

**Theme 5. New business models and understandings of human behaviour**

*5.1. Business models, organisations, and alternative valuation*

**A critical inquiry into new legal business models for social enterprises and their ability to create institutional change**

**Summary:**

The purpose of this article is to analyse how environmental and social entrepreneurs adopt new, legal business models, different from those used by traditional business and non-profit organisations. These legal institutions vary widely in their structure, but they all promote the dual pursuit of profit and social purpose. Based on a literature review, an analysis of legal frameworks and empirical data from the United Kingdom and the United States of America, this study identifies multiple challenging aspects of such models. Examples include weak enforcement mechanisms, high risk of goal conflicts, insufficient safeguards and a lack of accountability towards wider society and stakeholders. Early results indicate that a) the legal models represent inadequate institutional transformation if we are to achieve truly sustainable business models, and b) environmental and social entrepreneurs struggle to find a legal model that suits their needs and represents a real difference from business as usual.

**Extended abstract:**

Institutional change towards a sustainable economy is progressing slowly, especially within the private sector. Changing the way we produce goods and do business is of significant importance if we are to transition towards a sustainable society. While most politicians see businesses as a source to economic growth and prosperity, it is also a strong driver behind environmental degradation and unsustainable use of resources. What is good for the environment is often in conflict with what is good for business, e.g. short-termism, increased consumption pressures and low-cost production strategies.

One way of changing this is to re-structure institutions regarding businesses; for example the legal frameworks, conventions and norms (see Vatn 2005). Such a change would specifically imply a shift away from persistent institutions like shareholder primacy and profit maximization, towards a wider matrix of goals more aligned with overall societal welfare. Various reform efforts for improving sustainability of companies have been slow-moving, e.g. CSR-measures, certification, reform of executive pay or board representation (see Liao 2014). As opposed to such fine-tuning, this paper examines a more fundamental change to the model represented by new, legal business frameworks for social entrepreneurs. The purpose of this article is thus to analyse if and how environmental and social entrepreneurs choosing new, legal business models are able to create more sustainable institutions. This is analysed through a multi-disciplinary literature review, analysis of various legal models and empirical data from interviews with actors.

Environmental and social enterprises<sup>1</sup> can be defined as hybrid organisations that are “market-oriented, common-good mission-centered”, operating in the space between traditional for-profit and nonprofit enterprises (Boyd 2009, p. 9). They meld the social purpose traditionally associated with non-profit organisations with the economic purpose and market-based methods traditionally associated with for-profit firms (Wilson and Post 2011, p. 715). They are often seen as innovative (Ridley-Duff and Bull 2011), with the potential to create larger-scale socioeconomic structural transformation (Foxon and Parrish 2008), although the *panacea hypothesis* has received some criticism (see Hall, Daneke et al. 2010 for a discussion). Most importantly, they represent institutional change by adopting legal hybrid models that integrate social and environmental purpose.

To enable the delivery of social and environmental value from these actors to society, governments in various countries have created legal frameworks that secure dual purpose or blended mission (see Liao *forthcoming*; Lambooy and Argyrou 2014; Brakman Reiser 2012). This has been necessary due to certain limitations inherent in current frameworks for for-profit and non-profit organisations<sup>2</sup>, as these are often unable to capture the nature of social enterprises. These innovative legal models have mechanisms to secure the protection and delivery of social and/or environmental value, by introducing e.g. reporting requirements, dividend caps and protection to directors when prioritising environmental/social value over profit. They also enable actors to attract investment capital. Examples include the L3C Low-profit Limited Liability Company (2008), the Flexible Purpose Corporation (2011) and the Benefit Corporation (BC) (2010) in the US, and the Community Interest Company (CIC) (2005) in the UK<sup>3</sup>.

This paper is a critical analysis of the various institutional dimensions represented by in particular two of the above models; Benefit Corporations and Community Interest Companies. The emphasis is on enterprises that are both environmentally and socially oriented. The study is based on a literature review and analysis of all the aforementioned models, combined with empirical data from a field study of 15 BCs and 15 CICs. The following aspects are analysed: What types of activities do these new, legal institutions facilitate; What are the possibilities and what are the limitations to the models; How are plural goals safeguarded in theory and practice; What are the rights-structures and how are various interests protected; and if and how entrepreneurs attempt to compensate for any shortcomings of the legal framework. Interviews for this study will be carried out in January 2015.

Institutional theory will be applied as an analytical lens to investigate the institutional change represented by the above legal frameworks. They vary significantly in their institutional structuring, and thus also in their potential to represent any significant change towards increased sustainability. Examples include how they ensure enforcement, transparency, funding, directors’ duties, reporting, and profit distribution (see Brakman Reiser 2012). Another important aspect is their potential to achieve change in behaviour. This may occur by the frameworks; a) providing actors with agency and enable them to take different choices regarding how business is carried out, and b) providing a structure that represents a different institutional rationality contexts, improved safeguards and accountability. In general, social entrepreneurs are assumed to be intrinsically motivated to provide social/environmental value (see e.g. Ridley-Duff and Bull 2011; Choi and Gray 2008). However, they also have to operate within the defined framework.

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<sup>1</sup> Entrepreneurs (social) working with environmental issues are also known as *Ecopreneurs* (Pastakia 1998) or *Sustainability entrepreneurs* (Parrish 2010).

<sup>2</sup> This depends on the jurisdictional area and is not to say that companies cannot define their purpose as dual under current forms. Social entrepreneurs tend to use a variety of legal frameworks in practice.

<sup>3</sup> Similar legal models exist in Belgium, Italy, Greece and Portugal, and many of them build on long-standing traditions of cooperatives. These are, however, less business-centred.

In practice, all the above models have struggled on various levels. Preliminary results from the literature review suggests various problematic aspects. E.g. the L3C has significant shortcomings when it comes to reporting requirements; its creators focus on attracting private investment into the social sector, but see reporting as unfair and contradictory to the idea of the free, capitalist enterprise (Lang 2013, p.17). On the other hand, the UK has created a CIC government regulator and stricter requirements for reporting. The Benefit Corporation has among other things been criticised for its lack of accountability (André 2011). In general, there is a lack of enforcement mechanisms and strong standards (Brakman Reiser 2012). While these models have been created specifically for them, environmental and social entrepreneurs have been slow at adopting them. Thus, early results from this study indicate that a) all the above legal models represent inadequate institutional transformations if we are to achieve truly sustainable business models, and b) environmental and social entrepreneurs struggle to find a legal model that suits their needs and that represents a real difference from business as usual.

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