Summary of determinants of legal structure of social enterprise**

Table 6.10 below shows six key determinants of legal structure of social enterprises that have been identified by the case study analysis.

**Table 6.10: Determinants of legal structures of social enterprise**

- 1. Ownership of business**
- 2. Access to funding**
- 3. Access to equity**
- 4. Availability of legal advice**
- 5. Policy environment**
- 6. Social objectives**

Table 6.10: Formulated from case study analysis

The above findings offer a useful taxonomy of determinants of the legal structure of social enterprises. They suggest a much broader menu of such determinants than previously identified. The impetus comes both from pressures of globalisation and the traditional moral and social objectives which have characterised the social economy since its emergence. The above model contradicts a common view among researchers i.e. that the choice of legal structure is simply an administrative matter (Gair, 2005). The motivations behind the selection of a legal structure reveal the complexity associated with creating and developing a governance model for a social enterprise that is fit for purpose. The mission of the social enterprise, as we have seen, exerts some influence on an organisation's decision to select a specific type of a legal structure. It acts as a lever, powering and driving the decisions of individuals and organisations (Dees, 2001). These determinants of legal structures are analysed further in Chapter 7.

The next section looks at the relationship between governance and type of legal structure of a social enterprise. We saw that governance of social enterprises emerged as a key theme from the case study analysis as shown in Section 6.2.

### **6.7 Governance of social enterprises and legal structure**

As previously noted, a key element of the hybrid framework underpinning this investigation is that it allows us to critically analyse internal systems and processes of organisations. Chapter 3 showed that through elements of the theory of the firm such as Agency, Stewardship and Resource Dependency theories, we can analyse the internal governance of firms and examine how the nature of this governance influences their operations. Governance and in particular the role of the board is crucial in enabling a firm to achieve its objectives (Daily et al, 2003; Nicholson,



2004). We have previously discussed the nature of social enterprises' governance. In the non-profit sector governance is commonly characterised by democratic models consisting of independent, voluntary or unpaid boards of directors and trustees who run the organisation on behalf of members (Barker, 2003; Low, 2006). These directors and trustees are normally individuals with specific skills or knowledge that can benefit the organisation. This type of governance model is particularly problematic according to Barker (2003) and Etchart and Davis (2003) who argue that the shared ownership associated with democratic governance of social enterprise is a significant weakness, militating against commercial viability. They suggest instead a much broader multi-stakeholder model of a social enterprise, to enhance its capacity for growth and sustainability. This new line of thought is becoming more prominent with recommendations to explore stewardship models of governance for social enterprises, given the growing economic and social demands they face (Low, 2006; Van Slyke, 2000; Mason et al, 2006).

The next section looks at the results emerging from the internal structural analysis of the organisations under scrutiny.

#### ***6.7.1 Board of directors, composition and purpose***

The board of directors of any organisation is critical in shaping its strategic thrust. Daily et al (2003) argue that the board is the locus of the internal governance of a corporation and performs a number of tasks and roles. Chapter 3, with its use of the BTF approach and particularly thorough agency, stewardship and resource dependency approaches, shows that the board of directors performs several functions and roles. Muth and Donaldson (1998) suggest that these include control, co-optation and empowerment, while Zahra and Pearce (1989) highlight service, strategy and control. Within the social economy, however the role of the board is largely focussed on ensuring accountability, legitimacy and transparency, as discussed in Chapter 2 (Dees, 2001; Campbell, 2007). Boards of directors of non-profits are commonly associated with unpaid voluntary members. Other researches such as Barker (2002a) however assert that boards' functions in the social enterprise should be no different from those in the commercial world, although their composition may be different.

Analysis of the composition of the board of directors and the functions of the boards of the cases under investigation painted an intriguing picture. The next section focuses initially on board composition.

## **1. Board structure and composition of CLG case studies**

Looking at the governance of The Cafe and The Community Champion that have CLG legal structures, we can see in Table 6.11 below that their boards consist entirely of unpaid volunteers who also live locally. These volunteers sitting on the board also include operational management staff. The respondent from The Community champion said *'we are all volunteers; we don't want to get anything out of this...I mean...financially. We are here to help the community'*. These volunteers are therefore motivated by philanthropic rather than economic considerations in their involvement in the governance of these social enterprises. This is consistent with Evans (2001) and Pearce's (2003) observations on volunteerism in the non-profit sector discussed in Chapter 2. The individuals on the boards of these organisations have not been selected on the strength of the specific skills or knowledge that they bring to the organisation, but rather because of their passion for the community and its well being. The respondent from The Cafe made this clear when he said, *'we [the directors] could be doing other financially rewarding things in our life....we want to help the community and this is what brought us together'*.

In addition, the memoranda and articles of these organisations preclude personal remuneration of individuals within the organisation, except the payment of wages and reasonable travel expenses. For example, clause 5.2 of the memorandum and articles of association of The Community Champion says that board members must not:

*receive any payment of money or other material benefit (whether directly or indirectly) from the organisation except;*

- 5.2.1 reimbursement of reasonable out-of-pocket expenses (including hotel and travel costs) actually incurred*
- 5.2.3 payment to any company in which a director has no more than a 1 per cent shareholding*
- 5.2.4 in exceptional cases, other payments or benefits*

Clause 39 on The Cafe's memorandum and articles of association states that:

*‘the trustees may be paid all the reasonable travelling, hotel and other expenses, properly incurred by them in connection with their duties...but shall otherwise be paid no remuneration’.*

These clauses are typical of not-for-profit democratic governance models typified by shared ownership and protection of community assets, observations made by (Pearce, 2003; Barker, 2002). This is confirmed by the results from the questionnaire returns on the governance of social enterprises undertaken in this study. These results are shown in Table 6.11 below which is a cross tabulation of description of organisation and governance of social enterprise.

**Table 6.11: Governance of social enterprise**

<i>Description of organisation</i>	<i>Governance of social enterprise</i>						<i>Total</i>
	Volunteer board and staff	Paid board of directors and staff	Manager/main entrepreneur	Volunteer board of directors and paid staff	Volunteer board and part time paid staff	Managed by host organisation	
Social enterprise	5	2	9	41	1	0	58
Co-operative	1	0	0	1	0	0	2
Community organisation	4	1	4	23	2	0	34
Combination of all three	0	0	1	0	0	0	1
Registered charity	0	0	0	2		0	2
Development Trust	0	0	0	2	0	0	2
Social firm	0			1		0	1
Not for profit organisation	0	0	0	1	0	0	1
Self financing unit	0	0	0	0	0	1	1
<b>Total</b>	<b>10</b>	<b>3</b>	<b>14</b>	<b>71</b>	<b>3</b>	<b>1</b>	<b>102</b>

Table 6.10: Created from questionnaire survey data

Two key issues appear in the above table. Firstly, it shows that the vast majority of these self-defined social enterprises are governed by volunteer boards of directors/trustees and paid staff. This is not surprising, since historically this has been the most common form of governance structure in social enterprises.

Secondly, it can be seen that the number of self-defined social enterprises with paid boards of directors and staff account for a very small percentage of the sample (3%). Even though this number is negligible, it nonetheless signifies a deviation from the norm of purely voluntary boards. The main reason for this could be the need to foster commitment and retain essential skills necessary for the growth of the organisation.

## **2. Board structure and composition of CLS case studies**

The case study organisations with CLS legal structures have an added dimension to their boards of directors. In addition to typical for-profit shareholders, voluntary organisations and their respective lead entrepreneur hold some shares. The quantitative research revealed that 14% of social enterprises have co-opted owner managers on their boards. In this case, there is a distinct move from traditional forms of participative and democratic management principles as social entrepreneurs take the lead and provide hands-on management of the social enterprise. This development is also indicative of the gradual movement of social enterprise from democratic to stewardship models of governance (Low, 2006; Mason et al, 2006; Barker, 2002b). These developments are underpinned by the need to foster managerial motivation, which is one of the key principles associated with stewardship theory and particularly the work of Muth and Donaldson (1998), Donaldson and Davis (1991) and Nicholson and Kiel (2004) discussed in Chapter 3.

The presence of voluntary boards of directors in the governance of share capital social enterprises also raises eyebrows. Closer scrutiny of these organisations' memoranda and articles of association revealed that this voluntary board of directors, in essence, hold shares that do not benefit from capital gain, but serve the purpose of a social lock. This social lock, similar to that of the CIC discussed in Chapter 2, ensures that the organisation does not compromise the achievement of its social aims. This vital purpose was confirmed by the respondent from The Trainer, who, in reference to these board members, remarked *'they vote on decisions pertaining to the overall direction of the company... They ensure that social ethos is maintained and that the company remains a social enterprise'*.

The next section focuses on the functions of the boards of directors of the organisations under scrutiny

### **6.7.2. Board functions**

#### **1. CLG Board Functions**

Chapter 3 discusses the board of directors' role under selected contractual elements of the theory of the firm, namely Agency (AT), Stewardship (ST) and Resource Dependency (RDT) approaches. It can be seen that the board of directors performs a variety of functions that assist firms in achieving their objectives. Zahra and Pearce (1989) for example, summarises the role of the board as service, control and strategic. Muth and Donaldson (1998) on the other hand summarise the primary roles of the board as managerial control through AT, co-optation through the RDT and empowerment through the ST approach. Chapter 3 also critically analyses the implications of using such theoretical lenses to understand governance of social enterprise. We saw that Callen et al (2009) argue that the AT and RDT approaches are applicable to non-profits and social enterprise although these areas are still under-researched in the social economy. The analysis of the functions or roles of the boards of directors of the case studies under scrutiny is discussed below.

For cases with CLG legal status their boards demonstrate democratic governance principles, associated with social enterprise, such as social ownership and participation of community members in the running of the organisation. In addition to setting the strategic direction of the organisation and ratifying decisions, the boards of directors of The Cafe and The Community Champion also control and direct the organisations' day to day activities. These activities, particularly monitoring and control of activities are consistent with the Agency theory, associated with the work of Berle and Means (1932) and Jensen and Meckling (1976) amongst others. In this case the boards are agents of their stakeholders, i.e. the community (Callen, 2009; Miller-Millensen, 2003),

For example, the respondent from The Community Champion remarked, '*the board works closely with the manager and operational staff...we monitor everything because as I have said, our activities are funded and we have to be accountable to funders*'. Regarding the function of its board, the respondent from The Cafe said

*'everything is done democratically, but it is our duty to ensure that the staff are doing their duties, because we are accountable to the community and funders'.* These responses show that, although not usually possessing residual assets, social enterprises do need to protect the assets they have from abuse, observations also made by Miller-Millensen (2003).

The boards' functions, however, appear to be incongruent with the democratic governance models associated with social enterprise. This type of governance emphasises values of participation and employee involvement in the governance of the social enterprise. However, it appears to be presenting operational problems, typified by The Community Champion. By closely controlling the activities of managers as well as making and ratifying decisions, the board is effectively implementing its own decisions, a situation the organisation itself acknowledges. *'We need a management team....we don't find time to sit back and try to look forward to find our direction...it's an area we badly miss out on'.* These statements reveal that executive and governance roles in social enterprise governance models are not clearly delineated and therefore can create dysfunction. They also show the lack of strategic foresight in some boards of organisations with shared ownership, discussed previously.

Curiously, senior management positions in both organisations were unpaid and their respective boards stated that they expected volunteers to fill these posts. The chief executive of The Cafe showed the characteristics of a volunteer in the true sense of the word when he said *'I am the manager, but volunteer manager really, but also a director...I am employed elsewhere and I come here a couple of days per week'.* Similarly, the manager of The Community Champion runs a commercial organisation of his own and volunteers his time, one day per week, to the social enterprise. He said, *'My background is commercial, I come out of business and volunteer my services, but charities and charitable businesses are all new to me'.* Although these individuals are part of the boards of their respective organisations, it does not appear that their commercial expertise is being exploited for the benefit of the organisation. Their poor financial positions, shown in Section 6.9, support this.

The Cafe and The Community Champion do not have any external share holders whom they have to satisfy financially but they have stakeholders such as the community members who vote and appoint directors onto the board. The duties of these boards are largely fiduciary i.e. holding the organisation and its assets in trust.

This is a characteristic of democratic governance models associated with the non-profit sector (Spear et al, 2007; Low, 2006). Although the boards of The Community Champion and The Cafe perform a strategic role, this is severely limited by lack of an enterprise culture and failure to clearly separate the roles of the board and executives. While these boards demonstrate democratic governance principles, they are also monitoring and controlling their respective organisation's activities on behalf of the community they serve.

The next section discusses the boards' functions in case study organisations with CLS legal structures.

### **3. CLS Board function**

The functions and roles of the board of directors of the enterprises with CLS legal status differ from those discussed above. Unlike those with CLG legal status, there is a clear attempt by the board to provide autonomy for senior managers to work in the best interests of the organisation. This is consistent with the ST approach to governance (Pfeffer and Salancik, 1978; Davis et al, 1992). Perhaps this is because of the extended stakeholder interest arising from their legal structure and the need to take into account views and inputs from those who have vested interests in the organisation. As the respondent from The Trainer said, *'We have a good board... they let us do the work. We go to them for advice on issues affecting the organisation... the senior managers here ...we let them get on with it'*. The respondent from The Landscaper also said, *'the board members are similar to what they would be in a private company....it's a practical choice rather than a social choice... They [the board] are responsible for strategic issues including ... help with key decisions'*. In both cases the lead entrepreneurs perform the CEO role and are also central in the decision making process of the board as they are part of it. They are mandated to make operational decisions and their expertise is recognised by their respective boards, a point made by a respondent from The Landscaper when he said *'I still make the day to day decisions and go to them [the board] for legal and financial advice'*. This response highlights the role of the board as adviser and strategy formulator i.e. making key decisions and providing the necessary direction and strategic focus required for the organisation to achieve its objectives (Nicholson and Kiel, 2004; Zahra and Pearce, 1989).



The boards of directors of the two CLS organisations are also responsible for recruiting the top management of the firm who are responsible for operational issues. This top management reports to the board (Cohen and Cyert, 1965). For example, The Trainer has two full time paid senior managers. When asked how these were recruited, the respondent said, *'As you know we have a board, and this is one of its duties to recruit senior managers, it's not my responsibility alone'*. The Landscaper, however, is yet to recruit a senior manager but the respondent confirmed that recruitment of such staff is done by the board. Both were managed by full time paid managers, who were also the owners of the businesses, as well as board members.

The two CLS organisations had mechanisms that permit external share holders to invest financial resources in the organisations for financial gain. They also had mechanisms to co-opt individuals or funders onto their boards for the benefit of their organisations. This is addressed by resource dependency theory which provides insight on how a firm can mobilise resources through its type of governance (Daily et al, 2003; Muth and Donaldson, 1998). The Trainer managed to attract three social enterprises onto its board, two of which actually bought dividend bearing shares valued at £2500 each, while The Landscaper was in the process of exploring potential voluntary organisations that might be so co-opted. When asked to elaborate further on the purchase of shares by social enterprises, the respondent from The Trainer said, *'yes, they [the social enterprises] also want to grow their capital...and it's good for us that we can raise finance this way, without seeking a loan'*. He explained further *'they sit on the board and can vote'*. The Landscaper made some concessions to allow one of its funders, the South Yorkshire Key Fund for social economy, to be included on the board. This funder had expressed a commitment, not only to sit on the board, but also to purchase dividend bearing shares. This development shows us that even funders and Community Development Financial Institutions (CDFIs) are now seriously considering their financial survival. The funder's expectations however were clearly stated in their share agreement communication with the social enterprise:

*'The shares that the Key fund will take will be preference shares that provide a return on interest of 6%.....the interest of this share will be paid in priority to any declared dividend'* (South Yorkshire Key Fund, 2004).

Although the dividend rate of return of 6% is quite low compared to commercial rates, it nonetheless shows that support organisations are now more interested in growing

their capital, a phenomenon noticed by Buttenheim (2002). The funder also made it clear that they wanted to ensure that public funds were not abused. The investment agreement document clearly stated that the share they were buying in the company would enable *'the SYKF to retain some form of control over the investment of public funds in your private company'* (SYKFSE, 2004). These are significant developments in the social economy. By co-opting a funder onto the board, the Landscaper was establishing links with external organisations and ensuring access to financial resources essential for its survival. This is a characteristic of the RDT approach (Pfeffer and Salancik, 1978). It is important to note that this participation of the funder in the governance of the organisation was facilitated by a share capital legal structure. Results from descriptive statistics discussed in Section 6.4.5 reveal that one of the reasons why some informants selected CLS structures was their ability to facilitate access to equity investments. It would not have been possible for individuals or organisations such as funders to invest in organisations with CLG legal status and expect financial benefits through capital growth since CLG has *'no concept of sharing profits with those who are involved in it'*, a fact made clear by a respondent from HLW, one of the firms of solicitors that provide advice to social enterprises.

Analysis of the roles of the boards of directors of social enterprises with CLS legal structures reveals that they empower senior managers as well as co-opt key resources and expertise from external sources (Muth and Donaldson, 1998). These particular roles are associated with stewardship and resource dependency theorists as discussed in Chapter 3. The analysis also shows how nature of governance and type of legal structure can influence a social enterprise's ability to extract resources from the wider market to support its social aims. This is exemplified by the emergence of social enterprises and voluntary organisations buying shares in other social enterprises, which is certainly something new within the sector. This social enterprise governance model reflects a drift from a democratic to a stewardship model as discussed in Chapter 3 and associated with the work of Low (2006). This development implies a desire to run the social enterprise along commercial lines, similar to private enterprises.

The next section focuses on the financial analysis of the case study organisations, in particular their sources of funding. This is one of the key themes shown in Section 6.2 that emerged from the case study analysis and requires further exploration. This analysis makes it possible to ascertain and explore any relationships between financial performance and type of legal structure.

## 6.8 Sources of funding and legal structure

Chapter 2 reveals that there are several sources of funding for social enterprises, depending on their stage of development. These are classified as traditional and non-traditional sources of financial support. Traditional sources include a number of financial packages such as loans and grants (Alter, 2004; Walker, 1995). Grant funding in particular continues to be one of the most common sources of finance for social enterprises (Heal, 2009). Due to the complexity of the economic environment and the continuing need to address social needs, social enterprises are increasingly considering non-traditional financial sources for survival (Brown, 2007). These include use of patient capital and equity funding to augment their budgets so that they can deliver more value. The literature review also shows that social enterprises need to compete with the private sector for resources in the market and therefore require suitable mechanisms to do so (Heaney, 2010).

The analysis of organisations with CLS legal status showed that their sources of funding comprised grant finance, loan finance, equity investments and entrepreneurs' own capital. While loan finance indicates a willingness to take risk, the presence of equity investments is evidence of a decisive shift in resource mobilisation strategies. It also indicates selection of a legal structure that enables an organisation to widen its sources of finance. Further scrutiny of financial records and related documents held by these two social enterprises revealed that some social external organisations had also purchased, or intended to purchase dividend bearing shares in these case studies. As previously noted, The Trainer had already issued two shares, worth £2.5k to local social enterprises and The Landscaper had issued dividend bearing shares to a major social enterprise support organisation in the region.

The sources of funding of social enterprises structured as CLG, on the other hand, comprised mainly grant funding together with some board members' own philanthropic capital investments. The grant funding was subject to specific caveats from the funders. For example in the case of The Cafe and The Community Champion, grant support was restricted to covering the costs of delivering training courses, wages and volunteer expenses. As the respondent from The Community Champion said '*the training that we deliver is all grant funded.....we can't use this for anything else*'. The philanthropic investments of board members also varied in nature. Analysis of financial information of The Community Champion obtained from

UK Companies House revealed that its current chair had invested a substantial amount of his own money in the organization, totalling £17,179. This philanthropic investment was accompanied by a promise made to repay him at such a time as the enterprise made a surplus. However, bearing in mind the dire financial situation of the organisation, it was difficult to see how the organisation could generate a surplus to repay these funds. The Cafe however is a rather intriguing case. The volunteer manager and his wife, who are both directors, own the land and the property that the social enterprise is using. *'We donated the land that we are operating from'*. They have leased the property to the social enterprise free of charge. This further throws into doubt the organisation's viability if proper economic rents are considered. The philanthropic investments made by board members of The Cafe and The Community Champion to their own organisations indicate a strong social mission and a rejection of personal capital accumulation.

It was also interesting, though unsurprising, to note that although CLGs can attract loan finance neither of these organisations had ever considered loan finance, or were willing to do so. Unlike the case studies with CLS legal structures, these show a clear aversion to risk. This therefore required the researcher to carry out deeper analytical work on the viability of these organisations by investigating further the provisions of their legal structures with regards to borrowing funds. While The Community Champion's governing documents did not allow the organisation to borrow funds and provide security for such funds, The Cafe's governance documents allowed it to do so. Clause 4.7 of the powers of the organisation in its memorandum and articles of association clearly state that the organisation can:

*'Borrow money and give security for loans'.*

Having the ability to borrow funds and pledge security of assets is critical to any social enterprise governance document, argues the National Council for Voluntary Organisations (NCVO, 2006). However, curiously, The Cafe has not yet seen the need to borrow money, despite the huge capital expenditure envisaged in the next phase of its development discussed in preceding sections.

Comparing these governing documents to those of the case studies with CLS legal status, a distinct difference is evident. Both social enterprises with share capital legal structures have governing documents that allow them to borrow money, including

loans. For example clause 3.9 in The Trainer's governing documents says that the organisation is permitted;

*'To borrow money and to secure by mortgage, charge or lien upon the whole or any part of the Company's undertaking and property (whether present or future), including its uncalled capital, the discharge by the Company or any other person of any obligation or liability'.*

The above clause makes it clear that the organisation is not restricted from securing financial resources from different sources or from making its assets available as collateral against external borrowings.

The next section focuses on the analysis of the case studies' turnover and its relationship to type of legal structure.

## **6.9 Nature of turnover and legal structure**

In Chapter 2, we saw that social enterprises generate income in a variety of ways. They are also continuously exploring ways of diversifying these sources of income. In Chapter 3 it was shown that through the BTF approach, it is possible to critically analyse an organisation with a multiplicity of objectives (Berle and Means, 1932). While social enterprises are conscious of their social, economic and environmental objectives, they are also acutely aware of the need for financial sustainability. Earned income in particular has become important for social enterprises, since traditional sources of funding are gradually becoming competitive and restricted. Discussions in Chapter 2 as well as evidence from descriptive statistics revealed that social enterprises' income comes from a combination of earned income from sale of goods and services and non-market resources such as government subsidies and private donations. Chapter 2 also showed that most social enterprises are funded by combining income from trading and grant funding from structural funds, donations or local authorities (Grenier, 2003). This income represents the turnover of such organisations, from which the organisation pays wages, builds reserves or compensates those who put their money at risk in order to develop the organisation. The later refers mainly to external shareholders who receive rewards for investing in social enterprises.

When the respondents from the case studies were asked to discuss their turnover, and in particular, its nature, the following picture emerged. Overall, the income that made up the turnover of the four case studies came from four sources, namely taxable trading income, equity investments, grants and donations, as well as contracts. This finding is consistent with results emerging from the descriptive statistics shown below in Table 6.12. It can be seen that a significant number of respondents (64%) generate their income from a combination of grant funding and earned income. It is important to note that trading activities also include contracting.

**Table 6.12: Type of legal structure and means of generating income cross tabulation**

<i>Means of generating income</i>							
<b>Type of legal structure</b>	100% grant funding	Grant and trading activities	100% trading including contracting	Not yet trading	Membership subscriptions	Cannot comment	Total
Company limited by Guarantee (CLG)	12	47	11	1	1	1	73
Company limited by shares (CLS)	0	6	2	0	0	0	8
Co-operatives (IPS)	0	6	0	0	0	0	6
Unincorporated association	0	6	2	0	1	0	9
Trust deed	0	1	0	0	0	1	2
Not yet constituted	0	1	0	0	3	0	4
<b>Total</b>	<b>12</b>	<b>67</b>	<b>15</b>	<b>1</b>	<b>5</b>	<b>2</b>	<b>102</b>

Table 6.12 Created from questionnaire survey data

The bulk of CLS social enterprises' income came from taxable income and contracts with various public bodies and private customers. This was also shown in the results from the questionnaire survey shown in Table 6.10 above. For example, The Trainer's earned income came from long term contracts with Learn Direct and JobCentre Plus. These two organisations (Learn Direct and JobCentre Plus) are government funded initiatives providing a range of support structures to improve the lives of disadvantaged people. In addition to direct trading activities, income for The Landscaper came from contracts with various private and public clients. As the respondent from The Landscaper said, *'one of the key areas of our work involves contracting...we are negotiating with a number of both private sector and local authority clients at the moment'*. Contracting in particular highlights a new dimension in the social enterprise sector. It implies that social enterprises have, or are beginning to acquire, the requisite business acumen, legal structures and strategic management skills required to win contracts and interact with businesses outside the sector.

The turnover of the case study organisations over a specific period (2006-2007) was analysed as shown in Table 6.13 below

**Table 6.13: Nature of turnover**

<b>Income £</b>		<b>% grants</b>	<b>%trading/contracting income</b>	<b>% donations</b>
<b>The Trainer</b>	200k	0	100%	0
<b>The Landscaper</b>	60k	0	100%	0
<b>The Cafe</b>	75k	70%	30%	0
			(trading only)	
<b>The Community Champion</b>	80k	75%	15%	10%
			(trading only)	

Source: Case study interviews and financial documents

Table.6.13 summarises the sources of income and turnover of the case studies under scrutiny. It shows that while CLG social enterprises were also generating income from trading, the amounts were small compared to the grants they received. From initial interviews with the manager of The Cafe, it appeared that turnover came from 100% trading activities (£75k per annum). Closer analysis of financial information gleaned from UK Companies House however, showed very little income being generated from trading, with a strong propensity for grant income being



exhibited. Therefore, The Cafe, despite having the potential to earn significant income from trading, was teetering on the verge of bankruptcy. The Community Champion similarly relies mainly on grants to sustain its activities, with negligible amounts of income coming from trading activities. Approximately 75% of the organization's turnover is made up of grant funding. However a respondent from this organisation surprisingly remarked, *'Our aim is to reduce grant funding to 10% of total income'*. It is difficult to see how this objective can be achieved in view of the organisation's negative attitude to trading as discussed in preceding sections.

The role grant funding is playing in supporting social enterprises' activities is consistent with the results from questionnaire returns. As Table 6.10 above indicates, only 11% of the social enterprises with CLG legal status were generating income from trading activities. Grant funding continues to play a pivotal role in the activities of those respondents. It can also be seen from Table 6.10 that it is only those with CLG status which are likely to continue relying on grants for their survival. Due to documented changes in the grant-funding environment as discussed in Chapters 1 and 2, it is likely that few other windows of opportunity for funding will be available to them. They will find it difficult to extract financial resources in the form of loans (because they cannot pay them back), or venture capital (because they have no mechanisms for issuing shares or dividends) (Brown, 2003). Social enterprises with share capital legal structures, on the other hand, have the potential to access wider sources of income and strengthen their capacity so as to secure large contracts. This is illustrated by the ability of The Trainer and The Landscaper to secure such contracts from private and public bodies.

Having analysed the sources of funding and turnover of the social enterprises under investigation, the next section summarises their financial health.

## **6.10 Summary of financial position**

This analysis is based on calculation of current ratios and assessment of the nature of the organisations' current balance sheets as of 30 June 2007. The results are shown below in Table 6.14. Figures are based on the most recent information from the audited accounts of the organisations obtained from UK Companies House. The current ratio shows the organisation's capability to cover short term debts at short notice (Capon, 2008; Grant, 2002). The formula for calculating this ratio is Current Assets (CA)/ Current Liabilities (CL) (David, 2009). Using the current ratio makes it

possible to critically analyse social enterprises as business entities and assess how well they can meet short term cash needs. It was also necessary to analyse the balance sheets of the case studies to evaluate their long term solvency, feasibility of projected strategies and creditworthiness (David, 2009).

**Table 6.14: Financial health of the case studies**

	<i>The Trainer</i>	<i>The Landscaper</i>	<i>The Cafe</i>	<i>The Community Champion</i>
<b>Current ratio</b>	<u>(CA)£19,647</u> (CL)£13,360	<u>(CA)£5,411</u> (CL) £328	<u>£40,939 (CA)</u> £43,929(CL)	<u>(CA)£47,300</u> (CL)£51,260
<b>Balance Sheet</b>	<u>+ve Capital &amp; Reserves</u>	<u>+ve Capital &amp; reserves</u>	<u>-ve Capital &amp; reserves</u>	<u>-ve Capital &amp; reserves</u>
	TA-TL £58,100-£30,397 = £27,703	TA-TL £11,153-£328 = £10,824	TA-TL £64,650-£67,640 = (£2,990)	TA-TL £58,165-£62,125 = (£3,960)
	(Total Capital & retained earnings + shareholders' funds) +ve	(Total Capital & retained earnings + Shareholders funds) +ve	£ Nil Retained earnings & Reserves -ve	£Nil Retained earnings &Reserves -ve

CA-Current Assets  
CL-Current Liabilities  
TA-Total Assets  
TL-Total Liabilities

Source: Case studies financial information

The above analysis shows that those social enterprises with share capital legal structures have positive balance sheets and current ratios in contrast to those structured as company limited by guarantee. While this does not necessarily mean that the share capital social enterprises are sustainable, it nonetheless puts them in a favourable position to borrow funds or attract external financial investments. A negative current ratio implies that an organisation cannot meet its short term debt obligations. Coupled with negative balance sheets, this suggests that those with CLG legal status will find it difficult to attract substantial financial resources, a situation that has been discussed in previous sections. Their attractiveness to potential lenders, given their poor commercial performance, must be in question. This scenario perhaps explains why these two organisations did not attempt to access loans.

Neither has considered loan finance to support their activities nor expressed any willingness to do so in the future. On this issue, the respondent from The Cafe said, *'No, we have no intention of getting loans at present because we are currently talking to a number of grant funders who like our project'*.

The results from qualitative interviews shown in Table 6.3 reinforce this point. They reveal that social enterprise support organisations are keen to support social enterprises demonstrating well thought out and tested business ideas, crystallised into comprehensive and bankable business plans. According to research commissioned by the Small Business Service in 2004, most commercial loans made to social enterprises were on the same terms as those provided to mainstream businesses (SBS, 2004). From our analysis, organisations with CLS legal structures are more likely to access this type of support than those with CLG legal status.

The financial analysis of the enterprises with CLG legal status in this investigation shows that they are not in a position to employ full time paid staff, unlike those with CLS legal status. The analysis and interviews also show that the staff posts are funded from external sources rather than from generated income. This situation exerts great pressure on the organisation to continuously seek additional funding to keep key staff in post. Revealing the scale of the problems caused by inadequate staffing levels, the respondent from the Cafe said, *'the lady that works in the café has phoned in sick and so it's only me today'*. According to the UK National Joint Council pay scales (2008), a manager of an organisation within the social enterprise sector would be paid a salary ranging from £26K to £28k per annum. Therefore if we factor in the costs of paid managers into the cost structures of their respective organisations, they would be rendered insolvent. This shows that some social enterprises with CLG status might struggle to attain viability. This does not however imply that all social enterprises with CLG legal status are unable to employ full time paid staff or achieve financial sustainability.

The reasonable financial health of The Trainer and The Landscaper could have several explanations. Firstly, both organisations have viable business models that have enabled them to secure contracts consistently. For example, after barely two years of trading, The Landscaper had cleared its loan of £8k from The South Yorkshire Key Fund for Social Economy. As the respondent from The Cafe said, *'I have already told them [The Key Fund] that I will be writing them a cheque to clear my loan'*. Secondly, their legal structures enabled them to secure additional capital

through share allocation. This method of raising finance enabled the organisations to develop the capacity and credibility to successfully compete for work. Here we see legal structures that not only allow various stakeholders to participate in the organisations, but also allow financial reward through capital gain. Although management becomes considerably more complex, the need to achieve financial sustainability to pay wages and dividends is an added impetus to work harder.

## **6.11 Chapter summary**

In Chapter 3, the BTF approach and contractual elements of the theory of the firm made it possible to analyse the objectives and the internal and external dynamics of social enterprises. We saw that the majority of social enterprises are heavily reliant on grant funding and have traditional governance and legal structures associated with common ownership. It was also clear that social enterprises exist and operate within a wider macro-economic environment and require appropriate legal structures to mobilise financial resources for their survival. Like for-profit organisations, they are exposed to influences of both micro- and macro- economic factors, making this objective difficult to achieve. The in-depth case study analysis has assisted us in identifying key issues relating to legal structures, governance and operational features of social enterprises. The evidence from this analysis also confirms the challenges that social enterprises are facing in accessing financial resources, particularly with regards to the type of legal structure they possess.

The results provide insight into the determinants of legal structure of social enterprise, an important area identified in the literature review as under-researched. The findings of this investigation reveal that the determinants of social enterprises' legal structures are much more complex than previously recognised. Both internal and external factors affect social enterprises' decisions on the type of legal structure to adopt. The resultant legal structures influence the outcomes of social enterprises in different ways. For example, social enterprises with CLG legal status may face restrictions in accessing some types of financial resources beyond the social economy in comparison to those with CLS legal status. Determinants of legal structures are further critically analysed in Chapter 7.

The case study analysis shows that innovation in governance models has become an important pre-requisite for success in competitive markets. In this instance, moving towards for-profit stewardship models that are driven by share capital legal structures

has opened up opportunities that traditional social economy organisations cannot exploit. The relatively good financial performance of CLS legal structures as shown in Table 6.12 is evidence of this.

The hybrid framework of analysis discussed in Chapter 3 and shown in Figure 3.3 was used to define the parameters of this investigation. The framework made it possible to identify and investigate key areas of social enterprise development, evidenced by the results shown and critically analysed in this chapter. Evidence to support the arguments presented in this chapter has been triangulated with information drawn from descriptive statistics and qualitative research undertaken prior to the case study analysis.

The next chapter discusses and analyses further the findings emerging from this investigation.

## **CHAPTER 7: DISCUSSION AND ANALYSIS**

### **7.1 Introduction**

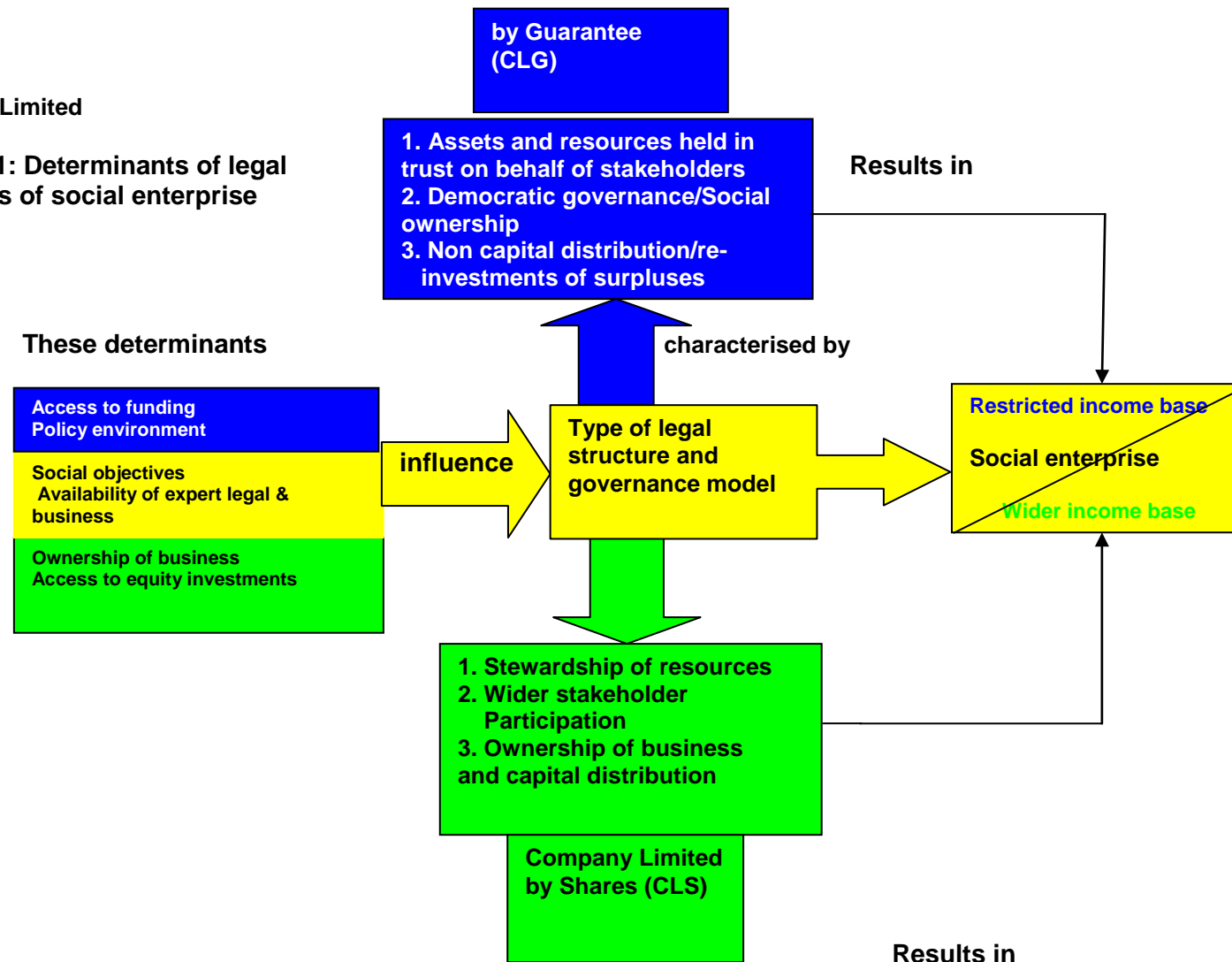
This chapter draws on key analytical points raised by the findings in Chapter 6. These will be analysed in the context of what we know about social enterprises, and the theoretical frameworks outlined in the literature review. Extending further the core elements of the hybrid framework that has guided discussions in Chapter 6, we critically analyse both empirical and theoretical findings emerging from the investigation. The discussions and analysis of literature on social enterprises in Chapters 2 and 3 have revealed significant gaps in knowledge of the contemporary development of social enterprise. One such gap relates to legal structures and how they influence social enterprises' operations in competitive markets. In addition we saw that the current literature fails to sufficiently address the reasons why a social enterprise selects a specific legal structure. Using elements of the hybrid framework, the in-depth case study analysis in Chapter 6 reveals the complexity of legal structure determinants and their influence on what a social enterprise does. Results from questionnaire survey in the form of descriptive statistics were used to triangulate evidence from the analysis of case studies in this chapter. The methodology chapter highlighted the difficulties of researching social enterprises, in particular their internal processes and governance structures, despite a number of empirical research exercises having been commissioned in the sector. It was only through a mixed method approach involving in-depth case study analysis that it was possible to make a significant contribution to knowledge of the determinants of legal structures as outlined in Chapter 6. Chapter 5 discussed the socio-economic context of social enterprises in South Yorkshire, showing that the region contains some of the most deprived areas in the UK and that social enterprises are playing an important role in revitalising economically deprived areas.

This chapter consists of two parts. The first commences with a diagrammatic representation and summary of the key results from the case study analysis as well as evidence from descriptive statistics. The second further discusses and analyses the themes identified and explored in the case study analysis. The different ways in which the type of legal structure influences the outcomes of social enterprise are

explored. Links are made to the emerging results discussed in Chapter 6 as well as to relevant literature and theoretical frameworks selected for this study.

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Figure 7.1: Determinants of legal structures of social enterprise





## 7.2 Summary of case study analysis results

Figure 7.1 above brings together key elements emerging from the in-depth case study analysis in the previous chapter. The network of flows shown above is in the form of a multiplicity of interactions that attempt to capture the dynamics and complexity of the evolution of social enterprises. It is important to note that the information in the diagram has been empirically derived. Figure 7.1 therefore extends further the three themes (determinants of legal structure, governance and financial sustainability) identified and analysed in Chapter 6. These are pertinent to our understanding of the establishment and development of social enterprise in South Yorkshire. Further analysis and discussion of these themes is guided by the theoretical frameworks previously identified.

Figure 7.1 shows that specific determinants result in particular types of legal structure for social enterprise. This in turn informs the social enterprise's governance model as well as its ability to achieve financial sustainability. For example in the case of The Trainer, the need to access equity investments and to own the business idea influenced the choice of a CLS legal structure, whose governance model was characterised by elements of both stewardship and resource dependency approaches. This social enterprise has the potential to increase its turnover and cash flows into the organisation due to its robust business model and a legal structure that allows it to access a variety of commercial opportunities. Such an organisation therefore seeks to integrate the achievement of both financial and social goals in its operations. This resonates with the views of BTF theorists, such as Cyert and March (1963) and Berle and Means (1932).

On the other hand, the need to access grant funding was a key determinant of choosing a CLG structure. The governance models of such organisations are characterised by an aversion towards material infrastructure and a commitment to democracy and inclusiveness in the running of the organisation. The case study analysis shows that such characteristics are important in guiding the operations of The Community Champion and The Cafe. Their heavy reliance on grant funding means that both enterprises have limited prospects of achieving long term financial sustainability, given the demands of a competitive market. Their vulnerability to the vagaries of the market and their inability to pursue a wide range of commercial opportunities means that their potential to attain financial viability is limited, as shown in Figure 7.1. This is confirmed by the financial health of the organisations under

scrutiny as shown in Table 6.14 as well as by observations of researchers such as Barker (2002b) and Brown (2007) who take the view that social enterprises need to be more entrepreneurial and to reconsider their legal structures in view of the changing macro-economic environment.

The emerging results summarised above are further discussed and analysed in the following sections. We start with a focus on the determinants of social enterprises' legal structures.

### **7.3. Determinants of legal structure**

As mentioned in Chapter 3, the hybrid framework of analysis, particularly through the IPE approach, made it possible to critically analyse the history and institutional foundations of social enterprises. Through the questionnaire survey discussed in the methodology chapter, self-defined social enterprises were scrutinised. A key objective was to identify the types of legal structures they had and the reasons behind their selection. Table 6.2 reveals a menu of legal structures of self-defined social enterprises in South Yorkshire. The purpose of the case study analysis was to identify and discuss the determinants of legal structure of these organisations. This revealed the determinants to be much more complex than previously recognised. The literature on this significant aspect of social enterprise development, as shown in Chapter 3, is over-simplistic and does not provide sufficient insight into this key component of social enterprise growth. Table 6.9 highlights the extra judicial issues that emerged from the case study analysis. These are central in guiding social enterprises when they are deciding which legal structure to adopt. It is clear that the literature on legal structures generally ignores the influence of endogenous factors such as ownership and remuneration of entrepreneurs that emerged from the case study analysis. For example, Gair (2005) suggests that selection of a legal structure is simply an administrative issue. Other researchers and influential social enterprise support organisations suggest that a social enterprise's choice of legal structure depends on its needs (SEL, 2003; Common Wealth Ventures, 2003; Ahmed et al, 2009; Alter, 2003). The findings emerging from this investigation shown in Table 6.10 and Figure 7.1 above, however, reveal the complexity around determinants of legal structure and their influence on the activities of social enterprises.

From the case study analysis, 'access to equity investments' and 'ownership of the business' were determinants of selecting a CLS legal structure. The impetus

therefore originated from both operational and personal motives as the results have shown. As the respondent from the Trainer said *'I am always looking at ways to develop this organisation - people have invested their money and I also need to put food on the table'*. Regarding the need to access equity investments, the case study analysis showed that the CLS legal vehicle enabled The Trainer and The Landscaper to widen their sources of finance and extract value beyond the traditional social economy. This legal vehicle, together with their entrepreneurial skills, resulted in healthy balance sheets as shown in Table 6.14. As previously noted researchers such as Battenheim (2002) and Dees (1998) argue that social enterprises' survival as businesses depends on their ability to extract value by interacting with stakeholders beyond their sector.

Maintaining ownership of the business was also a strong determinant of selecting a CLS legal structure. This enabled access to part of the surpluses generated by the social enterprise, as evidenced from the questionnaire survey and discussions in Chapter 6. Both entrepreneurs leading CLS social enterprises have invested their own financial resources in their respective organisations with the intention of maximising social value as well as benefiting from capital growth. This is consistent with observations made by Leadbeater (2002) that many traits and behaviours of successful social entrepreneurs mirror those shown in the for-profit sector. Although researchers such as Chell, (2007) and Pearce (2003) insist that social enterprises are established primarily to create social value, rather than to increase the personal wealth of those leading them, this investigation has revealed otherwise. We have shown that it is possible to achieve both individual and organisational objectives and still operate as a viable social enterprise.

The implications of the determinants 'access to equity investments' and 'ownership' for social enterprise growth are as follows. Firstly, they reveal the entrepreneurial outlook of those running The Trainer and The Cafe. They selected legal structures that had the potential to achieve and maintain viability for their organisations. As the respondent from the Trainer said *'I am a serial entrepreneur... I am always thinking of how this business can get better!'* This supports the contemporary perception that a social enterprise is essentially a firm, though one motivated by strong social objectives.

Secondly, ownership of project idea, remuneration and access to a portion of the profits or capital growth (for organisations and individuals alike) are fundamental

facets of enterprise. They are essential because they enable enterprise and commercial activity to flourish so that value is generated for stakeholders (Barker, 2002a; Parkinson, 2003). This is a key function that the CLS legal structure performs, which others, such as CLG, cannot do, as Chapter 2 discusses.

Moving on to the determinants of the CLG legal structure, Figure 7.1 shows that, 'access to funding' and 'influence of policy environment' emerged as strong determinants of the CLG legal structure, despite the latter also having some influence in CLS legal structures. The heavy reliance on grant funding demonstrated by The Community Champion and The Cafe meant that, for them, the pursuit of commercial opportunities was not a high priority. When asked how the organisation was going to recruit high calibre staff, the respondent from The Community Champion said '*Yes we are looking at employing people...but not paid positions... in a volunteer sort of way*'. For these organisations the selection of legal structure was influenced by their philanthropic objectives. They required a legal structure that assisted them to mobilise grant funding to support their social objectives. It was therefore inevitable that their activities would be supported by volunteer, rather than paid, staff given the lack of trading income. CLG legal status was sufficient for them to achieve their social objectives.

The case study analysis also showed that the prevailing policy paradigm had a profound influence on the types of legal structures those social enterprises select. Discussions in Section 6.4.1 show that, although this influenced all social enterprises being investigated, it appeared to have a stronger effect on those organisations that adopted the CLG legal status. This could be explained in part by the role that the central government was playing in the provision of financial support to address deprivation and exclusion. They were keen to support community led interventions to address socio-economic deprivation, rather than commercial organisations. Their funding criteria meant, as the analysis in Chapter 6 shows, that most applicants would select a legal status such as the CLG, which was compliant with the set criteria. Both The Community Champion and The Cafe acknowledged the influence of funders' requirements on their decision to select CLG legal status.

Determinants such as the policy environment and access to grant funding are more likely to influence the selection of legal vehicles such as the CLG, which reinforce the social ethos associated with social enterprises. This legal set up also permits communities to participate in the running of the organisations .Hence such legal

structures are associated with democratic governance models of social enterprise (Low, 2006).

The availability of expert legal and business advice was also influential in determining the specific type of legal structure as discussed in Chapter 6. The case study analysis showed that, in all cases, the process of selecting a legal structure was preceded by consultations with legal experts. The literature review, discussed in Chapter 3, revealed the advice available to social enterprise on legal structures to be severely limited (Carter, 2003). This was also evident in the responses to the questionnaire which indicated that there was a dearth of experts in the legal structures of social enterprise. This determinant, shaded in yellow in Figure 7.1, is common to both legal structures, as is 'social objectives'. Strong social objectives, as the analysis in Chapter 6 shows, enabled all the organisations under scrutiny to identify themselves as social enterprises. This is consistent with the philanthropic origins of social enterprises as discussed in Chapter 2. For example, by adopting CLG legal status, The Community Champion and The Cafe are affirming their intentions and social mission. They are also sending a message to both internal and external stakeholders about the work they are doing in tackling deprivation and exclusion in the communities they serve. This is evidenced in Chapter 2 where several researchers and academics such as Chell (2007) Pearce (2003) and Paton (2003) regard the achievement of social objectives as the driving force of social enterprise.

The influence of mission, discussed in Chapter 2 and Section 7.5, is to direct the work of social enterprises (Dees et al, 2001) towards the achievement of their social, economic and environmental objectives (Dart, 2004; SEL, 1999). According to Figure 7.1, if a social enterprise intends to pursue a predominantly commercial route then a CLS legal structure would be the most likely option. This was evident in the analyses of The Trainer and The Landscaper. As the respondent from the Landscaper remarked, *'we intended to be a business right from the start....I would like to see the company growing organically.....able to take advantages of various contracts across all sectors'*. This clearly shows a desire to develop a robust business model for the enterprise as well as to take advantage of mechanisms such as the CLS legal vehicle to achieve viability. This type of structure is shaded in green in Figure 7.1 and represents The Trainer and The Cafe. Although these organisations were guided by strong social objectives, their missions were underpinned by commercial objectives, hence the selection of this type of legal structure. On the other hand, a social

enterprise with a more philanthropic outlook such as The Community Champion is likely to opt for a CLG status as confirmed by the respondents in Section 6.4.2(1). This legal vehicle allows it to maximise extraction of value to achieve its social objectives.

Table 7.1 below further analyses the determinants of legal structure of social enterprises and how they influence the choice of legal structure. The analysis is empirically derived from observations made from quantitative data and case study interviews. For the purpose of analysis, the determinants of legal structure have been numbered from 1 to 6.

### **7.3.1 Determinants of legal structure and their functions**

**Table 7.1: Functionality of determinants of legal structures of social enterprise**

<b>Determinant</b>	<b>Purpose</b>
1. Ownership of business	<b>Functional</b>
2. Access to funding	
3. Access to equity	
4. Availability of legal advice	
5. Policy environment	<b>Normative</b>
6. Strong social objectives	

Table 7.1 Derived from case study analysis

The above table shows that we can divide these six determinants of social enterprises' legal structures into two categories, functional and normative, to illustrate the functions they play in the organisations' development.

#### **1. Functional determinants**

The first four shown above can be described as functional determinants of legal structure. They enable social enterprises to address the daily challenges of running a business as well as issues relating to the remuneration of those running the social enterprises or associated with them. The challenges include pressures from macro-

economic forces in an increasingly competitive global economic environment which no business can control (Arradon and Wyler, 2008). Consequently, social enterprises need to adapt to these changes in order to survive as businesses. This strategy, as seen in Chapter 3, is a core component of the BTF approach associated with researchers such as Cyert and March (1963). In the case study analysis, it was seen that the determinants 'ownership of business' and 'access to equity investments' strongly influenced The Trainer and The Landscaper to adopt CLS legal status. On the other hand, the need to access grant funding as well as availability of business and legal advice provided the impetus for The Community Champion and The Cafe to select CLG legal status.

Both CLG and CLS legal structures enabled the social enterprises under scrutiny to make that vital connection with communities they serve. This is reflected in their boards of governance which draw their membership from these communities, as discussed in Section 6.6. The determinants, irrespective of the type of legal structure they produce, are also being used as a lever to open opportunities for social enterprises to achieve either economic or social goals. This is a function of the board that Provan et al (1980) and Muth and Donaldson (1998) refer to as boundary spanning. In conclusion, therefore, the case study analysis shows that functionality influences the type of legal structure that a social enterprise or entrepreneur selects.

## ***2. Normative determinants***

The last two determinants shown in Table 7.1, namely 'policy environment' and 'strong social objectives' could be classified as normative determinants of legal structure. They are considered in this analysis to represent interventions both at policy and local levels aimed at addressing social injustices. Though constantly evolving, these determinants have been associated with the development of social enterprises as they emerged from the social economy. As we have seen, social enterprises emerged from social economy organisations that were established primarily to tackle socio-economic deprivation (Bridge et al, 2009; Salamon, 1994). This relationship between institutional interventions and welfare reform is discussed in depth in Chapter 2 drawing on the work of such researchers as Lindsey (2005), Gueslin (1987) and Moulaert and Ailenei (2005). In Chapter 5, it was shown that addressing deprivation and exclusion is central to government policy on social enterprises (Po-Hi, 2003; DTI, 2002; Schwartz, 2010). The case study analysis has shown that this policy thrust is influencing organisational design and legal structures

of social enterprises. These determinants therefore continue to affect the development of contemporary social enterprises in their efforts to address economic and social objectives.

The findings of this investigation therefore show that the decision to select a legal structure is not a straightforward administrative process. As previously noted, some authors such as Bridge et al (2009) are of the view that the legal structure is determined by the activities that the social enterprise is involved in. We also saw that others such as Ahmed et al (2004) suggest that most legal structures of social enterprises can be adapted to suit most purposes. The results of this investigation, however, show that there are broader issues to be considered, rendering the process of identifying a suitable legal structure quite a complicated undertaking. This supports the views of researchers such as Peattie and Morley (2008), Barker (2002b) and Brown (2002) that social enterprises' legal structures represent an area that is under-researched, yet vital for the development of the sector. The results of this investigation show that, irrespective of legal structure, social and moral issues underpin the activities of social enterprises and continue to be an integral element of their identity.

Having discussed the determinants and their influence on choice of legal structure, the next section focuses on how the type of legal structure influences the nature of governance and management of social enterprises. This is another theme the case study analysis identified as central to our understanding of how their legal structure influences social enterprises' operations.

#### **7.4 Governance of social enterprises and legal structure:**

One of the key elements of the hybrid framework outlined in Chapter 3 is that it allows us to critically analyse firms' governance, specifically through the contractual elements of the theory of the firm. The chapter also employs these theoretical lenses to scrutinise the governance of social enterprise. A typical social enterprise governance model involves social ownership with small groups of volunteers providing both strategic and operational management (Barker, 2003; SEL, 2003; Paton, 2003). This type of governance is referred to as the democratic model of governance and is closely associated with the historical and philanthropic origins of social enterprise. Given the drawbacks of such a governance model, some



researchers such as Low (2006), Low and Chinnock (2008), Spear et al (2007) and Mason et al (2006) suggest alternative governance models such as stewardship should be considered. We have seen how alternative corporate governance theoretical approaches such as Agency, Stewardship and Resource Dependency approaches can be applied to critically analyse the way social enterprises operate. Work associated with researchers such as Callen et al (2009), Miller-Millensen (2003), Low (2006) and Pfeffer (1973) provides insight into how social enterprises and other non-profit organisations are using their boards of directors to achieve organisational goals. Chapter 3 also discussed how social enterprise governance is increasingly shifting from the democratic to the stewardship model. Researchers are quick to point out that, although this model requires further exploration, it offers potential benefits such as access to other forms of finance such as equity investments. These arguments stem from the fact that social enterprises, like any other businesses, are operating in an environment susceptible to the effects of macro-economic change (Douglas, 2000; Cornforth, 1988). They therefore require governance models that will allow them to compete for resources in the market. To achieve this objective, Spear et al (2007) also stress the need for a suitable legal framework to drive the governance of these organisations.

Figure 7.1 provides a snapshot of the governance models of the social enterprises under investigation. The case study analysis revealed that the social enterprises with CLG legal structures are led by voluntary board members at both strategic and operational level. This type of governance is associated with the democratic or membership governance model and associated with the work of researchers such as Low (2006), Pearce (2003) and Paton (2003). The role of the boards of directors of The Café and The Community Champion was to represent the interests of their stakeholders and manage community assets and resources on their behalf (Iecovich, 2005). This is clearly consistent with the democratic governance model of social enterprise. It is also evident that the governance models of these cases do not show a clear separation of roles, observations also made by Low and Chinnock (2008) and Spear et al (2007). The board has a strong desire to control the organisation's staff and activities. Callen et al (2009) consider this to be the agency role that the board plays to protect the assets of the organisation. This controlling role may also be explained by the makeup of the boards of The Community Champion and The Café.

The power asymmetries and decision making within The Café and The Community Champion further exacerbates their functionality, transparency and efficiency. The

board members of both CLG and CLS organisations wield considerable power. They control funds, creating what Haberberg and Rieple (2001) refer to as a micro-political condition. For example the two board members of The Cafe donated the land and buildings to the social enterprise they are managing, giving them powerful vested interests in the organisation. Similarly the chairman of The Community Champion is its founding member and de facto managing director, volunteering five days a week at the organisation. He donated £17,179 to the organisation (The Community Champion Annual Report). The result of this has been the emergence of governance models in The Cafe and The Community Champion that McNulty and Pettigrew (1999) described as a minimalist board, run by individuals and small factions, with little or no conflict, challenge or dissent.

The failure to separate executive and operational roles in the governance of The Café and The Community Champion is compromising board functionality. This is a challenge which the board of The Community Champion acknowledged as discussed in Chapter 6. While the CLG legal structure allows these organisations to operate this way, it obviously casts doubt on their ability to develop vision in the wider context and to think strategically. This is one of the key reasons for failure of governance in social enterprises (Low and Chinnock, 2008). Research has revealed that more often than not, trustees and other non-executive members of boards of directors of such organisations lack the commitment or willingness required for social enterprises to operate in competitive markets (Lloyd, 2006; Barker, 2002b). This has been demonstrated in the analysis of social enterprises with CLG legal status. The Community Champion, for example, exhibits a clear failure to exploit the private sector skills of its manager to improve its operational efficiency. It appears that this manager, as noted in Section 6.6.2, was hired to instil a business culture in the organisation. The reverse however, occurred as he appears to have become a 'convert' to the voluntary sector. This was revealed by his views towards grant funding as a whole:

*'It was new to me that people would come and provide grants.....I came from an area which said that if you didn't deliver a service, no one would pay you'.*

This statement to some extent indicates a failure of the organisation to take advantage of the commercial skills and knowledge being imported into the organisation through boundary spanning, a key feature of the RDT approach as discussed in Chapter 3.

The governance of the organisations with CLS legal structures is distinctly different from those with CLG legal status. The role of their boards is limited to strategic formulation and advisory functions. Their senior managers act as CEOs and are provided with the autonomy to make operational decisions (Davis et al, 1997). Their CEOs chair board meetings and their respective boards recognise and respect their business expertise. This was confirmed by the respondent from The Trainer who said, *'I also chair board meetings and this also gives me a chance to discuss and new ideas with everyone on the board'*. This clearly shows that there are no conflicts between the board and top management. These are key features of the ST approach identified by researchers such as Donaldson and Davis (1991), Muth and Donaldson (1998), Pfeffer and Salancik (1978) as discussed in Chapter 3. Some members of the boards of The Trainer and The Landscaper are investors who have a stake in the assets and ownership through shareholding (Low, 2006). Such governance models resonate well with the arguments by Barker (2003), Smith (2005) and Ridley-Duff (2002a) who suggest that not all social enterprises need to have community/social ownership. In addition we can see an element of the RDT approach particularly in terms of boundary spanning. For example, The Landscaper was keen for the funder (The Key Fund) to purchase a stake in the organisation and sit on the board. This was a strategy to facilitate access to the resources and technical expertise of the funder's representative on the board. As the Landscaper informant said, *'Of course having a funder on the board is good thing...perhaps they will give us more money when they can see how well we are doing'*. The development of such multi-stakeholder boards in social enterprises reveals the need for innovation in order to meet the challenges of globalisation and other external influences (Salamon and Anheier, 1996; Bubb, 2007), in particular the need to adapt and widen sources of expertise, a significant feature of modern firms (de Kam, 2005; Bowen, 2007). The entrepreneurs and senior managers running these organisations are not volunteers but sustain their livelihoods from this work. They are able to do so because the share capital legal structure driving this type of governance model accommodates and aligns their personal ambitions with those of their respective organisations. This is also an important feature of the ST approach.

Innovation in governance models is also illustrated by how these share capital social enterprises maintain their social ethos and protect their assets and resources from abuse. For example a clause in the memorandum and articles of association of The Trainer says:

*Should the company ever be sold the value will be distributed in proportion to the distribution of shares without regard to whether A or B. A decision to sell the company must be approved by at least 80% of A shares and 80% of B shares.*

The A shares represent owners of the social enterprise while B shares include investors and social economy organisations who have voting power. This clause is significant in that it demonstrates a commitment by those involved in the organisation to ensure that it remains a social enterprise, despite its for-profit orientation.

#### **7.4.1 Summary of governance and legal structure**

The literature review has shown that social enterprise boards, as in any business, are responsible for directing the operations of their organisations in pursuit of their objectives. This requires competent individuals supported by suitable legal frameworks to address challenges faced by social enterprises as they compete in the market. The case study analysis showed contrasting governance and management models of social enterprise as well as the influence of legal structure on the functionality of the governance models. Overall, the case study analysis of the composition and roles of the boards of directors reveals that the type of governance model is predicated on the mission and needs of the social enterprise. Consequently, the legal structure driving the specific governance model enables the organisations to achieve their specific objectives. Enterprises with CLS legal structures have governance models that empower individuals in the organisations. The role of the board is restricted to activities such as strategy formulation, advising and recruitment, leaving top management to address operational issues. These are key features of the stewardship approach to governance which is a new trajectory that the social enterprise sector is exploring. This investigation has shown that moves towards this type of governance have been facilitated by a CLS legal structure. Researchers such as Low (2006) and Mason et al (2006) seek to explore this route further. The governance models of social enterprises with CLS legal structures reflect their need to adapt to the pressures of the external economic environment to remain viable. Opting for such governance models therefore implies acknowledgement of the weaknesses of democratic models of governance as well as a willingness to take risk. For enterprises with CLG status, it is evident that their governance model and related legal structures conform to the philanthropic ideology underpinning the concept of social enterprise, with a clear desire to protect assets of the organisation

on behalf of the community and an aversion to trading, observations shared by Pearce (2003) and Chell (2007).

The above discussions and analysis focussed on the determinants of legal structure, type of legal structure and the resultant governance model. In continuing our analysis, the next section discusses how the type of legal structure influences the ability of a social enterprise to mobilise financial resources and attain sustainability. This is one of the three themes identified at the beginning of this chapter as central to our understanding of social enterprise.

## **7.5 Economic sustainability and legal structure**

The hybrid framework of analysis, allows us to analyse social enterprises' motivations, particularly their desire to achieve financial sustainability while at the same time maintaining their social ethos. In Chapter 2, we saw that social enterprises make use of a variety of sources of finance to cover the costs of delivering services and products to the community. These include grants, donations, membership fees, trading and loans (Grenier, 2003). We also saw that grant funding is one of the most important sources of finance for social enterprises. Researchers such as Dyson (2003), however, argue that overdependence on grants is threatening the development of social enterprise. The literature review and the case study analysis show that the decline in grants available to social enterprises has not been accompanied by any decrease in the social needs of communities. It has therefore become imperative for social enterprises to look beyond the social economy for financial resources (Foster and Bradach, 1994; Favreau, 2000). A report by Barclays Bank (2007) confirms this development by casting doubt on the long term potential of philanthropic financial support for social enterprises. According to the report, wealthy philanthropists are now less influenced by emotion when giving. Instead they are increasingly strategic in their donations, a move that reduces the grant funding base for social enterprises. The dual challenge of reduced or restricted funding and the increasing demands to fulfil socio-economic objectives are forcing social entrepreneurs to devise innovative and creative strategies to achieve sustainability.

### ***7.5.1 CLS legal structure and financial sustainability***

Figure.8.1 shows that a share capital legal structure drives a governance model with a wider stakeholder base including external equity investors. Potentially this can

result in a wider income base, given the opportunities to extract value beyond the social economy this type of structure provides. This view is shared by Dees (1998b) who argues that diversifying the funding base and instilling market discipline are key success factors for non-profits. Our analysis has shown that The Trainer and The Landscaper adopted CLS legal structures to strengthen their resource mobilisation strategies. These organisations managed to secure additional financial support through loans and equity finance. Their financial position is confirmed in Table 6.12 which shows positive balance sheets and quick ratios as opposed to those with CLG legal status. As discussed in Chapter 6, evidence from interviews of support organisations shows that a viable business model with an appropriate legal structure makes it easier for social enterprises to attract external financial investments. By demonstrating positive cash flows and balance sheets, social enterprises with CLS legal structures improve their chances of attracting venture capitalists. We can see that the ability of a legal structure to function as an efficient vehicle for both sustainable enterprising ideas and delivery of social objectives was a key influence on the decision making process of these case studies, a view shared by Barker (2003).

The emergence of share capital legal structures in the social economy demonstrates innovation in strategies to achieve financial sustainability. The success of such social enterprises in attracting grant funding from statutory funding organisations is a significant development. It shows that this type of legal vehicle, which had previously been an object of suspicion, is becoming accepted within the social economy. The case study analysis in Chapter 6 showed that share capital legal structures have the approval of some social enterprise support organisations. A respondent from Bates, Wells & Braithwaite, a firm of solicitors that advises social enterprises, believes that share capital legal structures will be an asset for the sector. As she said, *'It allows equity investments. That is a real driver of commercial growth... just as it is a driver of the commercial economy it should be a driver of the social economy'*. She was also confident that the benefits the share capital legal structure offers social enterprise will eventually change people's perceptions towards it, saying, *'I think it [share capital] will become a vehicle for social ownership, and when people get a feeling that they are part of something, it will become much more valuable than financial return'*. However, as discussed in Section 6.4.1, a number of the respondents were unsure about share capital legal structures and their relevance to social enterprises. They argued that the CLS legal structure is alien to traditional social entrepreneurship and should not be used by social enterprises.

These statements signify the evolving nature of the social economy as it adapts to changes in the global economic environment. Chapters 2 and 3 discussed the relationship between social enterprises and the market and the gradual shift towards for-profit stewardship governance models in the social economy. The entry of the share capital legal structure to the social economy was encouraged by policy developments in the UK under the previous Labour government, especially the setting up of a risk capital fund for social enterprises. Only social enterprises with CLS legal structures could take advantage of such financial instruments. It would be impossible for social enterprises with CLG legal status, irrespective of their financial health, to be fully involved in such an initiative since they are not able to offer market returns on investments. However, as Chapter 2 discussed, fundamental difficulties persist regarding the investment readiness of social enterprises in competitive environments. Few would disagree that equity investment in social enterprise is 'problematic' as a market for selling the shares has not always been available. In addition there is scepticism about the ability of the social enterprise sector to give market rate returns (Jump, 2007).

The Bank of England's (2003) report on the financing of social enterprises noted that most are neither familiar with, nor well-informed about, equity investments. However our case study analysis showed the benefits of having a share capital legal structure. It was this structure that allowed The Trainer and The Landscaper to operate like conventional businesses in the market while at the same time retaining their social ethos. As the respondent from the Landscaper remarked, *'We had a choice to become a 100% private company, but we chose the social enterprises route.....we want to address issues in our community.....we are not guided by profits only'*. This is consistent with Martinson (2007) and Barker (2002b) who argue that non-profits need to operate on the same terms as conventional businesses. By issuing shares to investors in return for a stake in the organisation, they are comparable to commercial businesses, where shares are a mechanism for representing ownership and share of assets and wealth (Parkinson, 2003; Mason et al, 2006). Importantly, this development shows that, although it is essentially a firm, a social enterprise rejects the profit maximization approach of neoclassical economic theory associated with researchers such as Veblen (1924) and Coase (1960) and discussed in Chapter 3. Instead it seeks to maximize extraction and delivery of value to the communities it serves through enterprise.

The next discussion focuses on the CLS legal structure and its implications for the financial sustainability of social enterprises.

### **7.5.2 CLG legal structure and financial sustainability**

The case study analysis provides clear evidence that enterprises with CLG legal status have difficulties in building sustainable business models. Hence most of them rely heavily on grant funding and so are vulnerable to severe reductions in their income as Figure 8.1 shows. This is one of the dangers of an over reliance on grant funding, identified by (Case, 2005; Carter, 2003). The current predicament of enterprises in this category was summarised by a respondent from Yorkshire Forward, an RDA.

*'They [social enterprises] need to move away from grants.....to be less risk averse. I think there has to be a wholesale change of mindset'.*

The Cafe is a typical example of what the above respondent was referring to, being simply unable or unwilling to exploit available commercial opportunities. It shows a lackadaisical approach to running a business and the language its manager uses is hardly entrepreneurial either. When asked for additional documents such as minutes of board meetings and future operational plans of his organisation, his reply was rather astonishing;

*'The only computer we had packed up ages ago.....keeping documents is something that we have not been good at, but we are now much better'.*

This response shows the general lack of seriousness and understanding of the mechanics of business typical of some of the social enterprises with governance models characterised by shared ownership, an observation also made by Smith (2005). It is therefore not surprising that the case study organisations with CLG legal status are virtually insolvent, with negative balance sheets. The Community Champion, for example, is funded to deliver specific training courses and does not show any willingness to pursue substantial trading activities to generate revenue. It is therefore in a precariously vulnerable financial position as we have already seen. Its continued operation depends entirely on the availability of grant funding, a position confirmed by a respondent from this organisation. *'We have a 12 month funding period [to carry out training activities] and it stops in July 2007.'* Given that the



interview took place in February 2007, the organisation had only four months of funding left. This situation represents the stark reality of most social enterprises that are dependent on grant funding to cover the costs of delivering their interventions.

Similarly, The Cafe is experiencing operational problems due to over-reliance on grant funding and large numbers of unpaid staff. For example, when the researcher arrived at the premises for the first interview, the volunteer manager was working on his own. He said, *'sorry, the lady who was supposed to be here has phoned in sick...so thats only me today'*. This respondent was attending to the cafe and the shop on his own.

Technically therefore it is difficult to see how The Community Champion and The Cafe can be described as viable businesses, given the state of their balance sheets as discussed in preceding sections. They are trapped in what Case (2005) calls a perpetual supplicant model, with little prospects of evolving into fully grown businesses. As Figure 7.1 shows, their legal structures are unlikely to assist them in improving income and cash flows through trading. Over-reliance on grants, even for large capital projects as evidenced by both The Community Champion and The Cafe's expansion plans, has stifled creativity and innovation. This finding is consistent with the Bank of England's (2003) review on financing for social enterprises which found that most directors of social enterprises are reluctant to take on debt financing, a point illustrated clearly in this case study analysis. This highlights general problems associated with legal structures characterised by social ownership. As Smallbone et al (2001) and Barker (2003) argue, such legal structures severely limit social enterprises' ability to secure meaningful capital funds or to tender for large contracts which might require involvement of external strategic partners. The nature of the legal structure limits their financing options and prevents a more effective commercial relationship with private sector and other for-profit investors. CLG status, as Conaty and McGeehan (2000) argue, acts as a constitutional barrier to attracting equity finance, a vital financial alternative for organisations operating in competitive markets.

### **7.5.3 Sources of funding and economic sustainability summary**

This investigation has shown that CLG legal structures enabled the enterprises under scrutiny to secure grant funding from a number of sources to finance their operations. However, while this type of legal structure may enable these organisations to achieve

their social objectives, it is not conducive to attaining their economic objectives. This may be one of the reasons why the generation of trading income is given a low priority as evidenced by their poor balance sheets. This state of affairs is likely to lead to restrictions in income, as shown in Figure 7.1, since grant funding is now severely restricted in the sector (Flockhart, 2005; Cook, 2009). Their strong philanthropic mission arguably presents a moral hazard to such social enterprises. They are playing a social function and feel that they do not need to operate as efficient businesses, a perspective confirmed by their strong propensity for grant funding. Despite their reluctance to fully commercialise or strengthen their income generating capabilities, CLG legal status continues to enable social enterprises to be credible and effective avenues for channelling funding and support to communities and addressing various socio-economic issues at grassroots level. Their continued survival might be explained by the sweat equity provided by volunteers at no financial cost to them (Haberberg and Rieple, 2001; Strothotte and Wustenhagen 2005).

The analysis of enterprises with CLS legal structures reveals that by adopting this type of legal vehicle they intend to move towards a blended sustainable model. Such an approach provides them with the flexibility and capability to attract a wide range of financial resources, including equity finance, to further their social aims. Adopting this strategy provides opportunities to grow their capital and therefore reinforce their social ethos. This type of organisation challenges traditional views on social enterprises such as those of Paton (2003) and Pearce (2003) who argue that commercial activities should not be an integral component of social enterprise. These findings however show us that, contrary to such views, social enterprises have a symbiotic relationship with the markets. They have not totally rejected and abandoned the traditional discourse of for-profit enterprises. Importantly, this means that the current UK government's definition of a social enterprise no longer captures its true essence (Marshall and Lovatt, 2004).

However, the quest for sustainability requires careful consideration. Research suggests that social enterprises following the commercial route do not always succeed in their endeavours. Indeed McBrearty (2007) observed that most voluntary organisations, including social enterprises, struggle to build business while maintaining focus on their core mission. We saw this in Chapter 2 where the dangers associated with the commercialisation of social enterprises are discussed. Social enterprises risk compromising or losing their reputation and thereby becoming discredited (Etchart and Davis 2003, Warrell, 2007a and c). The enterprises with CLS

legal structures face similar challenges in balancing these objectives while under pressure from investors to generate more profits.

The next discussion summarises key issues emerging from this chapter.

## **7.6 Chapter summary**

This chapter analysed the results from Chapter 6, in the context of the hybrid theoretical framework discussed in Chapter 3. The information supporting the arguments in this chapter has been drawn from the multiple methods of data collection employed in this investigation. On the basis of the three analytical elements of the hybrid framework, three key issues emerge from the analysis in this chapter.

The theoretical lens of the BTF approach made it possible to analyse social enterprises as businesses operating in challenging multi-actor environments and simultaneously pursuing social and economic goals. Through this approach, we saw that it is vital for social enterprises to generate surpluses in order to remain viable and to support their social objectives. The case study analysis in Chapter 6 showed that they can no longer ignore the global economic environment and its effect on their operations. Just like conventional businesses, they have to be entrepreneurial and compete for market share and resources with organisations outside the social economy. They have to demonstrate that they can adapt to changes in the economic environment and are investment-ready to access financial resources. Most crucially, they require suitable infrastructure in the form of a legal structure that enhances their potential to access a wide range of resources and expertise beyond the social economy.

Through the IPE approach this thesis analysed the historical institutional foundation of social enterprises. The focus was on understanding the values and norms of social enterprises through the analysis of their legal structures. It was clear that these organisations require suitable legal structures to support their entrepreneurial endeavours. Selecting an appropriate legal structure for a social enterprise is a key part of the organisation's development as discussions in this chapter reveal. This investigation reveals however that the determinants of legal structure include a multiplicity of internal and external factors which had previously escaped academic scrutiny. The legal structure that these determinants create also influences the

governance of a social enterprise and ultimately its ability to achieve financial sustainability.

The hybrid framework of analysis, including agency, stewardship and resource dependency theoretical approaches, allowed us to critically analyse social enterprises' internal governance. There is evidence that the democratic form of governance associated with social enterprise remains relevant in the social economy. It still performs a vital function in supporting social enterprises in achieving their objectives. However, due to pressures for social enterprise to become more business-like, it is also clear that there is a gradual shift from democratic and participative models to more business-oriented models of governance, such as stewardship. This reflects the evolution of social enterprises as they adapt to changes in the external economic environment and increased demand for their services. The demise of traditional sources of funding for social enterprise has necessitated internal organisational redesign to assist in mobilising resources to achieve their social objectives.

The next chapter focuses on the conclusions and recommendations of this investigation.

## **CHAPTER 8: CONCLUSION AND RECOMMENDATIONS**

This chapter presents the conclusion and recommendations arising out of the investigation. This is done in the context of the work undertaken using the hybrid framework of analysis outlined in Chapter 3. The chapter is divided into two parts. The first revisits the research questions and highlights the key findings and this investigation's contribution to knowledge. The second presents the overall conclusions and recommendations and indicates further research necessary to strengthen our understanding of the social enterprise sector.

### **8.1 Addressing research questions and contributing to knowledge**

The chapter starts by looking at the research questions and demonstrating how they have been answered. Evidence is drawn from the archival research, descriptive statistics and in-depth case study analysis carried out in the course of this investigation. In providing answers to the research questions the thesis' contribution to knowledge is also highlighted. Based on the investigation undertaken this contribution to knowledge is reflected in two core areas, empirical and theoretical as discussed below.

### **8.2 Legal structures of social enterprises in South Yorkshire**

The first research question was: what are the different types of legal structures of social enterprises in South Yorkshire? Therefore the nature and type of legal structures of social enterprises across South Yorkshire were examined. Despite the increasing importance of social enterprises in the region and various previous mapping exercises, the discussions in Chapter 4 highlight the paucity of information on the nature of organisations describing themselves as social enterprises in South Yorkshire. This thesis contributes significantly to filling this gap in knowledge as shown below.

Chapter 2 discusses in detail the main types of legal structures being used by social enterprises in the UK and outlines the advantages and drawbacks of each, using information drawn mainly from secondary sources and archival data. This chapter

also draws our attention to a new legal structure for social enterprises in the UK known as the Community Interest Company (CIC). Significantly, the CIC gives a legal brand to social enterprise and addresses the shortcomings of traditional legal structures for social enterprises in assisting them to achieve their objectives. There has long been a perception that social enterprises are philanthropic and voluntary based organisations that seek to address mainly social objectives with only a limited propensity or need for trading activities. The discussion in Chapter 2 attributes this position to the historical origins of social enterprise, which emphasised social justice and a rejection of material gain. Hence, as the literature review shows, historically derived legal structures such as the IPS cooperative model and the CLG are still associated with social enterprise since these reinforce their social ethos. This chapter also introduces a new share capital model for social enterprises, NEWCO, introduced in Sheffield. As for the CIC, the emergence and acceptance of this legal structure signifies a new era in the evolution of the social economy, as social enterprises become more entrepreneurial and competitive in the market.

### **8.2.1 Contribution to knowledge**

Table 6.2 shows the types of legal structures of social enterprises in South Yorkshire. This information was empirically derived from the results of questionnaire returns from the extensive quantitative research undertaken across the unitary boroughs of South Yorkshire. This table reveals that among the sample of 102 self-defined social enterprises in South Yorkshire, there are three key types of legal structure, namely CLG, CLS-NEWCO and Cooperative (IPS). While the results confirm that the CLG legal structure is the most prevalent in the social enterprise sector, of particular importance and interest is the emergence of a share capital legal structure, previously unknown in the social economy. This was the precursor of the CIC share capital version launched by the Labour government in 2005 and is a new addition to the menu of legal structures commonly associated with the sector. This legal structure, though confined to Sheffield when this study was undertaken, signifies efforts in the social economy, not only to maximise the extraction and delivery of value, but also to facilitate business ownership and remuneration of entrepreneurs in the social economy.

We can conclude that the CLS legal structure illustrates that existing non-profit distribution legal structures of social enterprise are not entirely adequate. There is therefore a need to consider other frameworks that can serve the changing needs of

social enterprises. The social enterprise legal structure landscape is likely to continue to be characterised by the contemporaneous existence of both for-profit and non-profit distribution legal models, indicating that commercial orientation alone cannot address the most intractable problems in society. This investigation has illuminated these significant issues associated with social enterprise development in the UK and beyond, that have previously eluded intellectual and academic enquiry.

The next section discusses the second research question and emerging contributions to knowledge.

### **8.3 Determinants of legal structures of social enterprises in South Yorkshire**

The second research question was: what are the key determinants of social enterprises' legal structures? This investigation seeks to identify and understand these determinants, given the evident lack of conclusive information and consensus on this subject, a subject that has previously evaded critical analysis. Answering this research question has provided this thesis' most important theoretical contribution to knowledge.

In pursuit of this, Chapter 2 discusses and presents a detailed historical perspective on the emergence of the social economy and social enterprises. It is evident that, although the early forms of social economy organisations managed to acquire legal status, the literature does not fully explain the reasons behind the nature and implications of these legal structures. In addition, while contemporary discourse on social enterprises reveals a consensus among researchers on the types of legal structures of organisations in the social economy, there is no substantial academic and intellectual analysis on what exactly influences social enterprises to select specific legal structures. Only a handful of researchers such as Bridge et al (2009) and Lawrie (2002) have attempted to explain the reasons behind the selection of a legal structure. However, so far this work has not developed a comprehensive understanding of the determinants of social enterprises' legal structures. As a result there is insufficient information available on this area to inform policy on social enterprise. There is still a huge gap in knowledge on social enterprise development that this thesis has significantly contributed towards closing.

The rooting of this thesis in the hybrid framework of analysis provided a robust platform to scrutinise and understand both internal and external influences on social

enterprises' operational environment. This thesis has revealed that there are specific intrinsic and extrinsic elements crucial to the decision making process when social enterprises select their legal structures.

### ***8.3.1 Theoretical contribution to knowledge***

It was argued in this thesis that, despite increasing academic interest in social enterprises' legal structures, very little attention has been devoted to understanding what influences social enterprises in their choice of legal structure and how the chosen legal structure affects the enterprise's outcomes. The major contribution to theory is in the form of a typology of six key determinants of social enterprises' legal structures as illustrated in Table 7.1. These determinants were derived from the in-depth analysis of four case studies, descriptive statistics from questionnaire returns and qualitative data from interviews of key informants from social enterprise support organisations. These determinants are intricate and involve a number of interconnected endogenous and exogenous factors that have not previously been subject to critical academic analysis. Both the endogenous factors (such as the need for business ownership and access to profits) and the exogenous factors (such as the availability of funding and the prevailing policy paradigm) significantly influence a social enterprise's choice of legal structure. These factors have been neglected by researchers and academics as they were considered alien to the social economy due to their commercial connotations and implications. The particular legal structure which arises from these determinants exerts specific influences on the type of governance model a social enterprise adopts, as well as the organisation's ability to mobilise financial resources from different sources as summarised in Figure 7.1. This thesis clearly shows that those organisations with CLS legal structures have governance models that have been deliberately created to support their commercial activities. In contrast, those with CLG legal structures have governance models that are strongly influenced by the philanthropic origins of social enterprise to view trading as a secondary activity.

We can conclude that the reasons for a social enterprise's choice of legal structure are much more complex than previously appreciated. Contemporary discourse on this issue takes a simplistic view that suggests that selection of a legal structure is a mere administrative issue and that, largely, the needs of the social enterprise determine the type of legal structure that it adopts.



The next section focuses on the third research question.

#### **8.4. Influence of type of legal structure on outcomes of social enterprises**

The third research question was: in what ways does the nature and type of legal structure influence the outcomes of social enterprises? This investigation sought to ascertain the effects of different types of legal structures on social enterprises' operations. In particular the investigation wanted to ascertain whether there is a relationship between a social enterprise's particular legal structure and the way the enterprise seeks to achieve its outcomes

In order to understand the development and evolution of social enterprise, it is necessary to understand how the particular type of legal structure influences the way social enterprises operate and achieve their objectives. Table 2.3 shows a menu of social enterprise legal structures and what they allow the organisations to do. It is evident that, by their nature, social enterprises with legal structures characterised by common ownership, such as CLGs and IPS, can only attract specific forms of finance, mainly grant funding. They are severely restricted in their ability to access different forms of finance beyond the social economy. In contrast, social enterprises with CLS legal structures have flexibility that allows them to take advantage of loan, grant and equity finance. The multi-functionality of this type of legal structure is revealed in Chapter 6 which reports on an in-depth case study analysis of four enterprises, two with CLS structures and two with CLG. This analysis provides insight into the practical application of these two key legal structures and how they influence the operations of social enterprises. For example the CLG is found to remain an important legal vehicle in the social economy, allowing organisations to deliver a variety of interventions. The share capital model, however, demonstrates its potential to assist social enterprises in maximising extraction of value beyond the social economy.

##### **8.4.1 Contribution to knowledge**

This investigation has added to knowledge on how their legal structure influences social enterprises' development and operational environment as discussions in Chapters 6 and 7 have shown. Figure 7.1 summarises the empirically derived influences of type of legal structure on a social enterprise's operations. This is further illustrated in Table 6.12 which shows the financial health of the organisations under

scrutiny. This is not to say, however, that CLG legal status is synonymous with bankruptcy, as organisations with such a legal vehicle can still achieve their objectives through institutional financial support.

The organisations with this type of legal structure tend to rely heavily on grant funding as opposed to generated income. This has resulted in negative financial performance and short termism of interventions as shown in Chapters 6 and 7. In contrast, those with CLS were found to have robust business models and legal structures with the flexibility to allow them to mobilise different types of external resources to develop their service delivery capacity. They demonstrate investment-readiness which increases their ability to secure additional resources to improve the impact of their operations in the community. The multi-functionality of this type of legal structure provides opportunities to maximise extraction and delivery of value as the results in Chapter 6 and subsequent discussion in Chapter 7 reveal.

It is clear that the way a social enterprise is constituted impacts on its operations and outcomes. In other words there is a relationship between its type of legal structure and what a social enterprise does. We can conclude that the flexibility of its legal structure is critical in enabling a social enterprise to exploit commercial opportunities to generate revenue to support its social aims. This flexibility in its governance structure allows the organisation to lever in resources and key skills from a variety of sources both within and beyond the sector. Without this flexibility and innovation in legal structure, social enterprises will struggle to survive in a competitive environment.

## **8.5 Overall conclusions**

The overall conclusion is that their type of legal structure is vital in assisting social enterprises to achieve their objectives. It is essential to understand the determinants of legal structure and the resultant legal model they create as these influence the way a social enterprise attains its outcomes. This thesis has argued that there is a relationship between type of legal structure and outcomes. The thesis also concludes that a social enterprise's choice of a legal structure is largely driven by its operational needs, in other words its ability to function as a vehicle for enterprise as well as a tool for the extraction and delivery of social value. This investigation provides robust empirical evidence to identify the key determinants of social enterprises' legal structures, an important element of social enterprise development previously

overlooked by social economy practitioners and academics. In conclusion, the elements of the typology of determinants of social enterprises' legal structure developed by this thesis form a strong foundation to further advance theoretical work on the study of social enterprise in the UK and beyond. This addition to theoretical knowledge on social enterprise is significant and timely, given the evolution of the sector and current demands on social enterprises to deliver more services.

## **8.6 Recommendations**

Based on the above conclusions, we make the recommendations specified below. These recommendations have been split into three areas. Since this thesis focuses on self-defined social enterprises, these recommendations have significant implications for social enterprise policy and practice. It is suggested that a significant paradigm shift is necessary in terms of the nature and form of both institutional and infrastructural support available to such organisations.

### ***8.6.1 Understanding legal structures and governance of social enterprise***

The results of the investigation show that there is a need to challenge conventional wisdom on the development of contemporary social enterprises. It must be recognised that a social enterprise is a business that needs to compete and survive in the market. Developments within the global economy have increased the intensity of competition among businesses for resources and markets and social enterprises are no exception. They need to be innovative and adaptable in the way they operate to ensure the viability and sustainability of their activities.

Social enterprises therefore require appropriate mechanisms and infrastructure to enable them to engage with institutions outside the social economy so as to extract value for the communities they serve. It is therefore reasonable to conclude that the selection of a suitable legal structure is a major decision for a social enterprise. Most traditional legal structures of social enterprise, though suitable for mutual ventures, are insufficiently attractive to public sector or private sector partners who may wish to engage in activities that enable them to grow their own capital. Therefore we recommend consideration of other constitutional models that have not been fully explored such as share capital models. This legal structure offers the flexibility required by social enterprises to operate in competitive markets.

The results of the investigation have shown that it has become necessary to re-visit the contemporary understanding of the concept of social enterprise. The current UK definition of a social enterprise is:

*'primarily social objectives and whose surpluses are principally re-invested for that purpose in the business, or in the community, rather than being driven by the need to maximise profit for shareholders and owners' (DT 2002, p, 7)*

This definition of a social enterprise precludes surplus distribution and business ownership, elements which have emerged from this thesis as among the key current drivers of enterprise in the social economy. This investigation's findings therefore call for a revision of the UK definition of a social enterprise. It is evident that we now need a definition that recognises that social enterprises are competitive businesses and that the difference between them and for-profit businesses relates solely to their objects and aims.

The introduction of CLS legal structures to the social economy indicates the need to consider other legal frameworks that can serve the changing needs of social enterprises. While the share capital model may challenge the ideology underlying social economy organisations, this legal vehicle offers a realistic alternative to grant dependency. The flexibility and suitability of legal structures is critical in enabling social enterprises to exploit commercial opportunities to generate revenue to support their social aims. This flexibility should also extend to social enterprises' governance structures as they are critical in the leverage of resources and key skills from a variety of sources both within and beyond the sector. Without this flexibility and innovation in legal structure, social enterprises are not likely to survive in a competitive environment.

### **8.6.2 Researching social enterprise**

It is also clear that methodological issues of studying the establishment and development of social enterprises need to be re-evaluated. This study demonstrates the applicability and relevance of a mixed method approach to researching and scrutinising social enterprises. While quantitative analysis can indicate patterns in a phenomenon that we are researching and qualitative approach provides an insight into processes, further investigation through case studies is important in consolidating findings. A mixed method approach is recommended for researching

social enterprise because it allows complementarity. This allows us to better understand the complexity of the social enterprise sector.

### **8.6.3 Policy implications**

The practical implications of this work in light of the conclusions drawn above suggest that current policy on social enterprise development needs to be clarified. Social enterprise policy should demonstrate and reflect the nuanced and complex variations in social enterprise development and sustainability as discussed below.

#### **1. Legal structure for social enterprise**

There should be a specific legal structure that identifies an organisation as a social enterprise and facilitates extraction of value beyond the social economy without restrictions. The CLS legal structure discussed in this investigation offers a practical way of achieving this objective. Although the CIC was designed for this specific purpose current evidence, as discussed in this thesis, suggests that this legal vehicle has not been entirely successful. Of particular concern are the asset locks on the CIC that 'cap' dividends and therefore act as a deterrent to venture capitalists.

#### **2. Sector specific legal advice**

Policy responses should be targeted at the needs of contemporary social enterprise. The determinants of social enterprises' legal structures as identified in this investigation indicate that legal advice is essential for social enterprises when deciding on their legal structure. The complexity of these determinants means that, from a policy perspective, there must be dedicated legal support systems included in current support infrastructure available for social enterprise. The literature review revealed a lack of legal experts in social enterprise. Lack of knowledge and ignorance of legal structures are constraining and undermining social enterprises' performance and their ability to attain their objectives. This is becoming more apparent as the UK coalition government begins to dispose of public assets and invite bids from both private companies and social enterprises to purchase and utilise them. This will present significant challenges for social enterprises particularly in terms of affordable and sector specific legal advice.

## **8.7 Further questions and theoretical challenges**

The results of this investigation raise further questions for future research on social enterprise, important since the concept itself is constantly evolving. These issues do not undermine the arguments raised in this thesis. Rather they seek to complement the investigation and contribute to the development of the social enterprise sector. Continued research is essential for shaping future thinking, policy and practice within this evolving sector. These questions are as follows;

### **1. Can social enterprises survive in a capital constrained environment?**

This investigation has highlighted contextual economic environmental constraints associated with globalisation and economic recession. It is clear that contemporary social enterprises exist in a highly competitive environment where they have to operate as businesses to access the resources they need to support their social objectives. The demise of traditional funding sources means that the capital needs of social enterprises are no longer guaranteed. Consequently, they have to look for alternative sources of capital and compete for these with other sectors in the economy. Evidence in this thesis shows that funders are now more inclined to provide loan finance rather than traditional grant funding because of their desire to grow their own capital. Social enterprises now have to prove that they are more entrepreneurial and investment-ready to access these new financial resources. These resources however are now more restricted and competitive due to the adverse economic environment. Some social enterprises are changing their legal structures to be more business-like in order to achieve their objectives. If they do so, are they guaranteed success in mobilising required financial resources in subdued markets while at the same time retaining their social credibility?

Key to social enterprises' success in achieving their objectives in capital constrained environments are personnel with the requisite business acumen to lead these enterprises. Given the well known difficulties that social economy organisations experience in attracting and retaining suitably experienced personnel, new strategies are required to address these issues. This might entail exploring potential links between the private sector and social enterprise to increase the flow of expertise into social enterprise. But this might lead to an overemphasis on trading activities to attract the interests of external resource providers, at the expense of achieving the

social goals which are the main reason for a social enterprise's existence. These are key areas for future research in this area.

## **2. Can share capital social enterprises successfully manage an extended stakeholder interest?**

The results of this investigation highlight the importance of internal organisational governance systems in assisting social enterprises to achieve their objectives. We have shown that social enterprises' governance models are evolving away from the democratic and participative models that have a long history with non-profit organisations. There is now evidence that social enterprises are considering alternative governance models such as stewardship and resource dependency approaches. The boards of directors of some social enterprises include stakeholders who have invested their own financial resources for financial gain. An important new challenge for social enterprise is to manage these stakeholders and their expectations, while at the same time ensuring that there is no mission drift, overreaching of management capacity or loss of autonomy. Such governance models can put extra demands on social enterprise boards and managers. In addition they have implications for the skills required by managers who must run social enterprise as well as manage an extended stakeholder portfolio. This becomes a contested area, given that traditional governance models have been characterised by bureaucratic participative approaches to decision making. These issues require further exploration and research.

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## Appendix 1

### University of Huddersfield Business School Social enterprise mapping questionnaire

This questionnaire is part of a larger research project that is looking into social enterprises in the South Yorkshire region. Walter Mswaka is conducting this study as part of a research degree programme at the University of Huddersfield. The aim of the study is to characterise social enterprises in South Yorkshire and how they operate. The overall objective is to establish some of the critical factors affecting their growth and sustainability. The responses you give to these questions will be treated in the strictest of confidence. None of the materials will directly identify individual project's respondents, unless where a specific request has been made and written consent given.

#### **Section A: Patterns and characteristics of social enterprises in South Yorkshire**

**Name:** .....

**Name of organisation:**.....

**Job Title:**.....

**Telephone No:**.....

**Contact Address:**.....

#### **How do you describe your organisation?**

**(Please tick any that are applicable)**

Social enterprise ☐

private, profit making enterprise ☐

Community organisation ☐

Other, please explain.

.....

#### **How long has your organisation been in existence?**

< a year ☐

2 – 4 years ☐

4 -6 years ☐

> 6 years ☐

.....

#### **3. How many people are employed by your organisation?**

Full time.....

Part time..... Voluntary staff.....

.....

#### **4. Do you have a legal structure/constitution?**

Yes ☐

No ☐

.....

#### **5. If yes, what type of a constitution do you have?**

Limited by guarantee ☐

share capital ☐ Share capital Community of Interest

Company (CIC) ☐

Co-operative/IPS ☐

Others: Please explain:

#### **6. Are you also a registered charity?**

Yes ☐

No ☐

.....

#### **7. What are/were the reasons behind your choice of constitution?**

☐ **Ability to attract external equity**

- ☐ Retain ownership/control of the organisation
- ☐ To attract grant funding
- ☐ It is the only constitution we are aware of

Other reasons, please explain:.....

.....

**8. How is the social enterprise managed?**

- ☐ Voluntary board of directors/trustees and voluntary staff
- ☐ Paid board of directors/trustees and staff
- ☐ Manager/main entrepreneur
- ☐ Development staff

Other management structure, please explain:

.....

9. How does your organization generate its income?

- 100% grant funded ☐ Both grant and trading activities ☐
- 100% Trading activities ☐ 100% Contracting ☐

Other means, please explain;.....

.....

10. If income is from both grant and trading activities, can you quantify;

Proportion of grant funding:.....%

Proportion of trading activities:.....%

.....

**11. What is your organisation's annual turnover?**

- <£10,000 ☐ £10,000 - £30,000 ☐
- £31,000 -£60,000 ☐ >£61,000 ☐

Section B: Issues, prospects and policies affecting social enterprises

12. What are your organization's financial objectives?

Please explain below.

13. Do you consider your organization to be achieving its financial objectives?

Yes ☐ No ☐

14. If not, what is preventing you from achieving these objectives?

Please explain below.

.....

What are your organization's social objectives?

Please explain below.

16. Do you consider your organization to be achieving its social objectives?

Yes ☐

No ☐

.....

17. If not, what is preventing you from achieving these objectives?

**(Please tick any that are applicable and explain in the spaces provided)**

☐ Appropriateness of constitution/legal structure

**Please explain:**

☐ lack of customers

**Please explain:**

☐ Funding

**Please explain:**

☐ Staffing

**Please explain:**

☐ Premises

**Please explain:**

☐ Management problems

**Please explain:**

Others, please explain

.....

18. Which of these, do you consider to be the most critical?

**(Please put them in order of importance, using a scale of 1, as the most critical and 6 least critical,**

☐ Appropriateness of constitution/legal structure

☐ Lack of customers

☐ Funding

☐ Staffing

☐ Premises

☐ Management problems

.....

19. If problems are associated with your current constitution, what action are you considering and why?

**(Please tick any that are applicable and explain, in the spaces provided)**

☐ Altering the rulebook and re-evaluation of your organisation's aims and objects

Please explain

☐ Changing current constitution to attract external equity

**Please explain**

☐ Changing current constitution to retain ownership and influence decision-making

**Please explain**

☐ Changing current constitution to remunerate directors

**Please explain**

Other Changes, please explain

.....

20 .Are you aware of any social enterprise support organizations in South Yorkshire, or with your specific region?

**Yes** ☐

**No** ☐

.....

21 .If yes, which organizations specified in the table below are you using or intending to contact? Using ticks please indicate types of services or support, you are receiving, or seeking in the spaces provided.

*Feel free to add other organizations that you are working with or intending to contact, not mentioned, in the table*

Types of services/support

Organization	Business planning	Capital funding	Revenue funding	Legal structures	Premises	Procurement	Marketing
South Yorkshire key Fund for Social Economy							
Barnsley Social enterprise Agency							
Social Enterprise Doncaster							
<b>Phoenix Enterprises (Rotherham)</b>							
Business Link, South Yorkshire							



South Yorkshire Investment Fund							
Sheffield community enterprise development unit, (SCEDU)							
Others							

22. Do you think that the operating environment for social enterprises in South Yorkshire is conducive for growth and sustainability?

Yes ☐ No ☐

.....

23. From the list below, which of these issues do you think need to be addressed?  
(Please tick any that are applicable and give reasons for your answer in the spaces provided)

☐ Legal/legislative environment

**Please explain**

☐ Availability of financial support

**Please explain**

☐ Availability of business advice and technical support

**Please explain**

☐ Attitudes of other entrepreneurs towards social enterprises

**Please explain**

Others please explain

Thank you for taking time to complete this questionnaire. Please return it in the pre-paid envelope provided, as soon as you can. For further information, please contact Walter Mswaka (SCEDU), on 0114 2015263

Appendix 2: South Yorkshire Support Organisations Interview Guide  
University of Huddersfield Business School  
Social enterprise support organisations' interview guide

This questionnaire is part of a larger research project that is looking into social enterprises in the South Yorkshire region. Walter Mswaka is conducting this study as part of a research degree programme at the University of Huddersfield. The aim of the study is to characterise social enterprises in South Yorkshire and how they operate. The overall objective is to establish some of the critical factors affecting their growth and sustainability. The responses you give to these questions will be treated in the strictest of confidence. None of the materials will directly identify individual project's respondents, unless where a specific request has been made and written consent given.

**Name:** .....

**Name of organisation:**.....

**Job Title:**.....

**Telephone No:**.....

**Contact Address:**.....

1. Can you tell me about what your organisation does and how your work relates to social enterprises?

2. What is your view of the operating environment for social enterprises in the UK, in general, and specifically, in South Yorkshire?

3. What type of support do you offer to organisations?

4. What criteria do you use for determining level and type of support?

**5. What do you think about the recent policy evolution in the social enterprise sector, particularly legal structures e.g. Community of Interest Companies (CICs) and share capital companies?**

6. What do you think about social enterprises structured as share capital companies?

7. What do you think about issues relating to ownership of social enterprises and governance? Do these affect the support you provide in any way?

8. Do you think that social enterprises have made a difference in tackling issues like socio-economic deprivation and exclusion?

9. What do you think could be done to enhance operational effectiveness of social enterprises?

Appendix 3  
University of Huddersfield Business School  
Social enterprise support organisations' interview guide 2

This questionnaire is part of a larger research project that is looking into social enterprises in the South Yorkshire region. Walter Mswaka is conducting this study as part of a research degree programme at the University of Huddersfield. The aim of the study is to characterise social enterprises in South Yorkshire and how they operate. The overall objective is to establish some of the critical factors affecting their growth and sustainability. The responses you give to these questions will be treated in the strictest of confidence. None of the materials will directly identify individual project's respondents, unless where a specific request has been made and written consent given.

Name: .....

Name of organisation:.....

Job Title:.....

Telephone No:.....

Contact Address:.....

**1. Can we discuss about what your organisation does and how this relates to social enterprises? What are your current priority areas?**

**2. What type of products/ services do you offer to organisations?**

**3. What criteria do you use for determining level and type of support?**

4. How many social enterprises/voluntary sector organisations do you support/represent?

5. What do you think about the recent policy evolution in the social enterprise sector, particularly legal structures e.g. Community of Interest Companies (CICs) and introduction of equity shares?

6. Does the nature of the legal structure of an organisation have an effect on the support you provide? If so, in what way?

7. What challenges do you think your organisation faces in promoting the establishment and growth of social enterprises?

**8. What is your view of the operating environment for social enterprises in the UK in general?**

**9. Do you think that social enterprises have made a difference in tackling issues like socio- economic deprivation and exclusion?**

**10. What do you think could be done to enhance operational effectiveness of social enterprises?**

Appendix 4-Case study interview guide  
University of Huddersfield Business School  
Case study interview guide

This questionnaire is part of a larger research project that is looking into social enterprises in the South Yorkshire region. Walter Mswaka is conducting this study as part of a research degree programme at the University of Huddersfield. The aim of the study is to characterise social enterprises in South Yorkshire and how they operate. The overall objective is to establish some of the critical factors affecting their growth and sustainability. The responses you give to these questions will be treated in the strictest of confidence. None of the materials will directly identify individual project's respondents, unless where a specific request has been made and written consent given.

**Name:** .....

**Name of organisation:**.....

**Job Title:**.....

**Telephone No:**.....

**Contact Address:**.....

**1. Background and history**

When was your organisation set up and for what purpose?

**2. Constitution/legal structure**

Can we discuss about;

The type of constitution/legal structure that your organisation has

The impetus behind choice of structure

Did you consider other structures?

If yes, why did you discount them?

**3. Objectives**

What are the social objectives of your organisation?

What are the economic objectives?

Do you consider yourself to be achieving your social and economic objectives?

**4. Mission statement**

Can you describe the mission statement/goal of your organisation?

**5. Management structure**

Can you describe your organisation's management structure and the decision making process? (Roles between Boards of directors, shareholders and operational staff)

Who is involved in the management of the organisation?

## **6. Employees**

How many part time/full time employees does your organisation have?

## **7. Products/services**

What services or products does your organisation offer?

Who is your main target market?

What are your future plans?

Who are your competitors?

## **8. Banking and investments**

Who do you bank with; mainstream/social /ethical bank?

Have you accessed further investments and for what reasons?

If yes, what was the nature of these investments and how were they secured?

## **9. Turnover**

What is the turnover of your organisation?

If this includes grant funding and generated income, how is this split?

Does your organisation have audited accounts?

## **10. Impact of your organisation**

Have you evaluated socio economic environment of your organisations activities?

If yes, how did you do this? (Social accounting and other evaluation techniques?)

#### Appendix 5: Example of a case study interview

The Cafe, based in Doncaster, presents an example of how the interviews were generally undertaken and highlights some of the challenges faced by the researcher. The first visit to this social enterprise took place on Wednesday 10 January 2007 at 11 am.

The Cafe is situated in Fishlake, a quiet and conservative area of Doncaster. An appointment was made with the manager by phone, a week before the interview took place. The manager initially asked the researcher to email him, in advance of the meeting, a list of the questions he wanted to ask. Once this was done, the date and time of the interview was confirmed by phone. The manager had a rather unusual position in the organisation. In addition to being the manager, he was also the owner of the premises from which the social enterprise operated, as well as being a member of the management board.

The researcher used his own vehicle to drive to the organisation's premises which included a restaurant, a shop and a bed and breakfast with conference facilities. After exchanging pleasantries, the manager initially seemed quite keen to participate in the research and was genuinely interested in advertising his organisation. The interview took place in the restaurant. The manager warned the researcher that he was the only staff member on duty on that day, since the other two full time staff had phoned in sick. He therefore apologised in advance that he would be interrupting the interview to serve customers in the restaurant.

After ten minutes of the interview, the manager seemed tense and was providing long winded answers. The interview took about three hours with several interruptions from customers needing to be served. At one point a busload of local disabled youths came in to the restaurant to buy food and the manager had to attend to them for half an hour. This gave the researcher an opportunity to wander around the premises and see how the organisation was set up. He was also able to talk to two customers who were waiting to be served. He wanted to find out if they had a particular reason for visiting the restaurant and whether they knew that it was a social enterprise.

The second visit to the premises took place on 18 January 2007 to collect documents such as business plans and advertising materials. The manager could not provide sufficient information on the first visit because, as he admitted, his organisation was not good at keeping records. On the second visit and in subsequent emails and phone calls the manager was more relaxed and was happy to provide confidential information such as bank balances.

Appendix 6:  
List of the archival documents located and analysed

HM Treasury The Future role of the Third Sector in Social and Economic regeneration-Interim Report,6 December,2006

IPSEYH: Investment Plan for Social Enterprises in Yorkshire and the Humber 2004

Labour Party Manifesto (1997) Britain will be better with new labour

Labour Party Manifesto (2001) Ambitions for Britain. Labour Party London.

Labour Party Manifesto (2005) Britain forward not back

Economics Foundation (NEF) Report on social enterprises and co-operatives

Parliamentary select and audit committee reports on social enterprises

Sheffield Star (2003) Ethnic Minorities Deliver Goods, Sheffield Star

Sheffield Star (2004) Opportunities for social enterprise: <http://www.thestar.co.uk>. Accessed, January 2007.

Sheffield City Council (2003) Expanding opportunities for social enterprise through public procurement 25 June, 2003.

The Institute of Public Policy Research (IPPR) (2005) Co-operative social enterprise and its potential in public service delivery (Co-operatives UK/Co-operative Action Ltd/Institute for Public Policy

Yorkshire Forward (2005) Sustainable Future, Sustainable Development News from

Yorkshire Forward (2005) Why Yorkshire, facts and figures.

Yorkshire Post (2006) Yorkshire hit by 40% increase in gun crime, 27 January, 2006.

Yorkshire and Humber Plan (2005) Draft for Public Consultation, December, 2005.

Appendix 7  
Categorisation of case study information

<b>Information</b>	<b>Case study 1</b>	<b>Case study 2</b>	<b>Case study 3</b>	<b>Case study 4</b>
<b>Business plan</b>	3 year plan: 2005 -08	2 year plan: 2003- 05. Current business plan in draft form	Up to 2006	January 2007
<b>Mission statement</b>	Yes	Yes,	Yes	yes
<b>Feasibility reports</b>	Yes Feb 2003	Yes	Unavailable	Yes
<b>Financial statements</b>	Cash flow statements- including expenditure schedules	1.Audited accounts (1/6/04 -31/5/05  2.Accounts 29/5/03 – 29/5/04  3.Change of accounting reference 225 (27/6/05)		1.Abbreviated Accounts 30/6/2003  2.Abbreviated Accounts 30/6/2004 3.Abbreviated Accounts 30/6/2005  4.Change of accounting reference 225 (2/5/03)
	Not available			Key Fund Doncaster CVS
<b>Funding/investment applications</b>	SCEDU Key fund	SCEDU (£5k) KF (both 2003)	Key Fund Doncaster CVS	Key Fund Doncaster CVS
<b>Type of legal structure</b>	Share capital  Certificate of incorporation provided  Checked and confirmed with companies house register Copy obtained	Share capital (NEWCO) No. 4780228	Company Limited by guarantee No. 5336960	Company limited by guarantee – with charitable status No.4349742
<b>Memorandum and articles of association</b>	Copy obtained	Copy seen	Copy obtained	Copy obtained
<b>Directors/trustees current appointments</b>		Current appointments report 24/1/2007	Current appointments report 24/1/2007	Current appointments report 24/1/2007
<b>Funding applications/schemes</b>	£5kfromSCEDU for Taxi project  £30K to KF (seen)	Start up funding from SCEDU including incorporation £5k Key fund application for grant, loan and investment£24547 unavailable	1 x eco lottery fundraising form	Yes – KF Got sight of application  Doncaster CVS £5k for business plan Got sight of board minutes
<b>Minutes of meetings relating to incorporation</b>	Got sight of board minutes		No (organisation lost all minutes when computer broke down	



<b>Recorded interviews</b>	Yes	yes	Yes	Yes
<b>Newspaper cuttings</b>	Sheffield star – August 25 2005 (launch article) Burngreave messenger 11/2005 Sheffield star Feb. 3 2006 16/1/2006 Burngreave business awards Hakim Wais- Star 10/10/2003 Ethnic minorities deliver goods 25/5/2005 Hakim(Drivers training) 11/3/2003 launching NETT	no	Several	Star 2 June 1993
<b>Advertising materials</b>	2 x brochures Complimentary slip Business card Web express guide advert	2x brochures  1x log fuel brochure	Doncaster conference venues advertising website 2x brochures 1x menu advert	1x brochure

Appendix 8: Funder's application form

**NAME OF APPLICANT ORGANISATION:**

**TITLE OF PROJECT: Capacity Building**

**PROJECT VALUE.....£10,000.....** (including match funding)

**GATEWAY CRITERIA**

Criteria	<i>Demonstration of application of criteria</i>
Economic Criteria to the Community of Benefit	
Immediate economic benefit to the community of benefit, including retaining wealth in the local economy.	
Drawing investment into the local economy.	
Local employment.	
Local purchasing.	
Providing a service or facility that would otherwise not be available.	
Acting as a catalyst for the development of further economic activity.	
Social Criteria to the Community of Benefit	
Promoting access.	
Commitment to training.	
Providing a social or community-based role model (a "community champion").	
Promotion of social cohesion.	

Nature of Ownership	Ranking	Applicants Comments
Stewardship/ either no capital distribution or for specified social purposes only.		
Trusteeship/ either no capital distribution or for specified social purposes only.		
Wide Membership/limited provisions for capital distribution to individuals.		
Close Membership/wide provisions for capital distribution to individuals.	3.	
Sole Membership or full capital distribution.	4.	

## **1. Description of work to be carried out**

**1.1** Please explain exactly what work you are applying for funds to do. Also identify what work you have done on this project to date.

Market Analysis:

Project Outcomes:

## **1.4 Risk Assessment**

Details of main risks affecting project	Likelihood of risk/threat	Consequence of risk/threat	Steps to be undertaken to minimise and mitigate risk
i)Lack of computers	likely	Lack of service to users/failure of centre	Secure funding for the purchase of computers
ii) no match funding	unlikely	Shortfall of budget	To secure loan to start the provision
iii)			
iv)			

**1.5** Timetable or activity plan. (the table below is only a guide)

Action/Activity	Start Date	Completion Date	Person responsible

## **2. Contact Details**

## **3. Details of organisation**

Describe your organisation's broad history and aims.

## **4. Why are you applying to Sheffield Enterprise Clusters?**

## **5. What effect will this project have on other social or commercial enterprises?**

## **6. How will you manage this project?**

Please tell us who will manage your project, what their relevant skills are, what support they have available (internally and from other sources), what relevant skills are available within your organisation, and what skills you know you will need to bring in.

## **7. Cost of the proposal**

Please itemise the costs if possible. Tell us how much matched funding (in cash or in kind) you expect. We will only fund projects that can bring in at least 50% match in cash or in kind

## **8. Allocation of costs across the budget heads**

## **9. Planned expenditure & evidence profile**

Tell us when you plan to spend money, when you plan to claim it and what evidence will be produced to substantiate the work completed to date. This will enable us to plan our cash-flow and keep our funders happy.

## **10. Tendering arrangements**

## **11. Outputs to be delivered for the project**

(Please add your own categories of outputs or outcomes if appropriate.)

OUTPUT / OUTCOME	NUMBER	DESCRIPTION & EVIDENCE TO BE PRODUCED
Network initiatives		
Businesses assisted		
Research projects (feasibility studies)		
Permanent jobs		
Permanent jobs safeguarded		
Learning Opportunities		
Social enterprise start ups		

**NAME:**

**SIGNATURE:**

**DATE:**

Please return the completed form to your nominated Enterprise Agent at Sheffield Enterprise Clusters, 41 Southey Avenue, Sheffield S5 7NN, or 131 Upperthorpe Road, Sheffield, England S6 3EB