

Introduction to social enterprises

Legal information for community organisations

This fact sheet covers:

- ▶ what is a social enterprise?
- ▶ important factors to consider when starting a social enterprise
- ▶ financing a social enterprise
- ▶ choosing a legal structure for your social enterprise
- ▶ setting up and operating a social enterprise
- ▶ if things change or go wrong



Disclaimer

This fact sheet is an introductory resource to social enterprises. For more detailed information on setting up and operating a social enterprise (including social enterprise examples), refer to [our Social Enterprises guide](#).

The information in this fact sheet is intended as a guide only and is not legal advice. If you or your organisation has a specific legal issue, you should seek legal advice before deciding what to do.

Please refer to [the full disclaimer](#) that applies to this fact sheet.

What is a social enterprise?

There is no specific legal structure for social enterprises in Australia or a universally accepted definition of 'social enterprise'. However, working definitions agree that social enterprise involves running an enterprise that uses its revenue or business model to achieve an economic, social, cultural or environmental mission that benefits the public or a particular community.

At its core, being a social enterprise means using business models and skills to solve societal problems.

[Social Traders](#) (an Australian organisation that connects certified social enterprises with business and government for potential social procurement opportunities) describes social enterprises as:

'businesses that exist to create public or community benefit. Unlike traditional businesses, primarily driven by profit, social enterprises embed purpose into everything they do. It's business at its best'

To receive certification with Social Traders, the following five criteria are assessed:

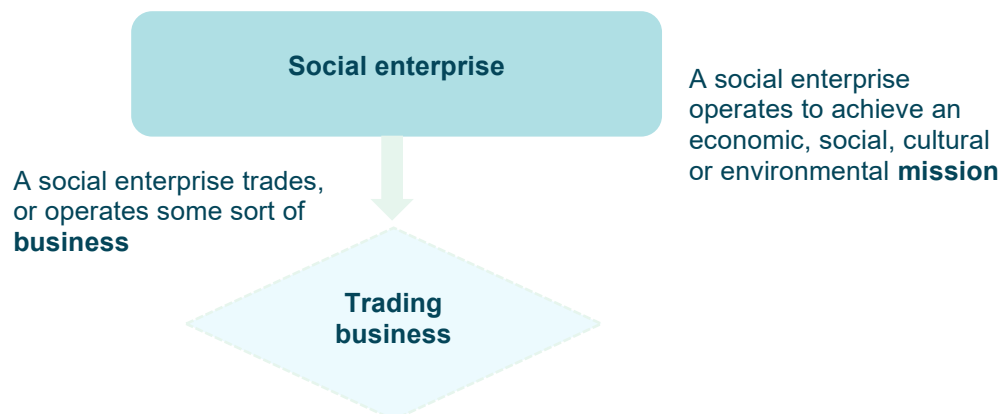
1. **Purpose:** Their reason for being is to solve a social or environmental problem.
2. **Operations:** They prioritise purpose, people and planet over profit in day-to-day decisions.
3. **Revenue:** They operate with a self-sustaining revenue model.
4. **Use of surplus:** The majority of any surplus is reinvested towards their mission.
5. **Structure:** Their legal and financial structures are designed to protect and lock in purpose for the long term.

The Social Traders definition may be used or required by some funders, including governments and corporates under social procurement policies.

A social enterprise can:

- be large or small
- be 'for-profit' or 'not-for-profit', or can involve a hybrid of both
- look like a normal business offering products or services and directing its profits to a cause
- operate with its mission embedded throughout its business model (for example, by employing underemployed populations or taking special environmental approaches to producing products and then using profits to further support the mission)

Example of a social enterprise



Social enterprise impact models

Common social enterprise impact models can be broadly divided into three categories:

- **Direct benefit model** - businesses that create or maintain services in direct response to social or economic needs in the community
- **Cross subsidy model** - businesses that create or maintain services in direct response to social or economic needs in the community and use the profits to support access to those otherwise excluded from the market
- **Donation model** - businesses that generate profit to make donations that support other community or not-for-profit organisational activities

Important factors to consider when starting a social enterprise

At the initial stages of starting up a social enterprise, key issues you need to address include:

- **working out the 'why'**

Understanding the mission of the social enterprise including who you want to benefit, how and why.

- **preparing a business plan**

A business plan is essential for setting up a successful social enterprise and working out the business model. It's often a critical tool when convincing funders or investors to support your project.

- **working out how you will fund the social enterprise**

Identifying sources of funding for your organisation is important because some funding sources are mutually exclusive and only available to for-profits or not-for-profits. This can have a significant influence on your choice of legal structure.

- **considering how you will measure the social enterprise's impact**

You will need to consider how the enterprise will demonstrate the impact that it is making through its work towards its mission or purpose and your theory of change.

- **deciding whether the social enterprise should incorporate**

It's a good idea to test the assumption that you need to set up and operate an incorporated entity to achieve your goals. Some options don't require setting up a whole new organisation

- **deciding whether the social enterprise should be for-profit or not-for-profit**

The key difference between a for-profit and a not-for-profit entity is the way that profits are used. It's time-consuming and expensive (and it can be difficult) to change legal structures down the track, so it's worth putting thought and effort in at the start to set yourself up for success.

A 'not-for-profit' organisation doesn't operate for the profit, personal gain or other benefit of its members. Rather, any profit made is used to further the aims of the organisation. That means all profits are put back into the organisation to continue to pay for its activities and functions and to achieve its mission.

In contrast, a 'for-profit' organisation is set up to make a profit for the people who are members or owners of the organisation. For-profit social enterprises normally distribute some profits to investors and retain some profits to be used by the social enterprise to create public value and achieve the mission of the organisation.

- **considering whether a not-for-profit social enterprise should register as a charity with the Australian Charities and Not-for-profits Commission (ACNC)**

Tax concessions are usually only available to charities registered with the ACNC. In deciding whether to register as a charity, social enterprises need to carefully consider whether the benefits of tax concessions outweigh the restrictions that concessions place on an organisation.



Refer to our [social enterprises guide](#) for checklists on:

- preliminary questions to consider
- things to cover in your business plan
- measuring impact, and
- eligibility for registration as a charity

Financing a social enterprise

A social enterprise's legal structure (for-profit or not-for-profit) influences its access to funding sources. While debt finance is generally available under both structures, equity investment is typically only available to for-profits. Some funding options like donations and certain grants typically require the recipient organisation to be a registered not-for-profit charity with Deductible Gift Recipient (**DGR**) status.

At a high level:

Funding sources	Eligible or suitable entities		Level of complexity
	For profit	Not-for-profit	
Equity	✓	✗	Medium – high
Debt	✓	✓	Medium - high
Donations	✗ (with some exceptions)	✓	Low - medium
Grants	✗ (with some exceptions)	✓	Medium - high
Social Investment Bonds	✓	✓	Very high
Crowd Funding	✓	✓	Low
Micro donations	✗ (with some exceptions)	✓	Low
Membership (as distinct from shareholders) fees	✗ (with some exceptions)	✓	Low

Choosing a legal structure

Choosing a legal structure is a very important decision, because it will affect issues like:

- the different types of funding your social enterprise can receive (as set out above)
- your social enterprise's eligibility for tax concessions and charity registration, and
- ongoing reporting requirements and other regulatory issues your social enterprise must meet

For-profit social enterprises often use a private company structure (if it has a small pool of owners), or a public company or co-operative structure (if it has a larger pool of owners).

For-profit structures are typically about wealth creation and have shareholders entitled to a 'share' of income (dividends) and capital (surplus on a winding up). In a social enterprise, the dividends and capital must be balanced against the requirements to reinvest the majority of the profit or surplus in the fulfilment of the mission.

Common structure choices for **not-for-profit social enterprises** include incorporated associations, companies limited by guarantee and non-distributing co-operatives. A not-for-profit structure does not mean no profit – in fact, to be sustainable all entities must operate to create value and a surplus.

But – not-for-profit structures require all assets to be used for the organisation's objects ('mission lock') and (unlike a for-profit structure):

- there are no distributions to members ('distribution lock'), and
- on winding up assets must be distributed to another entity with equivalent objects ('asset lock')

Indigenous corporations are another option for Aboriginal and Torres Strait Islanders, both under a for-profit or not-for-profit structure.

Hybrid structures - it's possible to use a combination of not-for-profit and for-profit structures. This can allow for innovation and flexibility, as enterprises can tailor the formal legal structure to their needs and enable both investment opportunities and access to tax concessions.

**Note**

Different reporting and compliance obligations will apply to your enterprise, depending on which legal structure you choose.

Before choosing a legal structure, you should be aware of the reporting requirements you will need to comply with and what level of reporting and compliance your enterprise can manage.

The reporting requirements depend on the nature of the regulator – whether only state, federal, or both state and federal law applies – and whether the social enterprise is a charity.

Also, be aware that some regulators are stricter than others. Some regulators, like the ACNC, take a more educative approach to enforcement, whereas regulators like ASIC generally take a stricter enforcement-style approach.

Setting up and operating a social enterprise

Once your organisation has decided which incorporated structure it will use, the next step is to set up your organisation following the process required by the relevant legislation.

The incorporation process is different for each type of legal structure, however there are some fundamental steps that all organisations should take. These include forming a committee or board, finding members, drafting rules or a constitution and holding meetings. Your entity may also wish to register as a charity, apply for tax concessions, or apply for certification as a social enterprise.



For information on the benefits and limitations to certification as a social enterprise, see [our social enterprises guide](#).

Once you have set up your social enterprise, running the social enterprise will involve complying with many regulations and laws, including laws regarding insurance, employment, work health and safety, documents and record keeping, intellectual property, advertising, running events, privacy, as well as ongoing compliance and governance requirements.

If things change or go wrong

Your organisation will go through change at times of growth, retraction and sometimes in response to changes in the law. Other issues that may come up include conflict or disputes.

When things change, you should stay on top of what is happening in your organisation, and be mindful of the options available to you, such as changing the nature of your organisation, working with another organisation or winding up.

**Note**

Changes to company details must be made online. This can be done by registering for online access using your company's corporate key and logging in to [ASIC's online services portal](#). See ASIC's '[Changes to your company](#)' webpage for further information.



For guidance on dealing with these issues, see [our social enterprises guide](#).