In Confidence

Office of the Minister for the Community and Voluntary Sector

Chair
Cabinet Social Policy Committee

GROWING THE SOCIAL AND ECONOMIC POTENTIAL OF SOCIAL ENTERPRISE

Proposal

1. This paper proposes a Government position statement on social enterprise, and notes my intention to provide Vote Internal Affairs community grant funding to support social enterprise development. The Government position statement aims to encourage private sector and government agency responses to social enterprise development needs, which will assist growth in this highly innovative and community orientated sector.

Executive Summary

2. My community and voluntary sector responsibilities give me a strong interest in new approaches to building strong, resilient communities. The social enterprise sector has the potential to add significant social, environmental and economic value to local communities, and to contribute to government goals that rely on third party delivery.

3. Social enterprises are organisations with social or environmental goals, which use commercial methods to generate income. Despite increasing interest in this sector, emerging social enterprises face a range of barriers, centred on the need for developmental advice and funding tailored to their hybrid nature. The market is responding to a degree but a solid support infrastructure is lacking. Building social enterprise capability would help social enterprises to scale-up and attract investment.

4. I propose a Government position statement on social enterprise that acknowledges the potential contribution of social enterprise to social, environmental and economic goals, recognises development barriers, and indicates that government is willing to collaborate on sector development. The statement aims to encourage private and philanthropic funding, and government agency responsiveness to social enterprise. I propose to publicly release this statement, together with an announcement of a funding contribution to two social enterprise capability-building initiatives.

5. The two initiatives will be delivered by the Hikurangi Foundation, which currently incubates 15 social enterprises, and is a highly regarded player in the nascent social enterprise sector. The first initiative is a social enterprise accelerator pilot involving regional workshops from which 10 initiatives will be picked for intense support. A one-off grant of $0.146 million in 2013/14 will be provided subject to confirmation of matching private sector co-funding. I also intend to kick-start a national social enterprise incubation and development service by reprioritising baseline funding of $0.375 million in 2013/14 and $0.750 million in 2014/15.
6. Both initiatives will be funded from the Vote Internal Affairs’ Community Development Scheme (CDS), which is a category within the Community Funding Schemes multi-category appropriation. Funding for social enterprise development in outyears will be determined based on initial progress and further assessment of funding availability within baselines. Quantitative data, and an independent qualitative evaluation, will be required for both initiatives.

7. I propose to report back to the Cabinet Social Policy Committee in late 2014 on progress with the accelerator and incubation initiatives, and on cross-Government activity that gives effect to the government position statement on social enterprise.

The nature and value of social enterprise

8. Activity within communities to tackle economic, environmental and social challenges through “social enterprises” is increasing. As shown in Figure 1, social enterprises are hybrid organisations that mix social and economic goals.

Figure 1: The social enterprise hybrid

<table>
<thead>
<tr>
<th>NON-PROFIT ORGANISATIONS</th>
<th>SOCIAL ENTERPRISES</th>
<th>FOR-PROFIT COMPANIES</th>
</tr>
</thead>
<tbody>
<tr>
<td>Primary focus:</td>
<td>Primary focus:</td>
<td>Primary focus:</td>
</tr>
<tr>
<td>Social/environmental goals</td>
<td>Social and</td>
<td>Private financial profit</td>
</tr>
<tr>
<td>Private gain prohibited</td>
<td>environmental goals</td>
<td>through trading</td>
</tr>
<tr>
<td>Qualify for tax exemptions if purposes are charitable</td>
<td>Commercial methods</td>
<td>Able to pay return on investment</td>
</tr>
<tr>
<td>Mainly reliant on grants, fundraising, government contracts</td>
<td>Majority of surplus is reinvested in the social mission</td>
<td>Ineligible for charitable tax exemptions and grants</td>
</tr>
<tr>
<td></td>
<td></td>
<td>May have some social responsibility activities</td>
</tr>
</tbody>
</table>

9. Many social enterprises are structured as charitable trust boards or incorporated societies. While it is not unusual for non-profit organisations to sell goods and services, the desire for financial independence and innovation is motivating increased commercial activity. When trading becomes significant (for instance, 50 per cent of income) non-profit organisations may be considered social enterprises. Non-profit organisations often set up separate trading arms or purchase existing businesses which return surpluses to the parent body.

10. Other social enterprises are structured as limited liability companies with social/environmental goals at the heart of their missions. Their constitutions may stipulate that profit maximisation is to be balanced by ‘social good’ objectives. Many of the newer social enterprises, led by entrepreneurial (often young) people, are structured as companies, and in some cases as co-operatives.

11. Some social enterprise examples are:

- Rekindle (Christchurch) employs young people to make furniture from waste wood;
- Youthline Manukau has set up a community café in a restored fire truck;
- Harbour Co-operative (Lyttelton) provides food through a member-run store;
- the Community Business and Environment Centre (Kaitaia) operates a range of businesses and environmental programmes; and
• the Enspiral hub (Wellington) is a co-working space for innovative social enterprises, many of which harness new technology to achieve their goals.

12. The benefits of social enterprise are outlined in Figure 2. These include the potential to tackle social and environmental issues, grow local economies, mobilise talent and entrepreneurship, and create employment.

Figure 2: Benefits of social enterprise

<table>
<thead>
<tr>
<th>Innovative approaches to social/environmental concerns</th>
<th>Financial sustainability</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Apply business acumen to projects tackling social or environmental needs.</td>
<td>• Derive income from sales and attracting loans and investment, with minimal or no reliance on government funding.</td>
</tr>
<tr>
<td>• Are open to innovative contracting and payment methods.</td>
<td></td>
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</tbody>
</table>

<table>
<thead>
<tr>
<th>Encouraging ethical markets</th>
<th>Economic productivity</th>
</tr>
</thead>
<tbody>
<tr>
<td>• Respond to investor interest in ethical investment.</td>
<td>• Attract entrepreneurs with the ability to scale up ideas and contribute to the economy.</td>
</tr>
<tr>
<td>• Adopt and pioneer ethical practices such as fair trade.</td>
<td>• Create opportunities for people experiencing barriers to employment.</td>
</tr>
</tbody>
</table>

Barriers to social enterprise development

13. Social enterprises face a range of hurdles as they move from the start-up phase, through expansion, to maturity. Those that set up as, or emerge from, a non-profit background face challenges in moving from the familiar territory of grants and donations towards a commercial model, and acquiring the necessary business acumen. A 2013 Grant Thornton survey of non-profit organisations¹ found that many “considering establishing or buying social enterprises are doing so without sufficient preparation or due diligence”.

14. In 2012 a Department of Internal Affairs’ survey² identified 421 social enterprises operating across a wide range of industries, with many wanting advice on growing their businesses. Social enterprise owners/members frequently lack experience in developing business cases, marketing, and managing business finances. Mainstream businesses can access various Government funded incubator and mentoring programmes, and the Minister of Science and Innovation recently announced a $31.3 million investment in four new technology-focused incubators. Equivalent support specifically tailored to social enterprise is very limited.

15. Non-profit organisations, and organisations with charitable status, are prohibited from providing pecuniary gain to their members. Hence many not-for-profits, although interested in growth, have limited capacity to raise capital because they cannot pay returns to investors.

² Department of Internal Affairs (2013), Mapping social enterprises in New Zealand: Results of a 2012 Survey.
16. Social enterprises that begin with a predominantly commercial orientation typically face high levels of risk in the early stages, as do many other businesses. The initiators may put in much "sweat equity" and struggle to raise capital – sometimes placing mortgages on their homes, or drawing on friends and family for support, in order to get their ideas off the ground. They often lack steady revenue streams, which makes it difficult to manage core costs such as salaries, and to attract investment and guarantee loans. If set up as limited liability companies they are generally ineligible for philanthropic grants.

17. Mainstream businesses can approach a range of angel investors who provide capital for business start-ups, and venture capital sources. Development of a social finance market, where investors pursue both financial and social/environmental returns, is hampered by various factors. Potential investors are uncertain about social enterprise risk profiles (resulting in higher transaction costs of credit assessments) and often desire fast growth (which may not be easy to achieve). There are few financial intermediaries specialising in managing the transfer of funds from investors to social enterprises.

Rationale for government involvement in growing social enterprise

18. I believe there is benefit in government encouraging this market so that more social enterprises can scale-up and become investment-ready. As well as responding to community-identified needs, social enterprises support government goals including a productive and competitive economy. They are potential partners for a range of portfolios in achieving "collective impact", and may assist Better Public Services goals that require innovative third party service delivery. The ability of social enterprises to raise funds for social good by trading and (once mature) to attract investment, is valuable at a time when government's own finances are constrained.

19. Various overseas jurisdictions have implemented policies and initiatives to grow social enterprise. For instance, in 2011 the Australian government provided AUS$20 million for social enterprise investment, which was matched by private investment. In the United Kingdom, a legal structure has been created specifically for social enterprise, along with a tax relief scheme for investors. A Big Society Capital bank has been established using money from dormant bank accounts to fund intermediaries to invest in social enterprises, and the Public Services (Social Value) Act 2012 requires public bodies to give preference in commercial tendering processes to organisations able to deliver social outcomes. The gross ‘value-add’ of British social enterprise is now at least £18.5 billion per annum.

20. I have already taken steps to consider the regulatory environment for social enterprise in New Zealand. A Department of Internal Affairs’ report Legal Structures of Social Enterprise (2013) considered whether a specific legal structure, tailored for the hybrid nature of social enterprise, would help target funding and investment towards this sector. The conclusion was, while a new legal structure may be valid at some point, building the capability of social enterprises is the first priority. Creating a more robust pipeline of social enterprise propositions is likely to attract both New Zealand and overseas investment into this sector.

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3 Effort put into a start-up company by the founders in exchange for ownership shares of the company.
4 This figure is based on a tight definition of social enterprise Cabinet Office (2013) Social Enterprises: Market Trends.
21. Key messages and practical actions from government have the potential to stimulate private sector and philanthropic support. Providing government support for social enterprise would be consistent with interventions to build capability and capacity in the business and non-profit sectors, for instance Callaghan Innovation's Incubator Support Programme, and the Ministry of Social Development's Capability Investment Resource which provides mentors for support social service providers.

**Current activity that supports social enterprise development**

22. Various existing initiatives are helping build knowledge and skills around social enterprise. For instance, a recent social enterprise 'start-up weekend' in Wellington involved teams receiving expert mentoring to create product ideas. Also, Auckland Council is partnering with Auckland University of Technology to run an evening class on social enterprise development, and with the University of Auckland to develop a four-year programme to map Māori social enterprises and launch indigenous initiatives.

23. Social enterprise is a growing interest area amongst youth. For instance P3, a youth-led charity focused on poverty eradication in the Asia Pacific region, runs an annual social enterprise national competition, The Lion Foundation Young Enterprise Scheme – a business course that gives students a chance to set up a company – shows an increasing trend towards social enterprise initiatives.

24. At the regional level, the Department of Internal Affairs' community advisers are now trained to provide basic advice for fledgling social enterprises. The Auckland Council, Ministry of Business, Innovation and Employment, ASB Community Trust and others are jointly developing an Auckland region social enterprise strategy.

25. Recent initiatives that will assist funding for social enterprise include:

- the Canterbury Community Trust's new Social Enterprise Fund aims to create employment opportunities and encourage innovation, self-sufficiency and community participation in that region;
- the Government's recent decision to proceed with a social bond pilot offers a new funding mechanism for organisations able, either alone or with others, to manage private investment and outcome-focused contracting [SOC Min (13) 19/4]; and
- the Financial Markets Conduct Act 2013, which enables equity-based crowdfunding, has significant potential to encourage investment in social enterprise.

26. This patchwork of activity is positive. However, added impetus would be gained if Government signals its support for this sector.

**A Government position on social enterprise**

27. I am seeking agreement to a Government position statement on social enterprise, as set out in the Appendix. This acknowledges the potential contribution of social enterprise to social, environmental and economic goals and recognises barriers to its development. A clearer Government focus on social enterprise will:

- signal to the sector and potential investors that the Government is willing to collaborate in supporting sector development;
- encourage government agency initiatives to support the sector; and
• provide a focal point for a government overview of barriers and "what works" in supporting social enterprise.

28. The implementation of the position statement involves a light-handed approach to government’s role, and is not a directive to align government work programmes around this theme. It would, however, be valuable if government agencies would consider how social enterprises can contribute to the Government’s goals and whether they can help build strength in this sector. The position statement aims to encourage responsiveness and collaboration. For instance, this creates the potential to investigate a government social procurement policy. The Department of Internal Affairs will develop an overview of responses to the position statement, in collaboration with other agencies.

29. To avoid the risk of the position statement raising sector expectations without accompanying concrete actions by government, I plan to support social enterprise development by providing funding from within the Community and Voluntary Sector portfolio.

Two new initiatives to support social enterprise capability

30. I plan to fund two initiatives (from within existing appropriations) to help grow social enterprise capability:
• a social enterprise accelerator pilot; and
• a national social enterprise incubation and development service.

31. Both initiatives will be run by the Hikurangi Foundation, which is the only agency providing tailored developmental support for social enterprises as its core business. Originally funded by the Todd and Tindall Foundations to focus on environmental sustainability, the Hikurangi Foundation is a non-profit organisation currently incubating around 15 social enterprises. Its vision is to expand its services and become a national intermediary supporting wide ranging social and environmental social enterprises.

32. Following a scan of other relevant organisations and initiatives, taking into account their relative capabilities and knowledge of social enterprise, and after discussions with other relevant government agencies, officials determined that a contestable funding process is not required at this stage. The Hikurangi Foundation is best placed to rapidly inject support to the sector, and has good prospects of leveraging additional private sector support. It has an existing service to build on, and its professionalism and in-depth knowledge of social enterprise is widely respected. For instance, the Hikurangi Foundation is working with the ASB Community Trust and Ministry for the Environment on ways to increase the self-sufficiency of their grant recipients. The Hikurangi Foundation has a collaborative approach and will link with other relevant organisations, such as the volunteer-based Business Mentors New Zealand.

33. Future funding decisions related to the Hikurangi Foundation will partly depend on availability of funding and positive evaluations. However, an overview of other relevant providers will also be maintained, and a more contestable approach to such funding may be considered in the future. The Hikurangi Foundation will not

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5 Social procurement involves use of tendering and purchasing processes to generate positive social outcomes in addition to the efficient delivery of goods and services.
have a competitive advantage as the increasing profile of the sector (partly through this initiative) is likely to see other entrepreneurial organisations also growing in strength. Also, any possible future government funding will need to take into account the extent to which government intervention remains useful in order to stimulate ongoing market growth.

34. As with other community funding in my portfolio, the Hikurangi Foundation funding will be provided through grants. Office of the Auditor-General 2008 guidance acknowledges that investing arrangements often take the form of grants that are designed to build capacity or to support a particular activity or organisation. My planned social enterprise funding will be an investment in a credible partner organisation that can provide specialised leadership to the sector.

**Social enterprise accelerator pilot**

35. To stimulate social enterprise growth, I intend to provide a $0.146 million grant in 2013/14 to the Hikurangi Foundation for a social enterprise accelerator pilot. The grant is half the cost of the pilot and will be subject to a co-funder being secured. The Hikurangi Foundation is in discussions with a potential funding partner and with major corporates that would provide mentors, thus building on its significant existing pro bono networks.

36. 'Accelerators' have sprung up around the world in recent years, putting entrepreneurs through intense training to hone their business plans. New Zealand's accelerators, such as the Lightning Lab programme for digital entrepreneurs, are aimed at sparking business innovation. The Hikurangi Foundation's pilot will be specifically tailored to social enterprise.

37. Based on The Crunch accelerator programme run by Social Traders⁶ in Australia, the New Zealand pilot is planned for launch early in 2014. From a series of regional enterprise design workshops 10 teams will be selected for six month's coaching. At a final event, the teams will present to potential funders and investors.

38. The pilot will test the accelerator model, assess the level of demand, and determine corporate/philanthropic willingness to invest in the resulting ventures. Quantitative data will be matched with a client satisfaction evaluation to be undertaken by an independent party.

**Social enterprise incubation and development service**

39. I will also contribute funding to the Hikurangi Foundation to provide a national social enterprise incubation and development service. Operating from bases in Auckland, Wellington and Christchurch, the service will be a hub of expert support, resources, and one-on-one advice. This echoes recommendations in a recent Ian Axford fellow report⁷ that Government support development of a national intermediary body, as part of creating a more coherent social enterprise “ecosystem”.

40. Funding of $0.375 million in 2013/14 and $0.750 million in 2014/15 will kick-start the incubation and development service, by supporting the core infrastructure. With this funding as a base, the Hikurangi Foundation will seek to leverage

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⁶ Social Traders, funded by the Victorian government and a private foundation, supports social enterprise development across Australia.

⁷ Mary Jo Kaplan (2013). *Growing the Next Generation of Social Entrepreneurs and Start-ups in New Zealand*. Fulbright NZ
additional funding from philanthropic and corporate sources. Funding from the Community and Voluntary Sector portfolio for outyears will be determined at a later stage based on initial progress and the availability of funds.

Monitoring and evaluation

41. Assessment of the accelerator pilot will involve quantitative data such as the number of participating organisations, value of pro bono services brokered and extent of investment in graduating social enterprises. An independent party will provide qualitative data such as participants’ satisfaction, stories of change, and case studies of impact. The incubation and development service will use reporting frameworks based on proven comparable models overseas, such as that used by a well established social enterprise support service in Scotland.

Next steps

42. I intend to report back to the Cabinet Social Policy Committee by the end of 2014 about the progress with the accelerator and incubator initiatives, and on initiatives to support social enterprise. The progress report will note how existing Government programmes can support social enterprise needs, indicate any new cross-Government activity that gives affect to the government position statement, and note any new market-led responses.

Consultation

43. This paper has been prepared by the Department of Internal Affairs. The following agencies have been consulted: the Ministry for the Environment, Ministry of Business, Innovation and Employment, Ministry of Health, Ministry of Pacific Island Affairs, Ministry of Social Development, Ministry of Women’s Affairs, Te Puni Kōkiri and The Treasury. The Department of the Prime Minister and Cabinet has been informed.

44. Feedback on this paper indicates positive opportunities for these initiatives to add value to the activities of various portfolios, for instance by connecting with Te Puni Kōkiri’s Māori Business Facilitation Service, supporting development needs of Pacific, ethnic and women entrepreneurs, and connecting with Ministry of Social Development regional work on innovative responses to complex social issues.

Financial Implications

45. Funding for the two Hikurangi Foundation initiatives fits within the scope statement of the Vote Internal Affairs’ Community Development Scheme (CDS). The Community-Led Development (CLD) scheme, which is a sub-component of the CDS, involves five communities developing plans for their social, cultural and economic development. Delays in establishing the CLD scheme, and planning delays in two of the communities, has meant that funding is able to be reprioritised to support the two social enterprise development initiatives in 2013/14 and 2014/15.

46. With effect from 1 November 2013, the Vote Internal Affairs community-based funding schemes have been merged into a Community Funding Schemes multi-category appropriation. Once the future funding needs of the CLD communities are confirmed, further funding for social enterprise development may be possible for 2015/16 from within the CDS appropriation or other areas within the multi-category appropriation.
Legislative Implications and Regulatory Impact Analysis

47. A Regulatory Impact Statement is not required as there are no legislative implications at this stage.

Human Rights, Gender Implications, Disability Perspective

48. The paper is consistent with the New Zealand Bill of Rights Act 1990 and the Human Rights Act 1993. Social enterprises can provide employment opportunities for people who might otherwise be disadvantaged in the labour force, including people with disabilities. In Britain, 86 per cent of social enterprise leadership teams have at least one woman director whereas only 13 per cent of the Institute of Directors’ membership is female.6

Publicity

49. I also propose to issue a press release outlining the Government position statement on social enterprise and indicating that I will be providing grant funding to the Hikurangi Foundation. I intend to publish this Cabinet paper and related Cabinet decisions on the Department of Internal Affairs’ website, subject to consideration of any deletions that would be justified if the information had been requested under the Official Information Act 1982.

Recommendations

50. The Minister for the Community and Voluntary Sector recommends that the Committee:

1. note that there is a growing movement of social enterprises that use business tools to tackle social and environmental issues;

2. note that emerging social enterprises face a range of barriers, centred around the need for developmental advice and access to funding;

3. agree that the Government adopt a position statement on social enterprise (appended to this paper) to encourage private sector and government agency responses to social enterprise development needs;

4. note that the Minister for the Community and Voluntary Sector will be supporting social enterprise development by providing grant funding for a social enterprise accelerator pilot in 2013/14 and a social enterprise incubation and development service in 2013/14 and 2014/15, with funding for outyears to be determined based on initial progress and funds available within baselines;

5. note that this grant funding referred to in recommendation 4 is from the Vote Internal Affairs’ Community Development Scheme, which is a category within the Community Funding Schemes multi-category appropriation;

6. invite the Minister for the Community and Voluntary Sector to report back to the Cabinet Social Policy Committee by the end of 2014 on progress with the accelerator and incubator initiatives, and on cross-Government activity that gives effect to the Government position statement on social enterprise;

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7. **note** that the Minister for the Community and Voluntary Sector will issue a press release announcing the Government position statement (if approved) and grant funding for the two social enterprise development initiatives; and

8. **note** the Minister for the Community and Voluntary Sector intends to publish this paper and related Cabinet decisions online, subject to consideration of any deletions that would be justified if the information had been requested under the Official Information Act 1982.

Hon Jo Goodhew
Minister for the Community and Voluntary Sector

24/11/2013
APPENDIX

PROPOSED GOVERNMENT POSITION STATEMENT ON SOCIAL ENTERPRISE

This Government position statement acknowledges the value of the growing social enterprise sector and supports collaborative action to ensure social enterprises meet their full potential.

Social enterprises use commercial methods to support social or environmental goals. They principally reinvest surpluses in the social/environmental purpose rather than maximising profit for shareholders and owners. Potential benefits of social enterprise include innovative responses to societal issues, new employment opportunities, and sustainable income generation.

The Government is aware of the significant growth of the social enterprise sector internationally and wishes to support development of the sector in New Zealand. The Government acknowledges the innovation and entrepreneurship of this sector and the valuable contribution social enterprises can make to community strength and resilience.

Social enterprises can support a range of government goals including the development of a productive and competitive economy. The Government values the role of social enterprises as potential partners for a range of government agencies in achieving “collective impact”, and as contributors to Better Public Services goals involving third party service delivery.

The Government recognises that emerging social enterprises face a range of challenges, including the need for business advice and funding tailored to their hybrid social/commercial nature. The sector currently lacks a solid support infrastructure and many social enterprises struggle to access external finance.

The Government appreciates the importance of raising awareness of social enterprise, of taking action to help build capability, and encouraging finance for this emerging sector. Social enterprise networks, investors, philanthropic organisations, local authorities and central government agencies can all contribute to a future where social enterprises can flourish.

The Government, through its agencies, commits to identify any policy barriers to social enterprise growth and to work collaboratively to create an enabling, supportive environment where more social enterprises can grow and attract investment.