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**PURSUING PROFIT AND PURPOSE: TOWARDS A
HYBRID LEGAL STRUCTURE FOR SOCIAL
ENTERPRISES IN NEW ZEALAND**

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Abstract

The social enterprise movement is gaining momentum in New Zealand. Social enterprises are hybrid organisations that use business models to create social and environmental value. This relatively new approach to doing business is becoming increasingly important as New Zealand works to solve some of its most complex and pressing social and environment issues such as poverty, unemployment and climate change. However, the current legal structures available in New Zealand have been identified as creating a barrier for social enterprises. These structures force entities to have only a single primary mission. This paper posits that whilst the charitable trust and limited liability company forms have the flexibility to be adapted and combined, they continue to create an uncomfortable existence for social enterprise. This paper investigates whether a new legal structure specifically designed for social enterprises should be introduced in New Zealand. It analyses the features of the hybrid legal structures available in the United Kingdom and in the United States. Drawing from these examples, this paper observes that giving legal recognition to social enterprise, as a distinct entity, will bring legitimacy and favourable recognition to their business, thereby enabling and supporting more organisations to pursue profit and purpose, which will directly benefit all New Zealanders.

Keywords: “social enterprise”, “hybrid organisations”, “purpose-driven”, “hybrid legal structures”, “Companies Act 1993”.

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I Introduction

The world currently faces a number of complex and intractable social and environmental challenges, such as poverty, socio-economic inequality, environmental degradation and social exclusion.¹ These challenges – often called “wicked problems”² – have forced us to reconsider the role and purpose of business. It has become apparent that we cannot continue with the “business as usual” approach. Solving these challenges requires new approaches to doing business, and “social enterprise” presents a vehicle for achieving this.

While the term “social enterprise” remains disputed, there is general agreement that social enterprises are organisations that pursue a paramount social³ mission but are sustained by profit-making trading activities.⁴ These dual objectives, one drawn from the non-profit sector (social mission) and the other from the for-profit sector (economic profit), result in these types of organisations being referred to as “hybrids”.⁵ The increasing levels of success of social enterprise demonstrate that profits and purpose are not mutually exclusive, despite long-held views to the contrary.⁶

1 World Economic Forum *The Global Risks Report 2022* (11 January 2022) at 11.

2 Mary Kaplan *Growing the Next Generation of Social Enterprises and Start-Ups in New Zealand* (Ian Axford (New Zealand) Fellowships in Public Policy, August 2013) at 3; see generally Stony Brook University “What’s a Wicked Problem?” <www.stonybrook.edu>.

3 The term “social” is used widely throughout this Paper to encompass an organisations social, environment and cultural mission(s).

4 Sacha McMeeking, William Grant and Unaiki Melrose *Insights on Māori Social Enterprise 2017 - - Pakihi Whai Kaupapa* (Te Puni Kōkiri, 19 September 2017) at 6; see also Ākina Foundation “Social Enterprise – definition, perception and what is ahead” (15 August 2018) <www.akina.org.nz>; and Hon Stuart Nash and Hon Priyanka Radhakrishnan *Government Support for Social Enterprise* (Joint briefing by the Ministry of Business, Innovation and Employment and the Department of Internal Affairs, 15 December 2021) at [4].

5 Erynn E Beaton and Elena Dowin Kennedy “Responding to failure: the promise of market mending for social enterprise” (2021) 23 *Public Manag Rev* 641 at 643.

6 See generally for example Milton Friedman “The Social Responsibility of Business Is to Increase Its Profits” in Walther Ch Zimmerli, Markus Holzinger and Klaus Richter (eds) *Corporate Ethics and Corporate Governance* (Springer, Berlin, 2007) 173.

New Zealand's social enterprise sector, while still in its relative infancy, has shown great potential to grow into a robust market. These organisations provide innovative market-based solutions to social issues, create employment opportunities for marginalised or disadvantaged people and foster inclusive and sustainable economic development. Despite this, many challenges remain. The New Zealand Government has recognised “that emerging social enterprises face a range of challenges...The sector currently lacks a solid support infrastructure, and many enterprises struggle to access external finance”.⁷ The Government has committed to creating an “enabling, supportive environment” for social enterprises to thrive.⁸

In many ways, New Zealand is still catching up to the range of social enterprise models that have emerged. In several jurisdictions – including the United Kingdom, Canada and certain United States states – hybrid legal structures have been introduced to accommodate the dual mission of social enterprise (and other purpose-driven businesses). These forms enable organisations to voluntarily register as a company with limited liability, generating profits to be used for socially beneficial purposes. Meanwhile, New Zealand law continues to force a decision between a non-profit or a for-profit form.

This paper aims to contribute to the New Zealand literature on social enterprise. It advocates for the introduction of a hybrid legal structure – similar to those available in other jurisdictions. It considers that social enterprises have a fundamental role to play in modern society, but the creation of an enabling, supportive environment is still required.⁹ As Liao suggests: “hybrids may be a key contributor to establishing critical infrastructure to help solve some of the most pressing social and environmental issues of our time”.¹⁰

7 Department of Internal Affairs “Government Position Statement on Social Enterprise” (14 February 2014) <www.dia.govt.nz>.

8 Department of Internal Affairs, above n 7.

9 Department of Internal Affairs, above n 7.

10 Carol Liao “Limits to Corporate Reform and Alternative Legal Structures” in Beate Sjøfjell and Benjamin Richardson (eds) *Company Law and Sustainability: Legal Barriers and Opportunities* (Cambridge University Press, Cambridge, 2015) 274 at 275.

This paper is structured as follows. Part II explores the concept of social enterprise, its distinguishing characteristics and its relationship with existing organisational forms and social practices. Following this, the advantages of, and some challenges for, social enterprises are identified and explained.

Part III surveys the legal structures presently available in New Zealand. It identifies the structures most commonly adopted by social enterprises, and examines the advantages and drawbacks of each when applied in this context. While there are exceptions, it considers that the current structures are acting as a barrier – not an enabler – for established and prospective social enterprises that wish to profit, albeit without profit being the sole or primary objective. Against this background, the need for a hybrid legal structure emerges.

Part IV investigates the changing landscape of company law. It engages with the enduring shareholder versus stakeholder debate. While shareholder primacy is the dominant norm, it considers that over the past several decades there have been incremental movements toward a stakeholder model of governance. This has in part been due to growing social and environmental concerns. The Companies (Directors Duties) Amendment Bill – currently awaiting its first reading in the House - seeks to materialise this shift. This lays the foundations for the development of a hybrid legal structure, which would go a step further by embedding a broad set of stakeholder interests into its core. As mentioned, several jurisdictions have already done so.

Part V analyses the hybrid legal structures that have been introduced in the United Kingdom and certain United States states, highlighting the distinguishing features of each model. These hybrid structures have broadened the discussions beyond the shareholder versus stakeholder debate, expressly requiring an organisation to act in the interests of a wider set of stakeholders. These models (or some variation thereof) have subsequently been introduced in other jurisdictions, representing the growth in global demand for socially responsible business practices.

Part VI argues that a new legal structure, amongst other things, is required if New Zealand social enterprises are to reach their full potential.¹¹ In this part, the potential benefits and risks that may flow from the introduction of a new structure are considered. Against this background, Part VII proposes a hybrid legal structure for social enterprises in New Zealand, highlighting its governing features. This includes amendments to the Companies Act 1993. Given the scope of this Paper, this part does not intend to determine all the details, but seeks to introduce a framework that will be built upon in subsequent research and policy work.

II Social Enterprise: An Overview

This part provides a comprehensive overview of the social enterprise movement. It begins by engaging with the definitional debate.

A Defining Social Enterprise

Over the past several decades, the concept of social enterprise has grown dramatically around the world.¹² Social enterprise has been identified as a powerful tool for addressing pressing social problems, such as poverty, socio-economic inequality, environmental degradation and social exclusion.¹³ This has generated much interest amongst the academic, political and business community, given the failure of traditional approaches to address such problems.

11 Lindsay Jeffs “Social Entrepreneurs and Social Enterprises – Do they have a future in New Zealand?” (Paper presented at the 51st ICSB World Conference, Melbourne, June 2006) at 2.

12 Janelle A Kerlin “Defining Social Enterprise across Different Contexts: A Conceptual Framework Based on Institutional Factors” in Benjamin Gidron and Yeheskel Hasenfeld (eds) *Social Enterprises: An Organisational Perspective* (Palgrave Macmillan, London, 2012) 91 at 91; Anthony Abbatiello and others *The Rise of Social Enterprise: 2018 Deloitte Global Human Capital Trends* (Deloitte, 15 January 2018) at 3; François Bonnici *More in Common: The Global State of Social Enterprise* (British Council and Social Enterprise UK, June 2022) at 1 and 18; and Sally R Osberg and Roger L Martin “Two Keys to Sustainable Social Enterprise” (May 2015) Harvard Business Review <www.hbr.org>.

13 Mohammad Zainuddin and Ida Md Yasin “Employee Motivation in Social Enterprises: Tackling the Dual Mission Dilemma” (June 2018) Social Science Research Network (SSRN) <www.papers.ssrn.com> at 187.

Despite the nascent interest in social enterprise, the ideas fuelling the concept are not new, especially in New Zealand.¹⁴ Although the term itself was not used, for centuries Māori enterprises have pursued broad social and environmental goals and redirected profits for community benefits.¹⁵ As a concept, however, social enterprise proliferated following the Global Financial Crisis (GFC) in 2008.¹⁶ The GFC tightened government budgets and illuminated the problems caused by traditional profit-maximising corporations.¹⁷

A distinguishing feature of the academic research on social enterprise is the substantial debate concerning its definition.¹⁸ All definitions will invariably describe a business with a “social mission”.¹⁹ Yet, the term remains vague and elusive, “capable of meaning different things to different people across different contexts”.²⁰ This is because it is “culturally, economically, socially, historically and politically variable”.²¹ Esposito

14 Michelle Therese Hackett “The ‘Everyday’ Political Economy of Social Enterprise: Lessons from *Grameen Shakti* in Bangladesh” (PhD Thesis, University of Adelaide, 2012) at 2.1; and Kaplan, above n 2, at 4.

15 McMeeking, Grant and Melrose, above n 4, at 3; Kaplan, above n 2, at 4; Ani Kartikasari, Christopher Gan and Campbell Kerr “Essential to society, yet remains on the side-lines: The State of Social Enterprises in New Zealand” (2020) 198 AEER 626 at 629; and Robert Joseph and Richard Benton *Waking the Taniwha: Māori Governance in the 21st Century* (Thomson Reuters, Wellington, 2021) at 41-46, 53 and 56.

16 Kaplan, above n 2, at 3; Anthony Abbatiello and others, above n 12, at 3; Daryl Poon *The Emergence and Development of Social Enterprise Sectors* (Social Impact Research Experience, 2011) at 5; and Cole Hoover “the 600-year history of the social enterprise movement – and how the next 6 years are its most important” (11 October 2018) MovingWorlds Blog <www.blog.movingworld.org>.

17 Kaplan, above n 2, at 3.

18 Katherine Isabel Rostron “Defining the Social Enterprise: A Tangled Web” (2015) 2 IJMAR 85 at 86.

19 Rostron, above n 18, at 86.

20 Janelle A Kerlin “Social Enterprise in the United States and Europe: Understanding and Learning from the Differences” (2007) 17 VOLUNTAS 247 at 247; and Nitha Palakshappa and Suzanne Grant “Social enterprise and corporate social responsibility: Toward a deeper understanding of the links and overlaps” (2016) 24 IJEER 606 at 614.

21 Kerlin, above n 20, at 247; and Palakshappa and Grant, above n 20, at 614.

observes that “[d]espite the infancy of social enterprise, much ink has already been spilt attempting to define it”.²²

In an endeavour to solve the definitional challenge, Brouard and Larivert analysed over 30 definitions that have been proposed.²³ Pulling the threads together, they defined social enterprises “as organisations which pursue social missions or purposes that operate to create community benefit regardless of ownership or legal structure and with various degrees of self-sufficiency, innovation and social transformation”.²⁴ This clearly encompasses a broad range of organisations. The Department of Internal Affairs (DIA) suggest the following three criteria to determine the existence of a social enterprise:²⁵

- (1) a social, cultural, or environmental mission that achieves public or community benefit;
- (2) has a substantial proportion of income derived from trade; and
- (3) reinvests the majority, or all, of profits/surplus in the fulfilment of [its] mission.

Despite the varied definitions that have emerged in the literature, there is general agreement that a social enterprise is an organisation with a paramount social mission but is sustained by profit-making trading activities.²⁶ These dual objectives – social and economic value creation – result in these types of organisations often being referred to as “hybrid organisations”, “blended enterprises” or “purpose-driven”.²⁷ The social enterprise

22 Robert T Esposito "The Social Enterprise Revolution in Corporate Law: A Primer on Emerging Corporate Entities in Europe and the United States and the Case for the Benefit Corporation" (2013) 4 Wm & Mary Bus L Rev 639 at 646.

23 François Brouard and Sophie Larivert *Social Enterprises: Definitions and Boundaries* (Association for Nonprofit and Social Economy Research, 1 June 2011) at 9-10.

24 Brouard and Larivert, above n 23, at 11.

25 Department of Internal Affairs *Legal Structures for Social Enterprise* (June 2013) at 5.

26 McMeeking, Grant and Melrose, above n 4, at 6; see also Ākina Foundation, above n 4; and Hon Stuart Nash and Hon Priyanka Radhakrishnan, above n 4, at [4].

27 Department of Internal Affairs, above n 7; McMeeking, Grant and Melrose, above n 4, at 6; and Dana Brakman Reiser “Blended Enterprise and the Dual Mission Dilemma” (2010) 33 Vt L Rev 105 at 105.

movement represents a “new interpretation on an old way of thinking – that business should be about more than [just] profit”.²⁸

B Models of Social Enterprise

The definitional debate has led to the development of several models of social enterprise. These models inform a greater understanding of social enterprise and its relationship with existing organisational forms.²⁹

The most common model is the depiction of a continuum, which demonstrates that a social enterprise can fall somewhere on a line between a traditional for-profit business and a non-profit organisation.³⁰ A social enterprise blends elements of both under a single entity, affirming that the independence of social [and economic] value...creation is a myth”.³¹ Like traditional non-profit organisations, social enterprises have a paramount social mission. The social mission may vary considerably: for example, an organisation may work to eliminate period poverty,³² reduce food waste³³ or provide employment opportunities for people with disabilities.³⁴ Conversely, like traditional for-profits, they utilise commercial models and strategies to generate a profit – which ultimately serves to further their social mission, as opposed to being returned to shareholders.³⁵

However, the continuum model has been critiqued for overlooking the role of the public sector.³⁶ Social enterprises have emerged as the boundaries between the traditional three sectors of the economy – public, private and non-profit – have become increasingly

28 Boyle Mathieson Lawyers “What is ‘social enterprise’ and why does it matter?” (August 2018) <www.bmlaw.co.nz> at 1.

29 Palakshappa and Grant, above n 20, at 607.

30 See Appendix, pg. 42.

31 Liao, above n 10, at 293.

32 See for example Wā Collective “About Us” <www.wacollective.org.nz>.

33 See for example Everybody Eats “Our Mission” <www.everybodyeats.nz>.

34 See for example Kilmarnock Enterprises “Our Story” <www.kilmarnock.co.nz>.

35 Department of Internal Affairs, above n 7.

36 Palakshappa and Grant, above n 20, at 608.

blurred.³⁷ Social enterprises draw from these three sectors to “fill a gap”,³⁸ providing innovative solutions to social problems which the existing sectors have been unable (or unwilling) to address.³⁹ Recognising this relationship, a further – arguably more comprehensive – model has been developed using the depiction of a Venn diagram.⁴⁰ This model illustrates social enterprise as an emerging fourth sector that interacts with, but is distinct from, the private, public and non-profit sectors.⁴¹ According to Kaplan “social enterprises may achieve social impacts more efficiently than governments, more sustainably and creatively than not-for-profits, and more generously than businesses”.⁴²

Eat My Lunch – a well-known New Zealand social enterprise - provides a useful illustration of the definitions and models discussed above.⁴³ The business idea of Eat My Lunch was conceived in response to a growing social issue – that thousands of Kiwi kids go to school every day without lunch. Eat My Lunch is “on a mission to ensure no child is at school hungry”.⁴⁴ To achieve this mission, Eat My Lunch has adopted a buy-one, give-one model, so for every lunch brought, a lunch is given to a child who would otherwise go without. So, the bigger Eat My Lunch gets, the bigger its impact becomes. Since 2015, Eat My Lunch has given almost 2 million lunches to Kiwi kids, whilst generating a profit to further its social mission.⁴⁵

C Distinguishing Corporate Social Responsibility

To further our understanding of social enterprise, and how it differs from other established social practices, it is necessary to consider its relationship with corporate social

37 Helen Malandain and Steven Moe “How the ‘fourth sector’ of the economy can help us now” (March 2021) Pocketknife <www.pocketknife.co.nz>.

38 Nelarie Cornelius and others “Corporate Social Responsibility and the Social Enterprise” (2008) 81 J Bus Ethics 355 at 358.

39 Mohammad Zainuddin and Ida Md Yasin, above n 13, at 187.

40 See Appendix, pg. 42.

41 See Appendix, pg. 42.

42 Kaplan, above n 2, at v.

43 Eat my Lunch “Our Story” <www.eatmylunch.nz>.

44 Eat my Lunch, above n 43.

45 Eat my Lunch, above n 43.

responsibility (CSR). In the past, social enterprise has been conflated with CSR.⁴⁶ While the two are not necessarily mutually exclusive, they are distinct.

As with social enterprise, CSR is a term that is difficult to define, with its scope remaining the subject of considerable academic debate.⁴⁷ At its most basic, CSR is a form of self-regulation integrated into a business model.⁴⁸ It reflects a company's voluntary commitment to greater levels of responsibility and accountability towards stakeholders, including consumers, employees and the environment.⁴⁹ CSR provides a mechanism to encourage for-profit businesses to integrate social and environmental concerns into their operations.⁵⁰ However, it generally remains up to the business to determine the extent of that integration.

Social enterprise can be distinguished from CSR in two material respects. First, as Huybrechts and Nicholls observe, CSR is not necessarily entrepreneurial, nor innovative.⁵¹ For example, CSR may simply align a business's practices with established norms, such as employee treatment. Whereas social enterprises depend on entrepreneurship and

46 Jonathan Barrett "Should New Zealand Adopt Hybrid Social Enterprise Legislation?" (2013) 19 NZBLQ 253 at 254.

47 Esposito, above n 22, at 648; Palakshappa and Grant, above n 20, at 608; and Salmi Mohd Isa "Corporate Social Responsibility: What Can We Learn from the Stakeholders" (2012) 65 ICIBSoS 327 at 328.

48 University of Washing Center for Leadership & Social Responsibility "What is Corporate Social Responsibility" <www.corporatesocialresponsibility.com>.

49 Esposito, above n 22, at 648; and Dana Brakman Reiser "Alternative business organisations and social enterprises" in Eugene Heath, Byron Kaldis and Alexei Marcoux (eds) *The Routledge Companion to Business Ethics* (Routledge, London, 2018) 257 at 258.

50 Antony Page and Robert A Katz "Is Social Enterprise the New Corporate Social Responsibility?" (2011) 34 Seattle U L Rev 1351 at 1377.

51 David Littlewood and Diane Holt "Social Entrepreneurship and CSR Theory: Insights, Application and Value" in Laura J Spence and others (eds) *Research Handbook on Small Business Social Responsibility: Global Perspectives* (Edward Elgar Publishing, Cheltenham, 2018) 292 at 297.

innovation to find solutions to social problems.⁵² In this sense, CSR is considered a reactive approach to social change, whereas social enterprise is proactive.⁵³

Secondly, the respective aims of CSR and social enterprise are fundamentally different. Businesses engage in CSR for the ultimate goal that it will enhance profitability.⁵⁴ Thus, profit-making remains superior to social impact. Conversely, social enterprises give primacy to social mission, with profits seen as means to achieve that mission, rather than being an end as and of themselves.⁵⁵ Social enterprise moves beyond CSR, placing social mission at the heart of their business model.

D Balancing the Dual Mission

Before turning to discuss the ways that social enterprises may structure themselves, it is important to consider some of the challenges this emergent business model faces within the market. As mentioned, social enterprises pursue the dual mission of creating social and economic value. Ideally, a social enterprise would be able to pursue, and balance, both missions equally.⁵⁶ In reality, they often come into conflict. Managing this conflict can be challenging. This is known as the “two masters” problem.⁵⁷

Social enterprises have to decide how to allocate resources between their social and economic missions.⁵⁸ For example, should they operate domestically, which would create more jobs for their local community which they seek to serve, or offshore, which would

52 See generally Organisation for Economic Co-operation and Development (OECD) “Social entrepreneurship & Social enterprises” <www.oecd.org>; and University of Oxford “Social Enterprise? Entrepreneurship? Innovation?” <www.eship.ox.ac.uk>

53 Workforce Opportunity Services “Social Enterprise vs. Corporate Social Responsibility” (14 November 2018) <www.wforce.org>.

54 Timothy Besley and Maitreesh Ghatak “Profit with Purpose? A Theory of Social Enterprise” (2017) 9 *Am Econ J Econ Policy* 19 at 23.

55 Littlewood and Holt, above n 51, at 5.

56 Abdi Rahman Jama Rabi “How Social Enterprises Manage Mission Drift: A Systematic Review” (MBA Thesis, Örebro University, 2016) at 5.

57 Brakman Reiser, above n 49, at 263; see also Dana Brakman Reiser “Blended Enterprise and the Dual Mission Dilemma” (2010) 33 *Vt L Rev* 105 at 105.

58 Carmen Nobel “What To Do When Your Organisation Has Dual Missions” *Forbes* (online ed, New York City, 3 December 2015).

generate more profit?⁵⁹ These tensions give rise to the risk of “mission drift”.⁶⁰ Mission drift refers to the situation where the organisation diverges from, or compromises, its founding mission in pursuit for greater revenues.⁶¹ This is a particular risk for social enterprises as they scale.⁶² Market pressures may cause the enterprise to prioritise financial considerations over their social mission.⁶³

In addition to the risk of mission drift, the general public and potential financiers, are often suspicious of the integrity of the dual mission. For example, the public was outraged when finding out that Eat My Lunch was structured as a company, not a registered charity.⁶⁴ Eat My Lunch was accused of “social washing” and called to be more transparent about their business.⁶⁵ This is in part due to the entrenched (but arguably outdated) market perceptions around the purpose of a charity and a purpose of a business.⁶⁶ Namely, that a charity is “for good”, while a business is “for profit”, and a single entity cannot be both.⁶⁷ Horan et al. note that “social enterprises carry the burden...to show that they are not a corruption of charity or an unsuccessful business”.⁶⁸ Social enterprises often have to go to great lengths to convey their point of difference, which, by their very nature, they want to have known. This paper considers that giving social enterprises a place under the law, as a distinct entity, will increase public awareness and provide the sector with a sense of legitimacy.

59 Brakman Reiser, above n 49, at 263.

60 Abdi Rahman Jama Rabi, above n 56, at 1.

61 Abdi Rahman Jama Rabi, above n 56, at 15.

62 Marta Maretich, Jed Emerson and Alex Nicholls “Governing for Impact: Managing Mission-Driven Organisations Through Stages of Growth and Investment” (24 March 2016) Social Science Research Network (SSRN) <www.papers.ssrn.com> at 4; and Brakman Reiser, above n 57, at 106.

63 Brakman Reiser, above n 57, at 106-107; Abdi Rahman Jama Rabi, above n 5660, at 4; and Dan Zastawany “Social enterprises must not prioritise social aims over viability” *The Guardian* (online ed, London, 17 February 2014)

64 Henry Oliver “A fierce argument for and against Eat My Lunch” *The Spinoff* (online ed, New Zealand, 26 July 2018).

65 Henry Oliver, above n 64.

66 Ākina Foundation *A Roadmap for Impact* (Department of Internal Affairs, April 2021) at 35.

67 Steven Moe *Social Enterprises in New Zealand: A Legal Handbook* (eBook ed, Parry Field Lawyers, 2017) at 36-37.

68 Jane Horan and others *Structuring for Impact: Evolving Legal Structures for Business in New Zealand* (The Impact Initiative, 2019) at 16.

To summarise, this part has sought to provide a comprehensive overview of social enterprise, its distinguishing characteristics and relationship with existing organisational forms and social practices. The ability of social enterprises to provide innovative solutions to a range of social problems that the traditional three sectors - public, private and non-profit - have been unable (or unwilling) to address makes them a very important aspect of modern society.⁶⁹ By combining commercial methods with a social mission, social enterprises can deliver real and sustainable impact. But they need wide-ranging support. Koh notes that “if we do not [support them], we run a very real risk that social enterprises will continue to inspire and excite, but not change the world in a significant way”.⁷⁰ In acknowledgement of this, the next part explores the legal structures presently available in New Zealand to support this emerging fourth sector.

III Legal Structures Adopted by Social Enterprises

The global social enterprise movement is gaining momentum in New Zealand. While research is limited, it was estimated that in 2018 there were around 2,600 social enterprises in New Zealand, contributing about \$850 million to GDP each year, in addition to the less quantifiable social, environmental and cultural impacts.⁷¹ Social enterprises are operating across a variety of sectors – including agriculture, hospitality, tourism, technology, health and waste – and are serving a range of beneficiaries.⁷²

69 Mohammad Zainuddin and Ida Md Yasin, above n 13, at 187.

70 Harvey Koh “Can Social Enterprise Really Solve Poverty?” *Forbes* (online ed, New York City, 8 April 2014).

71 Konrad Hurren, Hugh Dixon and Ganesh Nana *Making Sense of the Numbers: The number and characteristics of Social Enterprises* (Business and Economic Research Limited (BERL), November 2018) at 24; Ministry of Business, Innovation and Employment *The future of business for Aotearoa New Zealand: An exploration of two trends influencing productivity and wellbeing – purpose-led businesses and use of blockchain technology* (May 2022) at [2.5.4]; and Ākina Foundation *The Impact Initiative: A summary of the three-year programme to develop Aotearoa New Zealand’s social enterprise sector* (Department of Internal Affairs, March 2021) at 5.

72 Department of Internal Affairs, above n 25, at 8; and Ākina Foundation “The Road Ahead for Social Enterprise” (29 April 2021) <www.akina.org.nz>.

The New Zealand social enterprise sector, while still in its relative infancy, has great potential to grow into a robust market.⁷³ With a similar population size to New Zealand, Scotland's social enterprise sector serves as a useful comparator.⁷⁴ In Scotland, there are more than 6,000 social enterprises, generating more than £2.7 billion for Scotland's economy each year, and supporting more than 88,000 jobs.⁷⁵ With the right support, it is foreseeable that New Zealand's social enterprise sector could outgrow those figures.

However, in New Zealand, there is no legal structure specifically designed to accommodate social enterprises. Instead, social enterprise founders must take “the ‘number 8 wire’ approach...and simply make do and work within existing [legal structures]”.⁷⁶ The challenge, however, is that the existing structures force a decision between a for-profit or a non-profit organisational form.⁷⁷ Social enterprises must attempt to fit their dual mission within a single mission form.⁷⁸ Sabeti observed that social enterprise founders often end up “shoehorning their vision into [a particular] structure and accepting burdensome trade-offs in the process”.⁷⁹

The structures most commonly adopted by social enterprises include the charitable trust, the limited liability company, or a combination of the two.⁸⁰ The choice of structure does, however, impact the enterprises' ability to truly pursue its dual mission. In particular, it impacts branding, governance, funding and profit and asset distribution. The next part explores these structures, highlighting the pertinent features, benefits and limitations of each when applied to social enterprise.

73 Kartikasari, Gan and Kerr, above n 15, at 627.

74 McMeeking, Grant and Melrose, above n 4, at 7; and Kartikasari, Gan and Kerr, above n 15, at 628.

75 Social Enterprise Scotland “Social Enterprise Scotland” <www.socialenterprise.scot>.

76 Moe, above n 67, at 33.

77 Heerad Sabeti “The For-Benefit Enterprise” (November 2011) Harvard Business Review <www.hbr.org> at 2; see also Brakman Reiser, above n 57, at 106.

78 Brakman Reiser, above n 57, at 106; and Kartikasari, Gan and Kerr, above n 15, at 628.

79 Sabeti, above n 77, at 2.

80 Department of Internal Affairs, above n 25, at 6; Moe, above n 67, at 33; and Hurren, Dixon and Nana, above n 71, at 7.

A Charitable Trust

A common structure for social enterprise is to incorporate as a charitable trust board under the Charitable Trusts Act 1957, to be managed by trustees.⁸¹ A charitable trust must advance “exclusively charitable purposes”.⁸² The trustees have a number of fiduciary obligations, of particular relevance is the duty to further the permitted purpose of the trust.⁸³ This form allows social enterprises to legally represent themselves as a charity, which is beneficial as charities are assumed to be “for good”.⁸⁴

A major advantage of this structure for a social enterprise is that its “charitable purpose”⁸⁵ must be enshrined in its founding documents, the Trust Deed, and adhered to, creating a “mission lock”.⁸⁶ The *Impact Initiative Report* found that many social entrepreneurs’ “default” to charitable structures for this reason.⁸⁷ In New Zealand, charitable purposes are limited to: relieving poverty, advancing education, advancing religion, or other purposes beneficial to the community (such as protecting the environment).⁸⁸ The narrow definition of charitable purposes limits the activities that a social enterprise can engage in, and expand to. The Charities Services notes that “a charity’s purpose and activities must provide benefits to the public, however not everything that benefits the public is considered ‘charitable’”.⁸⁹ Thus, not all social enterprises will meet this definition. Gary et al. observe

81 Charitable Trusts Act 1957, s 7(1).

82 Charitable Trusts Act 1957, s 2; and Charities Act 2005, s 5(1).

83 See Trusts Act 2019, ss 22-26; Charities Services “The new Trusts Act - What does it mean for registered charities?” (29 January 2021) <www.charities.govt.nz>; Charities Services “Social enterprise and charity” (6 April 2018) <www.charities.govt.nz>; and Emma Lindblom “Duties and Responsibilities of a Trustee in NZ” (18 February 2021) Legal Vision <www.legalvision.co.nz>.

84 Susan Gary and others *Purpose-driven structures For Impact Entrepreneurs in Aotearoa New Zealand: Considering Kaitiakitanga and Steward Ownership* (Chapman Tripp, November 2020) at 10; and Steven Moe, above n 67, at 37.

85 Charitable Trusts Act 1957, s 2; and Charities Act 2005, s 5(1).

86 Charities Services “Social enterprise and charity”, above n 83.

87 Jane Horan and others, above n 68, at 16.

88 Charitable Trusts Act 1957, s 2; Charities Act 2005, s 5(1); see also Charities Services “Charitable Purposes” <www.charities.govt.nz>.

89 Charities Services “Charitable Purposes”, above n 88; see also Charities Services “Social enterprise and charity”, above n 83.

that many of the United Nations Sustainable Development Goals (SDGs) would not be considered a charitable purpose.⁹⁰ The SDGs are a set of 17 global goals designed to be a shared “blueprint to achieve a better and more sustainable future for all”.⁹¹ They include (amongst others) ending hunger, promoting wellbeing, achieving gender equality and combatting climate change.⁹² Although important, many of these goals are too broad to be a “charitable purpose”. An organisation will be prevented from becoming a registered charity if its stated purpose is too broad, in particular, if it is open to multiple interpretations.⁹³

A charitable trust can carry out profit-making trading activities, however, any profits generated are subject to the “non-distribution constraint”.⁹⁴ The non-distribution constraint prohibits the distribution of profits to private individuals.⁹⁵ Thus, social enterprise founders are unable to make a pecuniary gain, other than reasonable remuneration for services.⁹⁶ Although social enterprises primarily exist to address a social issue, the inability to return a share of the profits is disadvantageous, given the resources that founders devote to the cause. However, compliance with the non-distribution constraint confers income tax

90 Susan Gary and others, above n 84, at 10; see also United Nations “Do you know all 17 SDGs?” <www.sdgs.un.org>.

91 United Nations “Take Action for the Sustainable Development Goals” <www.un.org>.

92 United Nations, above n 91.

93 For example, if an organisation had a purpose to “promote social wellbeing” this would be too broad and could be interpreted in many ways. To be charitable, the purpose to “promote social wellbeing” would have to be clearly and narrowly defined as (for example) “helping the elderly from becoming isolated from the community”, see Charities Services “Broad purposes” <www.charities.govt.nz>; and Charities Services “Social enterprise” <www.charities.govt.nz>.

94 Sue Barker *Focus on purpose – What Does a World-Leading Framework of Charities Law Look Like?* (New Zealand Law Foundation, 10 April 2022) at 40-42; Dana Brakman Reiser and Steven Dean “Hunting the Stag with Fly Paper: A Hybrid Financial Instrument for Social Enterprise” (2013) 54 BC L Rev 1495 at 1501; Charities Services “Public benefit and charitable purposes” <www.charities.govt.nz>; Charities Services “Social enterprise and charity”, above n 83; and Brakman Reiser, above n 57, at 106.

95 Moe, above n 67, at 33; Department of Internal Affairs, above n 25, at 5; and Charities Services “Social enterprise”, above n 93.

96 Charities Services “Charitable purpose and your rules” <www.charities.govt.nz>; Charities Services “Social enterprise and charity”, above n 83; and Charities Services “Public benefit and charitable purposes”, above n 94.

exemptions and contribution deductions.⁹⁷ These tax advantages are beneficial for social enterprises, especially those in the start-up phase. But it also means that if the trust is wound up, any surplus assets must be transferred to another charity, locking assets into charitable purposes in perpetuity.⁹⁸

The inability of the charitable trust to provide returns to equity investors limits the enterprise's ability to attract capital.⁹⁹ Funding streams are generally limited to government grants, private donations, debt-financing and retained earnings – sources which are generally inadequate to service the financial needs of a commercial enterprise.¹⁰⁰ If the enterprise fails to meet the charitable status criteria – which according to Brakman Reiser and Dean is not hard¹⁰¹ – the loss of tax exemptions may risk their financial health.¹⁰² Taken together, this limits the enterprise's ability to grow sustainably in the long term.

B Limited Liability Company

Another option taken by social enterprise is to incorporate a limited liability company (LLC) under the Companies Act 1993 (the Companies Act).¹⁰³ A company must have at least one director, who is appointed by the shareholders, to manage or direct the business and affairs of the company.¹⁰⁴ Upon incorporation, the company acquires a separate legal personality.¹⁰⁵ Shareholders' liability is also limited to the value of their shareholding.¹⁰⁶

Choosing the company form has advantages for social enterprise as it is flexible and well-understood amongst the business community. Funds can be raised by offering limited

97 Susan Gary and others, above n 84, at 10.

98 Department of Internal Affairs, above n 25, at 9.

99 Charities Services “Social enterprise and charity”, above n 83.

100 Moe, above n 67, at 34.

101 Brakman Reiser and Dean, above n 94, at 1502; and Charities Services “Charitable purpose and your rules”, above n 96.

102 Strategic Group on Social Enterprise and Social Finance *Social Enterprise and Social Finance: A Path to Growth* (Department of Internal Affairs, April 2016) at 17.

103 Companies Act 1993.

104 Companies Act 1993, ss 10 and 128(1).

105 Section 15.

106 Section 97.

liability shares to investors, which facilitates sustainable growth (although there may be difficulties in explaining that the business is not purely for-profit).¹⁰⁷ Adopting the company form also allows social enterprise founders to make a pecuniary gain, through dividends or selling shares.¹⁰⁸ However, this must be balanced against a lack of preferential tax treatment. It would also be difficult to access government funding – despite solving social problems otherwise addressed by the government – as they are not a charity, which is usually required. Companies can qualify for charitable status, although this would require them to advance exclusively charitable purposes, as with the trust.¹⁰⁹

The company form was established purely with the needs of for-profit enterprises in mind. There is nothing inherent in the company form that would protect the primacy of social mission for social enterprises. However, a constitution can be adopted.¹¹⁰ The constitution has the effect of negating or modifying the default set of rules in the Companies Act.¹¹¹ The social mission can be clearly articulated in the constitution. Further restrictions can also be included, for example, prohibiting a change in mission unless agreed by an overwhelming majority of shareholders.¹¹² The constitution would be publicly available through the Companies Office website.¹¹³ Shareholders agreements can also be entered into as an alternative and private mode of outlining the social mission and setting expectations.¹¹⁴ For example, Eat My Lunch brought in FoodStuffs North Island as an investor in 2017 – the country’s largest grocery retailer. The founders of Eat My Lunch ensured that the mission was the first line of the shareholder agreement.¹¹⁵

107 Moe, above n 67, at 36-37.

108 Susan Gary and others, above n 84, at 10.

109 Community Law “Charitable company” <www.communitytoolkit.org.nz>.

110 Companies Act 1993, s 32.

111 Section 27.

112 Section 16(2); and Ākina Foundation *How to Protect the Purpose of Your Business: Otherwise Known as ‘Mission Lock’* (Department of Internal Affairs, March 2021) at 1.

113 New Zealand Companies Office “Companies Register” <www.companies-register.companiesoffice.govt.nz>.

114 Companies Act 1993, s 31; see generally for discussion Brakman Reiser, above n 57, at 107.

115 Jane Horan and others, above n 68, at 24.

Given its flexibility, the company form appears to provide a satisfactory vehicle for social enterprises. Despite this, the company form does not create the right opportunities for social enterprises. The shareholder primacy norm - discussed further in part IV – creates problems for social enterprises.¹¹⁶ Although not found anywhere in the law, there is an expectation that the company should be run in a way that maximises shareholder value.¹¹⁷ However, social enterprises principally reinvest surpluses to further their social mission, rather than maximising shareholder value.¹¹⁸

The shareholder primacy norm has come to dominate the financial expectations and performance of a company.¹¹⁹ As mentioned, social enterprise founders may have great trouble explaining to potential financiers that they are not purely for-profit.¹²⁰ Although this will conceivably become easier as the social enterprise becomes better understood and as “impact investing”¹²¹ increases, it has been a challenge shared amongst social enterprises.¹²² For example, Eat My Lunch’s loan application was declined because, according to the bank manager, “there was no way [that they were] going to make money by giving away free stuff”.¹²³ They had to use their own equity instead. Furthermore, a company’s performance is usually measured in financial terms, focused on the “bottom line”. Whereas social enterprises measure social impact along with financial performance, focused on the “triple bottom line”.¹²⁴ Thus, it would be difficult to gain an accurate

116 Alice Klettner “Finding Balance between Profit and Purpose: Should Australia Create a Legal Structure for Social Enterprise?” (2019) 47 ABLR 335 at 337.

117 Jo Kelly “Governing for purpose and stakeholders in Aotearoa New Zealand (22 June 2021) MinterEllisonRuddWatts <www.minterellison.co.nz>.

118 Department of Internal Affairs, above n 7.

119 Klettner, above n 116, at 337; and Stephen M Bainbridge *Director Versus Shareholder Primacy in New Zealand Company Law as Compared to U.S.A Corporate Law* (UCLA School of Law, Law-Econ Research Paper No 14-05, 26 March 2014) at 11 and 26.

120 Moe, above n 67, at 36-37.

121 “Impact Investing” is investing with the intention to generate positive measurable social and environmental impact alongside a financial return; see Ākina Foundation, above n 66, at 30.

122 Department of Internal Affairs, above n 7.

123 Jane Horan and others, above n 68, at 21.

124 Jane Horan and others, above n 68, at 21.

understanding of the financial health, or performance, of the social enterprise, based on traditional financial reporting.

C Certified B Corporation

Although not a separate legal entity, it is useful to briefly mention the certified B Corporation (B Corp). B Corp is a status available for for-profit companies in New Zealand, and elsewhere around the world.¹²⁵ It is a private third-party certification administered by B Lab – a non-profit organisation working to transform “the global economy to benefit all people, communities and the planet”.¹²⁶ As of October 2022, there were 187 B Corps registered in New Zealand, up from just 22 in 2019, and one in 2014.¹²⁷ The B Corp phenomenon illustrates growing demand for sustainable business practices. Australia and New Zealand is the fastest-growing region for B Corps worldwide.¹²⁸ Interestingly, hybrid legal structures are absent in both jurisdictions.

To become certified, a company must meet the “highest standards of verified social and environmental performance, legal accountability, and public transparency to balance profit and purpose”.¹²⁹ Coupling the LLC structure with B Corp certification provides another option for social enterprises. Certification demonstrates the company’s commitment to purpose, and to the interests of both shareholders and stakeholders.¹³⁰ But as Gray et al. observe, there is nothing inherent in the B Corp status to protect the social mission.¹³¹ B

125 Susan Gary and others, above n 84, at 9.

126 B Lab “About B Lab” <www.bcorporation.net>.

127 B Corp Global “Find a B Corp” <www.bcorporation.net>; see also Ministry of Business, Innovation and Employment, above n 71, at 22.

128 B Lab Australia and New Zealand *State of the B: Business as a force for good in Australia and Aotearoa New Zealand* (2019) at 2; Maggie Coggan “The State of Australian and New Zealand B Corps Revealed” (12 November 2019) Probono Australia <www.probonoaustralia.com.au>; and Klettner, above n 116, at 343.

129 B Lab Australia and New Zealand “About B Corps – What is a B Corp?” <www.bcorporation.com.au>.

130 See generally B Lab Global “New Zealand” <www.bcorporation.net/en-us/legal-requirement/country/new-zealand>.

131 Susan Gary and others, above n 84, at 9.

Corp standards are not legally enforceable.¹³² Neither the directors, nor the company, will be liable for damages, should the company fail to meet them.¹³³ B Corp status can be lost, however, which could conceivably result in reputational damage. But this would typically require B Lab to monitor the activities of every certified organisation closely and regularly, or to refuse to renew an organisations certification, which is required every three years.¹³⁴

D Dual Entity Structure

A final option is to adopt a dual entity structure. A dual entity structure – combining the charitable trust with the LLC – may provide an opportunity for social enterprises to derive the unique benefits offered by each structure.¹³⁵ Most commonly, this would involve establishing a charitable trust that owns shares in a LLC, set up as its profit-making “trading arm”.¹³⁶ For example, Sanitarium – the manufacturer of Kiwi pantry staples Weet-Bix and Marmite – is the profit-making trading arm of the Seventh Day Adventist Church.¹³⁷ The profits generated from Sanitarium’s sales are recycled back to the Church, by way of dividend, to use for its charitable purposes.

A structure of this kind enables the charitable trust to retain a controlling interest in the company, while preserving its charitable status and, thus, its tax exemptions. In terms of funding, the charitable trust can attract private donations and grants, and the company can raise funds from investors.¹³⁸ However, deploying a dual entity structure can be expensive and complicated – especially for those in the start-up phase – and requires comprehensive legal and tax advice. For example, Patu Aotearoa – a social enterprise aimed at improving the fitness and health of Māori and Pasifika people – expressed “frustration” that they were

132 Michael O’Regan “B Corp certification won’t guarantee companies really care about people, planet and profit” (8 October 2019) The Conversation <www.theconversation.com>.

133 B Lab, above n 126.

134 B Corporation “Measuring a company’s entire social and environmental impact” <www.bcorporation.net>.

135 Moe, above n 67, at 38.

136 See appendix, pg. 43; see also Moe, above n 67, at 38.

137 Sanitarium “Our Story: Profits for Purpose” <www.sanitarium.co.nz>.

138 See appendix, pg. 43.

required to set up two entities.¹³⁹ The charitable trust alone cost them \$20,000 to establish – “money that could have otherwise been used to buy more equipment...for a community of need”.¹⁴⁰ As discussed below in Part VI, these costs could largely be avoided (or at least reduced) if a bespoke ‘off-the-shelf’ structure for social enterprise was available.¹⁴¹ The United Kingdom “community interest company” - discussed in detail below in Part V - was created with the specific aim of reducing the expense of registration for social enterprises.¹⁴²

The signalling effect is also highly relevant, as discussed further in Part VI.¹⁴³ Under a dual entity structure, the social enterprise remains identified as either a LLC (“for profit”) or as a charity (“for good”). The inability to signal the primacy of social impact is disadvantageous.¹⁴⁴ Having a specialist structure, as opposed to having to adapt existing ones, gives legitimacy and favourable recognition to a social enterprise’s businesses. Furthermore, Gary et al. observe that it is more beneficial to have the charity within the for-profit structure, but doing so would have implications for the charity’s tax exemptions.¹⁴⁵

In summary, the existing legal structures have their unique advantages and disadvantages, but none can be used by social enterprises with confidence. They have been identified as a barrier that hinders social enterprises from reaching their full potential, and with that, the potential impacts on society.¹⁴⁶ Given social enterprises are entities that operate with a view to profit, albeit without profit being the primary objective, the company form is most

139 Nikki Mandow “Social enterprises frustrated by NZ law” *Newsroom* (online ed, Auckland, 23 April 2019).

140 Nikki Mandow, above n 139; see generally Kartikasari, Gan and Kerr, above n 15, at 628.

141 See Part VI.

142 Robert Coffey, Judith Smyth and Max Hogg *Using the Community Interest Company model in the housing sector: A marriage in the making?* (Joseph Rowntree Foundation, 2007) at 4.

143 See Part VI.

144 Jane Horan and others, above n 68, at 30; and Steven Moe “Structuring for Impact” in Steven Moe *Laying Foundations for Reimagining Business* (Seeds Press, Christchurch (NZ), 2021) 48 at 49.

145 Susan Gary and others, above n 84, at 11; see further Moe, above n 67, at 38.

146 Jane Horan and others, above n 68, at 4; Kartikasari, Gan and Kerr, above n 15, at 626 and 630; and Moe, above n 144, at 49-50.

suitable.¹⁴⁷ Despite this, the company form still falls short of the support and recognition that is needed to enable and encourage social enterprise. Against this background, the remaining parts of this paper focus entirely on the company form, and how it may be amended for social enterprises. To this end, the next part explores the changing landscape of company law. It illustrates that over the past several decades there have been growing demands for sustainable business practices with higher standards of consideration of stakeholder interests.

IV The Changing Landscape of Company Law

This part provides an overview of the development of the company operating within contemporary New Zealand. It engages with the enduring shareholder versus stakeholder debate and highlights that over the past several decades there have been growing demands for a stakeholder governance model – both domestically and internationally. It considers that the Companies (Directors Duties) Amendment Bill – currently awaiting its first reading in the House – is a symptom of this wider global movement.

A Corporate Governance

Prior to the Companies Act 1993, companies were required to list their objects in their articles of association (now known as the constitution).¹⁴⁸ Any transaction outside the listed objects was voidable, known as the doctrine of *ultra vires*.¹⁴⁹ This is no longer a mandatory requirement. The effect of s 16 of the Companies Act is that a company can do anything that a natural person can do.¹⁵⁰ Unless the constitution specifically restricts the

147 Jane Horan and others, above n 68, at 32.

148 Jonathan Barrett and Ronán Feehily *Understanding Company Law* (4th ed, LexisNexis, Wellington, 2019) at [1.3].

149 Barrett and Feehily, above n 148, at [1.3]; Law Commission *Company Law Reform and Restatement* (NZLR R9, 1989) at [343]-[345]; and Colin Mayer *What is Wrong with Corporate Law? The Purpose of Law and the Law of Purpose* (European Corporate Governance Institute, Working Paper 649/2022, 2 May 2022) at 7.

150 Companies Act 1993, s 16.

objects of the company, its objects are unrestricted.¹⁵¹ When left unrestricted, the question then arises as to the purpose of the company, and for whom does it serve.

The corporate objective debate is one of the oldest, and largely unresolved, debates in company law.¹⁵² The two main competing paradigms are shareholder primacy and stakeholder theory. According to shareholder primacy, the sole purpose of the company is to maximise shareholder value.¹⁵³ Directors are mere agents of shareholders, and therefore, their primary responsibility is to them. Proponents claim that “when corporations are run to maximise shareholder value..., the performance of the economy as a whole, not just the interests of shareholders, can be enhanced”.¹⁵⁴ In light of rising global crises, we may question the credibility of that argument. Furthermore, shareholder primacy rests on a false assumption that shareholders are the “owners” of the company.¹⁵⁵ As within the company, a share only entitles a shareholder to receive a dividend where the company chooses to issue those¹⁵⁶ (along with other rights, such as being able to elect the board).¹⁵⁷ Shareholders have no rights against the assets of the company. This distinction prevents shareholders from being the true “owners” of the company.¹⁵⁸ Despite this, shareholder primacy has been the dominant norm shaping corporate behaviour across Anglo-American

151 Section (2); see also Rosemary Teele Langford “Purpose-Based Governance: A New Paradigm” (2020) 43 UNSWLJ 954 at 966.

152 Edward B Rock “For Whom Is the Corporation Managed in 2020? The Debate over Corporate Purpose” (2021) 76 *Bus Lawyer* 363 at 363.

153 Barrett and Feehily, above n 148, at [1.3].

154 William Lazonick and Mary O’Sullivan “Maximizing Shareholder Value: A New Ideology for Corporate Governance” (2000) 29 *Econ Soc* 13 at 27; and Jonathan Mukwiri “Myth of Shareholder Primacy in English Law” (2013) 24 *EBOR* 217 at 222.

155 Nina Boeger and Charlotte Villiers *Shaping the Corporate Landscape: Towards Corporate Reform and Enterprise Diversity* (1st ed, Bloomsbury Publishing, London, 2018) at 2.

156 Companies Act 1993, ss 52-53.

157 Sections 155, and 156; see generally New Zealand Companies Office “What it means to be a shareholder: Your rights and responsibilities as a company shareholder” <www.companies-register.companiesoffice.govt.nz>.

158 Paddy Ireland “Company Law and the Myth of Shareholder Ownership” (1999) 62 *Mod L Rev* 32 at 33; Justin Fox and J Y. Lorsch “What Good Are Shareholders?” (July 2012) *Harvard Business Review* <www.hbr.org>; and John Kay “Shareholders think they own the company – they are wrong” *The Financial Times* (online ed, London, 11 November 2014).

jurisdictions. In the absence of clear authority or direction, directors remain reluctant to stray far from the shareholder primacy norm.¹⁵⁹

In contrast, stakeholder theory holds that the corporative objective is to create value for all stakeholders - including shareholders, customers, employees, suppliers, the community and the environment. Stakeholder theory is premised on the idea that the company should serve the interests of all those who affect and are affected by the company's business.¹⁶⁰ This significantly widens the class of interests that directors must consider and balance when making business decisions.

B Directors' Duties

Section 131(1) of the Companies Act sets out the most "fundamental duty" owed by New Zealand directors to their company.¹⁶¹ It requires that a director "act in good faith and in what the director believes to be the best interests of the company".¹⁶² There remains considerable uncertainty as to the meaning of the "best interests of the company". Kalderimis and Swan observe that the question of who "*the company*" is...remains a matter of academic debate, largely between proponents of the 'shareholder primacy' and 'stakeholder' theories of corporate governance".¹⁶³

While the New Zealand courts have not determined which theory s 131(1) reflects, Bainbridge observes that "shareholder primacy is widely assumed to be a defining

159 Rosemary Teele Langford "Use of the Corporate Form for Public Benefit: Revitalisation of Corporations Law" (2020) 43 UNSWLJ 977 at 982; Silvana Schenone and Selwyn Eathorne *Stakeholder governance: A call to review directors' duties* (Institute of Directors and MinterEllisonRuddWatts, July 2021) at 3; Bainbridge, above n 119, at 26; and B Lab Australia and New Zealand *Submission to the Social Impact Investing Discussion Paper February 2017* (27 February 2017) at 6.

160 Mayer, above n 149, at 2; and Schenone and Eathorne, above n 159, at 3.

161 Lloyd Kavanagh "Thinking beyond shareholders; time to define "best interests of the company"" (7 April 2019) LinkedIn <www.linkedin.com>.

162 Companies Act 1993, s 131(1).

163 Daniel Kalderimis and Nicola Swan *Sustainable Finance Forum: Legal Opinion 2019* (The Aotearoa Circle, 30 November 2019) at [85].

characteristic of New Zealand company law”.¹⁶⁴ Accordingly, the “best interests of the company” have been interpreted as meaning the financial interests of the shareholders as a whole. This does not necessarily mean that stakeholder interests are to be ignored.¹⁶⁵ Indeed, proponents acknowledge that stakeholder interests are important to consider, but only if doing so would enhance shareholder wealth.¹⁶⁶ Thus, while directors may choose to take the interests of stakeholders into account, they face considerable legal uncertainty as to whether they are properly discharging their duty of good faith should they choose to favour such interests over the financial interests of shareholders.¹⁶⁷ For this reason, directors tend to act in accordance with the shareholder primacy norm.¹⁶⁸

C Towards Stakeholder Governance

Amidst rising global crises, the shareholder primacy norm is starting to show signs of wear. In 2019, the Business Roundtable – an association of CEOs of leading American corporations - released a statement committing to “lead their companies for the benefit of all stakeholders – customers, employees, suppliers, communities and shareholders”.¹⁶⁹ This must be compared to its 1996 statement which read that “the principal objective of a business enterprise is to generate economic returns to its owners”.¹⁷⁰ This signals a stark departure from shareholder primacy.¹⁷¹

In New Zealand, the business landscape has changed considerably since the Companies Act was introduced in 1993. Directors are increasingly expected to have regard to the interests of stakeholders.¹⁷² This has been achieved through legislative provisions external

164 Bainbridge, above n 119, at 26.

165 Schenone and Eathorne, above n 159, at 14.

166 Liao, above n 10, at 280.

167 B Lab Australia and New Zealand, above n 159, at 6.

168 B Lab Australia and New Zealand, above n 159, at 6.

169 Business Roundtable “Statement on the Purpose of a Corporation” (19 August 2019) <www.businessroundtable.org>.

170 Rock, above n 152, at 365.

171 Rock, above n 152, at 365.

172 Langford, above n 159, at 983.

to company law, such as employment,¹⁷³ consumer¹⁷⁴ and environmental law.¹⁷⁵ In relation to climate change, Kalderimis and Swan observed that New Zealand directors are generally permitted, and in many cases will be required, to take climate change risks into account when making business decisions.¹⁷⁶ However, they note that it is:¹⁷⁷

unclear whether and to what extent a New Zealand court could seek to interpret the director's duty to act in the best interests of the company as indirectly including a requirement to consider the interests of broader stakeholders.

Several jurisdictions have sought to facilitate change towards a stakeholder governance model by amending the duty to act in good faith to permit, or require, directors to consider stakeholders' interests along with shareholders. In the United Kingdom, directors are *required* to promote the success of the company for the benefit of its members (i.e., its shareholders) and in doing so have regard to other such matters including employees' interests, the need to foster the company's business relationships with suppliers, customers and others, as well as the impact of the company's operations on the community and the environment.¹⁷⁸ Similarly, in Canada, directors *may*, when acting in the best interests of the corporation, consider the interests of shareholders and other stakeholders, including employees, consumers and the environment.¹⁷⁹

In July 2021, a whitepaper published by the Institute of Directors and MinterEllisonRuddWatts called for a review of directors' duties.¹⁸⁰ The paper identified "unsolved questions as to a board's responsibility around maximising shareholders'

173 See for example Employment Relations Act 2000; and Health and Safety at Work Act 2015.

174 See for example Consumer Guarantees Act 1993; Commerce Act 1986; and Contract and Commercial Law Act 2017.

175 See for example Resource Management Act 1991.

176 Kalderimis and Swan, above n 163, at [7.1].

177 At [87.3].

178 Companies Act 2006 (UK), s 172(1).

179 Canada Business Corporations Act R.S.C 1985 (CA), s 122.

180 See Schenone and Eathorne, above n 159.

returns, creating long-term value, and the extent that various stakeholders’ interests should be considered and prioritised”.¹⁸¹

Since the publication of the whitepaper, the Companies (Directors Duties) Amendment Bill (the Bill) has been introduced into the House.¹⁸² The Bill signals a shift towards the stakeholder governance model. The Bill proposes an amendment to s 131 of the Companies Act – the duty of good faith. It seeks to clarify that a director *may*, when determining the best interests of the company, take into account an open-ended list of recognised environmental, social and governance factors (ESG), including: the principles of the Treaty of Waitangi, environmental impacts, good corporate ethics, fair and equitable employment practices and the interests of the wider community.¹⁸³

The explanatory note to the Bill further confirms the paradigm shift.¹⁸⁴ The note clarifies that a company may seek to promote any number of objectives, in addition, or in substitution, to profit-making. It clarifies that it is for the company, and its shareholders, to determine such objectives.¹⁸⁵ Therefore, broadening the scope of the corporate objective beyond mere profit-making. If passed, this would be beneficial for social enterprises that adopt the company form in the sense that it would clarify that incorporating for purposes, other than for profit, is permissible.

Since the introduction of the Bill, differing views have been offered as to its likely effect in practice.¹⁸⁶ This is because directors are permitted, but not required, to take ESG factors

181 Institute of Directors “Stakeholder focus highlights need to review directors’ duties” (30 July 2021) <www.iod.org.nz>.

182 Companies (Directors Duties) Amendment Bill 2021 (75-1).

183 Clause 4.

184 Explanatory note.

185 Explanatory note.

186 See Joe Windmeyer “Amending directors’ duties for company stakeholders” (4 October 2021) Russell McVeagh <www.russellmcveagh.com>; Roger Partridge “Directors’ Duties Bill is well-meaning but harmful” (4 May 2022) The New Zealand Initiative <www.nzinitiative.org.nz>; David Goodman and Tom Mohammed “Companies (Directors Duties) Amendment Bill - A shift towards the stakeholder view of corporate governance” (5 November 2021) Anderson Lloyd <www.al.nz>; Emma Geard “The Directors Duties Member’s Bill - another distraction from real climate action?”

into consideration. This is a significant legal difference. However, the Bill is not intended to bring about transformative change. But rather, to clarify an identified ambiguity in the law. This is implicit through the use of the phrase “to avoid doubt”.¹⁸⁷ This also suggests that many directors are already taking ESG factors into consideration.

Despite being permissive, the clarification is certainly helpful. If passed, the Bill may lead to changes in corporate behaviour. It may give directors confidence to consider, and act for, wider stakeholder interests.¹⁸⁸ Moe suggests that “the reform is the start of a positive reframing with increased scrutiny for companies and shows a roadmap for additional changes that may flow in the future”.¹⁸⁹

While the shareholder versus stakeholder debate continues, Liao observes that “innovative new corporate structures [have been] forming on the sidelines that embed stakeholder interests...into their governance structures”.¹⁹⁰ These structures sidestep this debate, expressly permitting an organisation to pursue socially beneficial purposes for broad stakeholder interests while generating profits and providing investment opportunities for socially conscious investors. The next part examines these structures.

V Hybrid Legal Structures for Social Enterprise

In more recent years, several jurisdictions have introduced hybrid legal structures. These structures bridge the gap between the traditional for-profit and non-profit organisational

(3 November 2021) Lawyers for Climate Action <www.lawyersforclimateaction.nz>; and Tom Corkill “Companies (Directors Duties) Amendment Bill - Amending directors’ duties for stakeholders” (23 November 2021) Norris Ward McKinnon <www.nwm.co.nz>.

187 Companies (Directors Duties) Amendment Bill, cl 4.

188 Kavanagh, above n 161.

189 Steven Moe “Proposed changes to the Companies Act mark the beginning of positive change” in Steven Moe *Laying Foundations for Reimagining Business* (Seeds Press, Christchurch (NZ), 2021) 19 at 21.

190 Carol Liao “The Next Stage of CSR for Canada: Transformational Corporate Governance, Hybrid Legal Structures, and the Growth of Social Enterprise” (2013) 9 *Int Sustain Dev* 53 at 73.

forms to enable the dual pursuit of social and economic value creation.¹⁹¹ While several models exist, this paper focuses on two. Namely, the “community interest company” (CIC) in the United Kingdom and the “benefit corporation” (BC) in the United States. This part outlines the distinguishing features of each model.

A Community Interest Company

Introduced in the United Kingdom in 2005, the CIC is a “purpose-built” organisational form for social enterprises. A CIC is a “special status” company, governed under the Companies Act 2006 (UK).¹⁹² There are now over 26,000 CICs, operating in every sector, and delivering substantial benefits to communities across the United Kingdom.¹⁹³

CICs are limited companies that operate to provide a benefit to the community.¹⁹⁴ The community benefit must satisfy the “community interest test”¹⁹⁵ administered by the CIC Regulator, a state official who supervises and monitors CIC activity.¹⁹⁶ The test requires that “a reasonable person might consider that its activities (or proposed activities) are being carried on for the benefit of the community”.¹⁹⁷ This test is broader than that which applies to charities in New Zealand, but clearly targets an entity with significant social goals.¹⁹⁸ CIC directors have a duty to ensure that the company is run in such a way that it will

191 Liao, above n 190, at 75; Department of Internal Affairs, above n 25, at 5; Patricia Mary Fitzgerald “The Emergence of Social Enterprise in Not-for-Profits” (PhD, University of Auckland, 2016) at 21; and Brakman Reiser and Dean, above n 94, at 1506.

192 Companies Act 2006 (UK), s 6.

193 Community Interest Companies “CIC Regulator: Annual Report 2021 to 2021” (10 August 2022) Gov UK <www.gov.uk>.

194 Department for Business, Energy & Industrial Strategy *Information and Guidance Notes: Chapter 1: Introduction* (Office of the Regulator of Community Interest Companies, May 2016) at 3.

195 Companies (Audit, Investigation and Community Enterprise) Act 2004 (UK), s 35(2).

196 Sections 27 and 38.

197 Section 35(2); and Department for Business, Energy & Industrial Strategy *Information and Guidance Notes: Chapter 4: Creating a Community Interest Company (CIC)* (Office of the Regulator of Community Interest Companies, May 2016) at 18.

198 See Part III(A) for discussion on the definition and interpretation of “charitable purposes” in New Zealand; for further discussion see Brakman Reiser, above n 57, at 112.

continue to satisfy this test.¹⁹⁹ Importantly, each CIC is required to submit an annual report detailing (amongst other things) the activities undertaken and how these have benefited the community, stakeholder engagement, any dividends paid and directors' remuneration.²⁰⁰

A CIC may be formed as a company limited by guarantee (similar to traditional non-profit corporations) or by shares (similar to traditional for-profit corporations).²⁰¹ If limited by guarantee, there is no share capital so profits cannot be distributed.²⁰² Rather, there are members – known as guarantors - who guarantee to meet the company's debts if it is wound up.²⁰³ If limited by shares, dividends can be distributed to shareholders, subject to a 35 percent "dividend cap".²⁰⁴ The remaining 65 percent of profits must be reinvested in the company or otherwise used for community purposes. Profit-taking is therefore permitted, but restricted. The dividend cap is designed to strike a "balance between encouraging people to invest in CICs and the principle that the assets and profits of a CIC should be

199 Department for Business, Energy & Industrial Strategy *Information and Guidance Notes: Chapter 4: Creating a Community Interest Company (CIC)*, above n 197, at 18; and Department for Business, Energy & Industrial Strategy *Information and Guidance Notes: Chapter 9: Corporate Governance* (Office of the Regulator of Community Interest Companies, May 2016) at 4.

200 Companies (Audit, Investigation and Community Enterprise) Act 2004 (UK), s 34; Community Interest Company Regulations 2005, ss 26-28; and Department for Business, Energy & Industrial Strategy *Information and Guidance Notes: Chapter 1: Introduction*, above n 194, at 3.

201 Companies (Audit, Investigation and Community Enterprise) Act 2004 (UK), s 26; see also Department for Business, Energy & Industrial Strategy *Information and Guidance Notes: Chapter 3: Limited Companies* (Office of the Regulator of Community Interest Companies, May 2016) at 3.

202 Companies (Audit, Investigation and Community Enterprise) Act 2004, sch 1; Department for Business, Energy & Industrial Strategy *Frequently Asked Questions for Funding Organisations* (Office of the Regulator of Community Interest Companies, May 2016) at 5; Esposito, above n 22, at 675; and Charu Wilkinson and others *A Map of Social Enterprises and their Eco-Systems in Europe* (European Commission, December 2014) at 56.

203 Stephen Lloyd "Transcript: Creating a CIC" (2010) 35 Vt L Rev 31 at 40-41; and Department for Business, Energy & Industrial Strategy *Information and Guidance Notes: Chapter 3: Limited Companies* (Office of the Regulator of Community Interest Companies, May 2016) at 3.

204 Companies (Audit, Investigation and Community Enterprise) Act 2004 (UK), s 30; Community Interest Company Regulations 2005, s 18; Department for Business, Energy & Industrial Strategy *Information and Guidance Notes: Chapter 6: The Asset Lock* (Office of the Regulator of Community Interest Companies, May 2016) at 9; and Lloyd, above n 203, at 33.

devoted to the benefit of the community”.²⁰⁵ The ability to raise capital in exchange for shares distinguishes CICs from charities. The overwhelming majority of CICs, however, are companies limited by guarantee.²⁰⁶

A “fundamental” feature of the CIC is the “asset lock”.²⁰⁷ This means that CIC assets must either be used in furtherance of the community purpose for which it was formed, or be transferred for full market value to another CIC or charity.²⁰⁸ Even if dissolved, the CICs assets must be distributed to another CIC or charity. This is similar to the approach for charitable entities in New Zealand.²⁰⁹ To ensure compliance with these key differentiators, the CIC Regulator has wide powers to monitor and intervene in CIC operations, which includes the power to appoint and remove directors, appoint managers, or to take steps to protect the CIC’s assets.²¹⁰ Part of the success of the CIC has been attributed to the role of the Regulator.²¹¹

The CIC is becoming increasingly popular across the United Kingdom, both for start-ups and existing organisations. Between 2021 to 2022, there was the largest number of limited company requests to convert to the CIC model since its inception in 2005.²¹² Recognition of the benefits and opportunities presented by the CIC model is thereby increasing.

205 Department for Business, Energy & Industrial Strategy *Information and Guidance Notes: Chapter 6: The Asset Lock*, above n 204, at 8.

206 Department for Business, Energy & Industrial Strategy *Information and Guidance Notes: Chapter 3: Limited Companies*, above n 203, at 4; Community Companies “Guarantee company formation” <www.communitycompanies.co.uk>; and J S Liptrap “The Dark Side of Colombia’s Benefit Corporation” (8 June 2022) University of Oxford Law Blog <www.law.ox.ac.uk>.

207 Department for Business, Energy & Industrial *Information and Guidance Notes: Chapter 6: The Asset Lock*, above n 204, at 4.

208 The Community Interest Company Regulations 2005, s 23, and schedules 1-3; Department for Business, Energy & Industrial Strategy *Information and Guidance Notes: Chapter 3: Limited Companies*, above n 203, at 7; and Department for Business, Energy & Industrial *Information and Guidance Notes: Chapter 6: The Asset Lock*, above n 204, at 4.

209 Jane Horan and others, above n 68, at 32.

210 Companies (Audit, Investigation and Community Enterprise) Act 2004 (UK), ss 42-50; and Esposito, above n 22, at 676.

211 Langford, above n 159, at 987-988.

212 Community Interest Companies, above n 193.

The CIC model has inspired other jurisdictions. In particular, it inspired the British Columbia “community contribution company” (C3), introduced in 2013 through amendments to the Business Corporations Act.²¹³ As of December 2020, over 90 companies had incorporated as C3s.²¹⁴ As small and medium-sized enterprises account for nearly all businesses in British Columbia,²¹⁵ and the population is similar to that of New Zealand,²¹⁶ it is useful to briefly compare the C3 with the CIC. Similar to the CIC, the C3’s governing features include: a stated “community benefit” purpose,²¹⁷ a dividend cap (although capped at 40 percent of annual profits),²¹⁸ an asset lock,²¹⁹ and annual reporting requirements.²²⁰ However, unlike the CIC, the C3 is required to have at least three directors (as opposed to one) and there is no dedicated state regulator providing oversight. The C3 model has been critiqued for its reliance on self-regulation.²²¹

B Benefit Corporation

Since 2010, forty United States states, have enacted legislation authorising the incorporation of a “benefit corporation” (BC).²²² Adopting the BC status is a voluntary act

213 Business Corporations Act SBC 2002 (BC), Part 2.2.

214 British Columbia Centre for Social Enterprise “Community Contribution Companies (C3)” <www.centreforsocialenterprise.com>.

215 British Columbia Ministry of Jobs, Economic Recovery and Innovation *Small Business Profile 2021* (October 2021) at 3.

216 Estimated population of British Columbia is 5.3 million as of 2022, and the estimated population of New Zealand is 5.12 million as of 2022.

217 A “community benefit” purpose is defined as a purpose beneficial to “society at large or a segment of society that is broader than the group of persons who are related to the [C3], and includes, without limitation, a purpose of providing health, social, environmental, cultural, educational, or other services”; see Business Corporations Act SBC 2002 (BC), s 51.91.

218 Business Corporations Act SBC 2002 (BC), s 51.94.

219 The “asset lock” restricts assets from being sold for less than fair market value except in the pursuit of social benefits that the entity was designed to pursue or in a transfer to another charity or C3; see Business Corporations Act SBC 2002 (BC), s 51.931; and Liao, above n 190, at 80.

220 A C3 must produce and publish an annual “community contribution” report, see Business Corporations Act SBC 2002 (BC), s 51.94.

221 Liao, above n 190, at 80.

222 Marcel Fukayama “Changing the rules of the game: Inside global policy at B Lab” (17 March 2022) B Corporation <www.bcorporation.net>.

requiring a two-thirds vote of the shareholders.²²³ There are now over 5,000 benefit corporations, including the well-known companies Allbirds²²⁴ and Patagonia.²²⁵

The legislation varies in its details between states, but all share essential elements as they are based on the Model Benefit Corporation Legislation proposed by B Lab.²²⁶ Proponents consider that the BC provides an ‘off-the-shelf’ organisational form for social entrepreneurs to run a for-profit business without fear of being sued for failing to maximise shareholder value.²²⁷

BCs differ from “traditional” corporations in three material respects. First, BCs are required to articulate a “public benefit” purpose in their constitution.²²⁸ This must include a “general public benefit”, defined as a “material positive impact on society and the environment, assessed against a third-party standard”,²²⁹ and may include, a “specific public benefit”, such as improving human health or preserving the environment.²³⁰ A “supermajority” (typically two-thirds) vote is required to amend the purpose.²³¹ This ensures the company stays mission-driven through capital raise and leadership or ownership changes.²³²

223 William H Clark and others *The Need and Rationale for the Benefit Corporation: Why is it the Legal Form that Best Addresses the Needs of Social Entrepreneurs, Investors, and, Ultimately, the Public* (White Paper PHTRANS/1101587.12, 18 January 2013) at 15.

224 Allbirds “ESG Overview” <www.ir.allbirds.com>.

225 Patagonia “B Lab” <www.patagonia.com/b-lab>.

226 Mark J Loewenstein “Benefit Corporations: A Challenge in Corporate Governance” (2013) 68 *Bus Law* 1007 at 1012; Clark and others, above n 223, at 14-20; Davide Galli and others “Signalling the Adoption of the Benefit Corporation Model: A Step towards Transparency” (2021) 13 *Sustainability* 1 at 2; Livia Ventura “Philanthropy and the For-profit Corporation: The Benefit Corporation as a New Form of Firm Altruism” (2021) 23 *EBOR* 603 at 616; and Joan MacLeod Heminway “Corporate Purpose and Litigation Risk in Publicly Held U.S. Benefit Corporations” (2017) 40 *Seattle U L Rev* 611 at 612-613.

227 Page and Katz, above n 50, at 1365.

228 Loewenstein, above n 226, at 1013.

229 Model Benefit Corporation Legislation, ss 102, 201(a); see also Loewenstein, above n 226, at 1013.

230 Model Benefit Corporation Legislation, ss 102, 201(b); see also Loewenstein, above n 226, at 1014.

231 Clark and others, above n 223, at 16.

232 Elissa Loughman “Benefit Corporation Update” Patagonia <www.patagonia.com>.

Secondly, the BC subscribes to stakeholder governance. Directors are required to consider the impact of their decisions on its shareholder and other stakeholders, such as employees, customers, suppliers, the community and the environment.²³³ Directors need not give priority to any particular interest, nor do they owe any enforceable fiduciary duties to such stakeholders, unless otherwise stated in the constitution.²³⁴

Thirdly, BCs are required to produce and publish an annual “benefit report”.²³⁵ The report must highlight the ways, and the extent to which, the company pursued its stated public benefit, and must assess its overall social and environmental performance against a third-party standard. This promotes accountability and transparency.²³⁶ To ensure compliance with these distinguishing features, enforcement is provided through “benefit enforcement proceedings” (BEP).²³⁷ Those with standing can bring a BEP against the corporation, or its directors.²³⁸ BEPs provide injunctive relief only.

The BC is often confused with the B Corp. Although both were first conceptualised by B Lab, they are fundamentally different “in the eyes of the law”.²³⁹ As mentioned, a BC is a type of legal structure authorised under state corporate law. Whereas, B Corp – as discussed in Part III – is a private third-party certification.²⁴⁰ Importantly, BCs are not required to be B Corps, and vice versa.

The recent experiences in Australia may provide useful insights for New Zealand legislators. B Lab ANZ (the Australian and New Zealand subsidiary of B Lab) strongly advocated for the creation of a benefit corporation in Australia. The proposal was based on

233 Model Benefit Corporation Legislation, s 301(a)(1); see generally Brakman Reiser, above n 57, at 114-115.

234 Section 301(a)(3).

235 Section 401(a); see generally Loewenstein, above n 226, at 1015.

236 Page and Katz, above n 50, at 1365.

237 Model Benefit Corporation Legislation, s 301(d); see also Loewenstein, above n 226, at 1020.

238 Section 305.

239 Keren G Raz “Toward an Improved Legal Form for Social Enterprise” (2012) 36 NYU RLSC 283 at 302.

240 Fairtrade International “Standards” <www.fairtrade.net>.

the United States BC and included the same distinguishing features. Although it would have introduced a new legal status through amendments to the Corporations Act 2001 (Cth), rather than a new type of company.²⁴¹ In 2020, B Lab ANZ withdrew the proposal as it failed to gain majority political, academic and societal support.²⁴² It was reasoned that the significant developments within Australia's corporate governance landscape enable organisations to adopt the essential features of the BC, without the need for legislative reform.²⁴³ In particular, existing legislation permits directors sufficient latitude to consider stakeholder interests.²⁴⁴

However, that is not to say that a hybrid legal structure is not suitable in Australia at all, it may just be that the BC model was considered unsuitable, or otherwise unnecessary. Following the withdrawal, B Lab ANZ has introduced a new requirement for all B Corps to amend their constitutions to include two clauses. The first relates to the company purpose.²⁴⁵ The second essentially implements the provision in the proposal that required directors to consider stakeholder interests when discharging their duties.²⁴⁶

Although the BC did not come into fruition in Australia, it has been introduced (or some variation thereof) in several other jurisdictions, including in Colombia, Ecuador, Peru,

241 Ian Ramsay and Mihika Upadhyaya "The Failed Attempt to Enact Benefit Legislation in Australia and the Rise of B Corps" (1 March 2021) Social Science Research Network (SSRN) <www.papers.ssrn.com> at 2; and B Lab Australia and New Zealand, above n 167, at 25.

242 B Corporation "The evolution of benefit company reform in Australia" (1 September 2020) <www.bcorporation.com.au>.

243 Langford, above n 159, at 978; Ramsay and Upadhyaya, above n 241, at 15; Klettner, above n 116, at 343; and B Corporation, above n 242.

244 Mayer, above n 149, at 4.

245 The purpose clause must state (or the effect) that "the purpose of the Company is to deliver returns to shareholders whilst having an overall positive impact on society and the environment"; see B Corporation "The B Corp legal requirement" <www.bcorporation.net>.

246 See B Corporation, above n 245; and Ramsay and Upadhyaya, above n 241, at 16.

British Columbia, France, Italy and Rwanda.²⁴⁷ According to B Lab, there are now over 10,000 BCs worldwide.²⁴⁸

In summary, this part has surveyed the distinguishing features of two hybrid legal structures: the United Kingdom CIC and the United States BC. These hybrid legal structures provide non-profits with the ability to generate equity capital and make a profit, and for-profits with the ability to consider stakeholder interests beyond that which is available under the traditional LLC and the accompanying shareholder primacy norm.²⁴⁹ This analysis provides a foundation upon which a fit-for-purpose structure could be built on in New Zealand.

VI Unlocking the Potential of Social Enterprise

Social enterprises have the ability to create real and sustainable impact, providing innovative solutions to wide-ranging social problems. However, the current legal structures in New Zealand are hindering social enterprises from being able to reach their full potential.²⁵⁰ Although there are exceptions, these structures have failed to provide the necessary recognition and support for social enterprises.²⁵¹ Jeffs considers that new legal structures, amongst other things, will be required if New Zealand social enterprises are to achieve their full potential.²⁵²

There is therefore a growing need to introduce a specialist legal structure to enable and encourage the growth of the social enterprise sector.²⁵³ Liao argues that “hybrids may be a key contributor to establishing critical infrastructure to help solve some of the most

247 B Lab Australia and New Zealand “Stakeholder Governance: Making business accountable to people and planet” <www.bcorporation.com.au>; and Livia Ventura, above n 226, at 606.

248 Ngwing Kimani “Rwanda Becomes 6th Country in the World to Pass Law on Conscious Business Practices” B Lab Africa <www.b-labafrika.net>.

249 Liao, above n 10, at 292.

250 Jane Horan and others, above n 68, at 4; and Kartikasari, Gan and Kerr, above n 15, at 630.

251 Jeffs, above n 11, at 1.

252 Jeffs, above n 11, at 2.

253 Kartikasari, Gan and Kerr, above n 15, at 630.

pressing social and environmental issues of our time”.²⁵⁴ Against this background, this part explores the potential benefits and risks that may flow from the introduction of a legal structure designed specifically for social enterprises.

A Potential Benefits

1 Signalling

The *Impact Initiative Report* observed that one of the “most resounding disadvantages of the existing legal structures is the lack of ability to signal...the primacy of impact for [social enterprise]”.²⁵⁵ A major benefit of a hybrid structure is that it provides a clear and inexpensive signal to those who share in its social mission, such as consumers and investors.²⁵⁶ Morgan observed that hybrid structures provide “a notably efficient shortcut” to the signalling process.²⁵⁷ For example, all CICs must include “Community Interest Company” or “c.i.c” at the end of their name.²⁵⁸ This has significant branding value and clearly distinguishes the entity from a traditional company which, in New Zealand, must include “Limited” or “Ltd” at the end of their name.²⁵⁹ This must be displayed on every written communication sent by the company (such as emails and letters) and on every document recording the obligations of the company (such as contracts and deeds).²⁶⁰

Having a distinguishable identity for social enterprise is beneficial, given their very nature is to be different.²⁶¹ A quantitative study carried out in British Columbia found that the main reason for adopting the C3 structure was for its “marketing and branding value”.²⁶²

254 Liao, above n 10, at 275.

255 Jane Horan and others, above n 68, at 30.

256 Page and Katz, above n 50, at 1374; see also B Lab Australia and New Zealand, above n 159, at 9.

257 Bronwen Morgan “Legal Models Beyond the Corporation in Australia: Plugging a Gap or Weaving a Tapestry?” (2018) 14 SEJ 180 at 190; and Ramsay and Upadhyaya, above n 241, at 14.

258 Companies (Audit, Investigation and Community Enterprise) Act 2004 (UK), s 33.

259 Companies Act 1993, s 21.

260 Section 25.

261 Charu Wilkinson and others, above n 202, at 61; and Suntae Kim and others “Why Companies Are Becoming B Corporations” (17 June 2016) Harvard Business Review <www.hbr.org>.

262 Bridget Horel *Community Contribution Companies in British Columbia: MBA Research Summary* (BC Centre for Social Enterprise, 30 August 2016) at 2.

The majority of respondents identified that “part of the reason for selecting the C3 model was because the structure itself publicly demonstrates a strong commitment to giving back to the community”.²⁶³ This gives social enterprises a sense of legitimacy, which is favourable given that consumers increasingly prefer to purchase from organisations with a social mission, but at the same time are increasingly sceptical of “greenwashing” (false or misleading claims about a company’s environmental responsibility) and “social washing” (false or misleading claims about a company’s social responsibility).²⁶⁴

2 *Lower transaction costs*

Presently, social entrepreneurs are having to rely on “expensive creative lawyering”²⁶⁵ to manipulate existing legal structures and convey commitments beyond mere profits. These transaction costs could be avoided if a hybrid structure was available offering ease of registration. Katz and Page observe that “there would be fewer wheels for social entrepreneurs and their [lawyers] to reinvent”.²⁶⁶ As the structures become widely recognisable, there would be less need for social entrepreneurs to explain them, especially to potential investors.²⁶⁷ Clear and consistent legal requirements would also provide investors with reassurances that would allow them to confidently invest in social enterprises.²⁶⁸

3 *Catalysing the development of a professional community*

Introducing a “brand” for social enterprise - as a distinct entity - may address other concerns shared by social entrepreneurs, such as difficulties in accessing adequate funding.²⁶⁹ Morgan suggested that the introduction of hybrid structures would likely lead to the creation of a fully developed professional community to support social enterprise,

263 Horel, above n 262, at 2.

264 Page and Katz, above n 50, at 1374; and Clark and others, above n 223, at 2.

265 Jane Horan and others, above n 68, at 11.

266 Page and Katz, above n 50, at 1373.

267 Page and Katz, above n 50, at 1373.

268 See generally B Lab Australia and New Zealand, above n 159, at 9-10; Charu Wilkinson and others, above n 202, at 61; and Aurélien Loric “Designing a Legal Vehicle for Social Enterprises: An Issue Spotting Exercise” (2013) 5 CJTL 100 at 127.

269 Moe, above n 67, at 53.

comprising of lawyers, accountants, business planners and tax advisors.²⁷⁰ This may make it easier to obtain tailored legal and business advice. Investment may also be encouraged as investors would be able to attain a greater understanding of this option.²⁷¹

4 *Increasing the demand for the structure itself*

A further potential advantage of introducing a hybrid structure is to increase demand for the structure itself and, with it, the prevalence of socially beneficial activity.²⁷² Social entrepreneurs, when presented with a variety of organisational forms, may find that the forms suit their business better than the existing options.²⁷³ This will likely be the case in New Zealand, given that the current structures have been identified as a barrier.²⁷⁴ Creating a more enabling, supportive environment may “attract new people towards establishing a social enterprise, so boosting entrepreneurship and economic growth within the social economy”.²⁷⁵ Demand for both the CIC and BC models have proliferated since their introduction, with the benefits and opportunities becoming increasingly realised amongst the business community.

All these factors call for the introduction of a hybrid legal structure.²⁷⁶ However, these potential benefits need to be balanced against the potential risks, as discussed in the next part.

270 Morgan, above n 257, at 190-191; and Ramsay and Upadhyaya, above n 241, at 14.

271 Moe, above n 67, at 55; see also Loric, above n 268, at 127.

272 Page and Katz, above n 50, at 1373.

273 Page and Katz, above n 50, at 1373; and Loric, above n 268, at 132.

274 Jane Horan and others, above n 68, at 4; see also Mandow, above n 139.

275 Employee Ownership Australia and New Zealand *Submission to the Social Impact Investing Discussion Paper* (2017) at 3; see also Orrick, UnLtd and Thomson Reuters Foundation *Balancing Purpose and Profit: Legal Mechanisms to Lock in Social Mission for “Profit with Purpose” Businesses across the G8* (2 December 2014) at 3; Morgan, above n 257, at 191; Page and Katz, above n 50, at 1374; and Clark and others, above n 223, at 6.

276 Orrick, UnLtd and Thomson Reuters, above n 275, at 3; Morgan, above n 257, at 191; Page and Katz, above n 50, at 1374; Clark and others, above n 223, at 6; Kartikasari, Gan and Kerr, above n 15, at 630; and B Lab Australia and New Zealand, above n 159, at 9-12.

B Potential Risks

1 Impact on traditional for-profits and non-profits

Commentators to the literature have raised concerns that a hybrid structure would be regressive on for-profits and non-profits.²⁷⁷ Regarding for-profits, there is a risk that a new structure may give traditional companies a “license to operate poorly” by transferring the responsibility to operate in a socially beneficial manner onto social enterprise.²⁷⁸ A hybrid structure may isolate the work of social enterprise as something “they do”, leaving traditional companies to focus solely on profit maximisation.²⁷⁹ A hybrid structure would, the argument goes, extend the dichotomy between “good” and “bad” companies, when socially beneficial purposes are something that all companies should be pursuing.²⁸⁰ It is reasonable for this to be of concern. However, a hybrid structure may work to put more pressure on traditional companies to operate in a socially beneficial manner, especially as consumer preferences continue to shift. As with the B Corp status, a hybrid structure may create a market incentive for companies to incorporate for socially beneficial purposes.²⁸¹ As mentioned, in the United Kingdom, the prevalence of limited companies requesting the switch to the CIC model is increasing.²⁸²

Conversely, regarding non-profits, there is concern that a new structure may divert resources from the non-profit sector, instead of attracting resources that would otherwise go to the for-profit sector.²⁸³ For example, those who would ordinarily donate to charities, may instead, choose to invest in a social enterprise, rather than those who would ordinarily

277 Barrett, above n 46, at 263; and Ramsay and Upadhyaya, above n 241, at 14.

278 Morgan, above n 257, at 190; Ramsay and Upadhyaya, above n 241, at 14; and B Corporation, above n 242.

279 Steven Moe “The social enterprise sector comes of age” *The Spinoff* (online ed, New Zealand, 18 October 2018).

280 Mark Underberg “Benefit Corporations vs. “Regular” Corporations: A Harmful Dichotomy” (13 May 2012) Harvard Law School Forum on Corporate Governance <www.corpgov.law.harvard.edu>.

281 Susan Gary and others, above n 84, at 10.

282 Community Interest Companies. above n 193.

283 Page and Katz, above n 50, at 1374.

invest in a company choosing to reinvest in a social enterprise.²⁸⁴ Whilst this is a valid concern, there does not appear to be any evidence to suggest that this has materialised in jurisdictions where hybrid forms have been introduced.²⁸⁵

2 *Social washing concerns*

Some further commentators have suggested that hybrid structures may increase the risk of “social washing”, in other words, organisations adopting the structure and deriving its benefits, but in reality, they are no more socially responsible than traditional companies.²⁸⁶ For example, the BC – by only mandating the creation of a “general public benefit” – can encompass a wide variety of activities.²⁸⁷ Liao observes that many businesses would satisfy this definition, “with little change to the status quo”.²⁸⁸ However, additional mechanisms built into the BC model sufficiently address these concerns. For example, the “general public benefit” must be assessed against an independent third-party standard, as well as the regular reporting requirements and effective enforcement mechanisms.²⁸⁹ For this reason, other commentators suggest that hybrid structures effectively address the current concerns over “social washing”.²⁹⁰ Presently, any organisation could market themselves as a social enterprise. A hybrid structure, with appropriate features and restrictions, may legitimise the social orientation of an organisation’s activities.

Whilst deserving of consideration, these risks may still be worth taking. Indeed, they have been for some-fifty jurisdictions that have introduced a hybrid structure.²⁹¹ Jeffs argues that the failure of New Zealand to keep pace “reflects the failure of successive New Zealand

284 Barrett, above n 46, at 263.

285 Barrett, above n 46, at 263.

286 Page and Katz, above n 50, at 1374.

287 Loric, above n 268, at 125.

288 Carol Liao “A Critical Canadian Perspective on the Benefit Corporation” (2017) 40 *Seattle U L Rev* 683 at 714.

289 Clark and others, above n 223, at 17; see generally Jane Horan and others, above n 68, at 31.

290 Carol Liao “Early Lessons in Social Enterprise Law” in Benjamin Means and Joseph W Yockey (eds) *The Cambridge Handbook of Social Enterprise Law* (Cambridge University Press, Cambridge, 2019) 101 at 103; Page and Katz, above n 50, at 1375; and Charu Wilkinson and others, above n 202, at 61.

291 B Lab Australia and New Zealand, above n 247.

Governments, and the wider society, to encourage and support new approaches” to business.²⁹² With New Zealand’s reputation for being innovative (known as “kiwi ingenuity”), socially aligned and environmentally friendly, a hybrid legal structure would seem like a natural fit.

As a practical matter, a new structure seems more politically viable than, for example, legislation requiring all companies to incorporate for, and pursue, a socially beneficial purpose. The decision to adopt the structure would be wholly voluntary. A social enterprise would not be required to, but they would, at least, have the option. Although commentators have suggested that a hybrid structure may be an intermediate step towards a future where all companies are required to incorporate for, and pursue, a socially beneficial purpose.²⁹³ Indeed, traditional companies have a lot to learn from social enterprises. Recent developments in the corporate governance landscape coupled with looming global crises mean that such a possibility cannot (and should not) be ruled out. But, for now, priority should be given to a hybrid structure for social enterprises. The next part analyses how this could be achieved.

VII Introducing the “Impact Company”

Drawing from the existing hybrid structures – the CIC and the BC – and the related academic commentary, this part proposes a framework designed specifically for New Zealand social enterprises. For consistency, the name used in the *Impact Initiative Report* is adopted: the “Impact Company”.²⁹⁴ This part provides a practical, high-level, discussion of the governing features. It does not intend to delineate all the details. Indeed, several important questions remain, such as whether tax laws should be amended to accommodate this model. However, it introduces a framework that can be built upon in subsequent research and policy work.

292 Jeffs, above n 11, at 5.

293 Mayer, above n 149, at 2; and Steven Moe “The bottom line is not enough, companies should be required to have a purpose” in Steven Moe *Laying Foundations for Reimagining Business* (Seeds Press, Christchurch (NZ), 2021) 11 at 12.

294 Jane Horan and others, above n 68, at 29.

New Zealand – by playing catch up – is arguably in an advantageous position where it can draw from the existing models to develop a framework that is not only better, but is tailored to New Zealand’s unique business landscape. The delay in acting could therefore be translated into a latecomer advantage. As mentioned, the term social enterprise is new within Te Ao Māori, but the concept of pursuing broad social goals for community benefits has been practiced for generations.²⁹⁵ The dual objectives of social enterprise resonate with the historical and contemporary models of business within Te Ao Māori.²⁹⁶ This provides an opportunity to partner with Māori and iwi enterprise to develop a holistic framework suitable for New Zealand.²⁹⁷

A Suitability of the Existing Hybrid Legal Structures

Part V examined the distinguishing features of two existing hybrid structures: the United Kingdom CIC and the United States BC. A key difference between the two is that the United Kingdom view social enterprises as an alternative to traditional charities, while the United States has embraced a broader view of social enterprises as an emerging fourth sector.²⁹⁸ This difference is reflected in the features of each model. For example, the asset lock and dividend cap which are “fundamental” to the CIC, are likely to be viewed as too restrictive for those currently operating within the for-profit sector. When compared to the CIC, the BC provides entrepreneurs and investors with much greater flexibility, particularly with respect to governance and distribution of profits and assets.²⁹⁹ However, this flexibility means that the BC model arguably lacks some of the necessary protections for social enterprise. For example, there is no legal obligation to reinvest profits/surpluses

295 McMeeking, Grant and Melrose, above n 4, at 3.

296 McMeeking, Grant and Melrose, above n 4, at 3; and Kartikasari, Gan and Kerr, above n 15, at 629.

297 See Steven Moe and Wayne Tukiri “What social enterprises in Aotearoa can learn from Māoritanga” *The Spinoff* (online ed, New Zealand, 21 August 2018); Joseph and Benton, above n 15, at 46-47; and Kartikasari, Gan and Kerr, above n 15, at 628-629.

298 Esposito, above n 22, at 646-647.

299 Kartikasari, Gan and Kerr, above n 15, at 630.

or otherwise direct them to social purposes.³⁰⁰ This fails to satisfy the practical definition of a social enterprise provided by the DIA, as outlined in part II.

While both models provide valuable insights, the CIC model is preferable, although some of its features should be relaxed to prevent the stifling of investment.³⁰¹ The CIC was primarily designed for use by small-scale community-based organisations. This is likely to be more suitable to New Zealand's business environment, given the vast majority of businesses are small and medium-sized enterprises.³⁰² Furthermore, the majority of New Zealand social enterprises have defaulted to the charitable trust structure.³⁰³ A CIC-like model would provide such organisations with the ability to raise equity capital and return a share of the profits, while preserving social mission.

B Governing Features

The impact company would be a variant of the LLC, and would therefore enjoy the benefits of separate legal personality and limited liability – two features that are familiar and well-understood by the business community.³⁰⁴ Its introduction would be achieved through amendments to the Companies Act.³⁰⁵ These amendments would allow an organisation to voluntarily incorporate as an impact company, provided certain criteria are satisfied – in addition to those of a traditional company. The model would be easy to facilitate in policy terms and would operate within the existing regulatory framework. Crucially, the adopted name – the “impact company” – clearly distinguishes the entity from a traditional company. The following discussion explores some of the governing features of the impact company.

300 Liao, above n 288, at 714.

301 Lloyd, above n 203, at 33.

302 Barrett and Feehily, above n 148, at [1.3].

303 Department of Internal Affairs, above n 25, at 6.

304 See Companies Act 1993, ss 15 and 97.

305 Companies Act 1993.

1 *Embedded social purpose*

Unlike a traditional company, an impact company would be required to have a constitution.³⁰⁶ The “social purpose”³⁰⁷ of the impact company would be required to be articulated in the constitution. The social purpose would be required to meet a threshold, defined in law. Existing examples include the “community interest test” in the United Kingdom, which adopts a “reasonable person” standard and is administered by the CIC regulator,³⁰⁸ and the “general public benefit purpose” in the United States, which adopts a “material positive benefit” standard and must be assessed against a third-party standard.³⁰⁹

When determining the appropriate threshold, it is important to balance the need for certainty against the need for flexibility. The law should avoid being overly prescriptive or restrictive. The threshold must permit a broad range of activities that may be undertaken for the benefit of the community. It must therefore be wider – or at least more flexible in its scope - than the definition of “charitable purposes”.³¹⁰ For example, it should encompass the United Nations SDGs, which as discussed in Part III(A) generally would not satisfy the strict requirements of “charitable purposes”.³¹¹ However, setting it too wide may dilute the purpose sought to be achieved. A possible option would be a “purpose beneficial to the community at large, or to a particular section of the community, that may include, but without limitation to, a purpose of providing health, environmental, cultural or educational goods and/or services”. As mentioned below, a government agency – such as the Ministry of Business, Innovation and Employment (MBIE) - should have the responsibility to approve each entity’s purpose.

306 See for comparison Companies Act 1993, s 26.

307 This Paper uses the term “social purpose” to refer to the organisations governing/founding social mission, see for comparison “community benefit purpose” in the United Kingdom or “general public benefit” in the United States.

308 Companies (Audit, Investigation and Community Enterprise) Act 2004 (UK), ss 27, 35(2), and 38; and Department for Business, Energy & Industrial Strategy *Information and Guidance Notes: Chapter 4: Creating a Community Interest Company (CIC)*, above n 197, at 18.

309 Model Benefit Corporation Legislation, ss 102, 201(a); see also Loewenstein, above n 226, at 1013.

310 See Charitable Trusts Act 1957, s 2; and Charities Act 2005, s 5(1).

311 Susan Gary and others, above n 84, at 10.

2 *Dividend cap*

An impact company will be able to attract the same types of capital as a traditional company. Given the majority of social enterprises in New Zealand have “defaulted” to charitable forms,³¹² the ability to attract equity capital and return profits to shareholders will be beneficial. However, dividends should be capped to ensure profit-making is not (or does not become) the primary objective.³¹³ An appropriate dividend cap will enable sustainable financing, while reassuring investors – and other stakeholders – that the entity is committed to trading for a social purpose. This is important for instilling public trust and confidence. The challenge, however, is setting the cap at the appropriate level. Existing examples include the 35 percent dividend cap in the United Kingdom,³¹⁴ and the 40 percent dividend cap in British Columbia.³¹⁵ In both jurisdictions, the majority of profits must be reinvested or otherwise used for social purposes, which satisfies the DIA’s criteria of a social enterprise.³¹⁶

As discussed, the overwhelming majority of CICs are companies limited by guarantee, and thus, are not subject to the dividend cap.³¹⁷ Given that all companies in New Zealand are limited by shares, a 40 percent dividend cap may be more appropriate. An impact company could decide to bind itself to a dividend cap at any level within this range, for example, a 25 percent cap. To encourage private investment following its introduction, temporary tax relief could be introduced – similar to the Social Investment Tax Relief in the United Kingdom.³¹⁸

312 Department of Internal Affairs, above n 25, at 6.

313 Moe, above n 67, at 54.

314 Companies (Audit, Investigation and Community Enterprise) Act 2004 (UK), s 30; The Community Interest Company Regulations 2005, s 18; and Department for Business, Energy & Industrial Strategy *Information and Guidance Notes: Chapter 6: The Asset Lock*, above n 204, at 9.

315 Business Corporations Act SBC 2002 (CA), s 51.94.

316 Department of Internal Affairs, above n 25, at 6; see generally Carol Liao, above n 290, at 103.

317 Department for Business, Energy & Industrial Strategy *Information and Guidance Notes: Chapter 3: Limited Companies*, above n 206, at 4; Liptrap, above n 206; and Community Companies, above n 206.

318 See Social Investment Tax Relief “SITR has been extended to 2023” <www.getsittr.org.uk>; see further Charu Wilkinson and others, above n 202, at 67.

3 *Directors' duties*

In terms of directors' duties, impact company directors should be guided by a duty to ensure that the company continues to satisfy the "social purpose" test.³¹⁹ Implicit in this is the assurance that the company is financially prudent, and thus will continue to advance its social purpose indefinitely. Beyond this, impact company directors should be subject to the general duties of directors under the Companies Act.³²⁰ The most important in this context are the duty of good faith,³²¹ the duty of care,³²² and the duty to comply with the Act and the constitution.³²³ Langford observes that the interpretation of these duties is informed by the entity's social purpose, as articulated in the constitution.³²⁴ It is useful to briefly discuss and respond to some common concerns relating to the application of these duties in this context.

In terms of the duty of good faith, the Companies (Directors Duties) Amendment Bill – if passed – will clarify that a director, when determining the best interests of the company, may take into account ESG factors during decision-making.³²⁵ Thus, a director will not be in breach of their duty of good faith if they do so. This is certainly helpful for impact company directors, given the broad range of objectives they act for, beyond commercial profit. For further clarity, an additional provision to the effect that "the creation of the "social benefit" is in the best interests of the impact company" should also be considered.³²⁶

In terms of the duty of care, Langford found that a director would not necessarily breach its duty of care if it failed to achieve its stated "social purpose", for example, to ensure no

319 See for comparison Department for Business, Energy & Industrial Strategy *Information and Guidance Notes: Chapter 4: Creating a Community Interest Company (CIC)*, above n 197, at 18.

320 Companies Act 1993, ss 131-138A.

321 Section 131.

322 Section 137.

323 Section 134.

324 Langford, above n 151, at 956.

325 Companies (Directors Duties) Amendment Bill 2021 (75-1), cl 4.

326 See for comparison Model Benefit Corporation Legislation, s 201(c).

child is at school hungry,³²⁷ provided they applied reasonable care, diligence and skill in seeking to achieve that purpose.³²⁸ Finally, the duty to comply with the Act and the constitution would require directors to act in accordance with the stated purpose, and with any additional requirements, such as annual reporting – as discussed below. Causing or allowing the company to depart from its stated social purpose would therefore be a breach of this duty.³²⁹

4 Reporting requirements

An impact company should be accountable to and transparent with all stakeholders.³³⁰ This could be achieved through annual reporting requirements, beyond those of a traditional company. An impact company should be required to report on both social and financial mandates – not too dissimilar from registered charities.³³¹ The report should be delivered to shareholders and made publicly available, for example, through the company’s website. The report should highlight (amongst other things) the specific actions undertaken in pursuit of the social purpose, an evaluation of the social impact achieved and an outlook on activities proposed for the following year.³³² Both the United Kingdom “community interest company report”³³³ and the United States “benefit report”³³⁴ provide useful guidelines.

Developing a set of consistent, comprehensive and comparable reporting standards will contribute to building public trust and confidence in the impact company brand, which is particularly important for investment purposes. It is unlikely that these additional reporting

327 See for comparison Eat my Lunch “Our Story” <www.eatmylunch.nz>.

328 Langford, above n 159, at 992-993.

329 Companies Act 1993, s 134.

330 Mara Del Baldo “Acting as a benefit corporation and a B Corp to responsibly pursue private and public benefits. The case of Paradisi Srl (Italy)” (2019) 4 Intl J Corp Soc 1 at 6.

331 Registered charities are required to file both an annual return and financial statements (Tiers 1 and 2) or a performance report (Tiers 3 and 4); see Charities Services “Annual reporting is crucial and here’s what you need to know” (20 January 2022) <www.charities.govt.nz>.

332 Del Baldo, above n 330, at 6.

333 See Companies (Audit, Investigation and Community Enterprise) Act 2004 (UK), s 34; and Community Interest Company Regulations 2005, ss 26-28.

334 Model Benefit Corporation Legislation, s 401(a); see generally Loewenstein, above n 226, at 1015.

requirements would be too onerous, given that many social entrepreneurs already voluntarily undertake to report on their social impact.

5 Dedicated government or third-party regulator

To support the integrity of the new structure, it would be advantageous to appoint a dedicated impact company regulator, or some other third-party agency, who would have the primary responsibility to provide oversight and ensure compliance. As mentioned, the C3 model has been critiqued for its absence of a dedicated regulator.³³⁵ Streamlining the responsibility for social enterprises will likely support the development of the sector. Given that the impact company would be governed under the Companies Act, it would be most practical for the regulator to be a subset of the Companies Office, which is part of the MBIE.³³⁶ Similar to both companies and charities, it would also be beneficial for impact companies to have their own, publicly accessible, register.³³⁷ This would allow the public to search for impact companies, and would enable the government to track the growth of the sector.

6 Possible fiscal incentives

The CIC and the BC are taxed at the same rate as traditional for-profit companies. In New Zealand, the corporate income tax rate is 28 percent.³³⁸ Despite this, there is a strong argument that those who are dedicating a substantial proportion of profits to a community benefit should be entitled to some preferential tax benefits.³³⁹ The government often derives direct economic benefits from social enterprises. For example, by employing differently abled, or people who would otherwise be considered “unemployable”, the government directly benefits from lower welfare spending.³⁴⁰ Perhaps a special tax rate

335 Liao, above n 190, at 80.

336 Ākina Foundation, above n 66, at 40.

337 See New Zealand Companies Office “Companies Register” <www.companies-register.companiesoffice.govt.nz>; and Charitable Trusts “Charitable Trusts Register” <www.ct-register.companiesoffice.govt.nz>.

338 Inland Revenue Department “Tax rates for businesses” (14 May 2021) <www.ird.govt.nz>.

339 Moe, above n 67, at 58-59.

340 Jeffs, above n 11, at 15.

could be introduced, that is between that which applies to charities (zero) and companies (28 percent). This could be applied to the proportion of profits that are being devoted to the community.³⁴¹ This would better reflect the dual nature of impact companies. Alternatively, some other fiscal incentive could be introduced, such as wage subsidies to compensate for the potential loss of productivity.³⁴² Further research evaluating possible options is required.

In summary, this part has proposed a legal framework for social enterprise. It has advocated for the introduction of a hybrid legal structure that accommodates the unique features of social enterprises. This will create a more enabling, supportive environment for organisations to pursue social impact through business, and will help to catalyse the shift in how social enterprise is viewed by investors, consumers and the broader public.³⁴³

VIII Conclusion

The social enterprise movement represents more than just a passing trend.³⁴⁴ Social enterprises are hybrid – purpose-driven – organisations that use commercial strategies to achieve a paramount social mission that benefits the community at large, or a particular section of the community. This provides a promising alternative to mainstream business approaches, and is becoming increasingly important as we work to solve some of our most complex and pressing social issues – such as poverty, unemployment and waste.

By providing market-based and scalable solutions, social enterprises have the ability to create real and sustainable impact. However, the sector is currently constrained by outdated legal frameworks that do not adequately accommodate entities that wish to pursue both social and economic value creation.³⁴⁵ The company form, and the accompanying

341 Moe, above n 67, at 59.

342 See Charu Wilkinson and others, above n 202, at 63-66 for overview of fiscal benefits attached to social enterprise legal forms and statuses in Europe.

343 Moe, above n 144, at 51. 144

344 Boyle Mathieson Lawyers, above n 28, at 2.

345 Barrett, above n 46, at 270; Jane Horan and others, above n 68, at 4; and Kartikasari, Gan and Kerr, above n 15, at 628.

shareholder primacy norm, creates legal uncertainty for social enterprises. Many social enterprises are having to rely on “expensive creative lawyering” to manipulate the company form and to convey commitments beyond mere profits.³⁴⁶ By their very nature, social enterprises want their point of difference to be known to external stakeholders, such as consumers and financiers.

This paper has analysed two hybrid structures: the United Kingdom CIC and the United States BC. These structures bridge the gap between the for-profit and non-profit sectors. They enable for-profits to pursue a social mission and to integrate stakeholder interests into their business operations, beyond that which is available under the traditional LLC and the accompanying shareholder primacy norm, and provide non-profits with the ability to raise equity capital and return profits. While each has its proponents and critics, they provide a legal basis for social enterprises – and other purpose-driven businesses – to simultaneously pursue a social mission and profit-making. Since being introduced, these structures have become increasingly embraced by both start-ups and existing businesses, and have subsequently been enacted (or some variation thereof) in other jurisdictions.³⁴⁷

The New Zealand government has been aware of the inadequacy of the current legal structures for social enterprise from as early as 2013.³⁴⁸ There have been repeatedly observed concerns that such structures are hindering the growth of the sector.³⁴⁹ The government has the opportunity to create an enabling, supportive environment for social enterprises – and other purpose-driven businesses – by dismantling the barriers that are currently restraining them. While previous governments have ruled out the need to do so, amidst rising social problems, we must continue to “challenge the “powerful but inaccurate myth” that there is only one appropriate form of organising collective economic activity

346 Jane Horan and others, above n 68, at 11.

347 See Part V for discussion.

348 Department of Internal Affairs, above n 25; Department of Internal Affairs, above n 7; see also Kartikasari, Gan and Kerr, above n 15, at 628-629; and Mandow, above n 139.

349 See Jeffs, above n 11, at 15; Jane Horan and others, above n 68, at 4, 8, and 20; and Kartikasari, Gan and Kerr, above n 15, at 628-629.

and that it corresponds to the shareholder-driven model of the limited liability firm”.³⁵⁰
We need organisational law that is fit-for-purpose for twenty-first century business.

This paper has advocated for the introduction of a hybrid legal structure: the “impact company”. The impact company will be a variant of the LLC but with additional features tailored to social enterprise so as to maximise their impact. Drawing from the existing hybrid structures, and the related academic commentary, the governing features of the impact company should include: an embedded social purpose, a dividend cap, expanded directors’ duties, annual reporting requirements, a dedicated regulator and possible fiscal incentives. The impact company will raise the profile of the social enterprise sector and provide a means to empower those who want to simultaneously pursue profit and purpose. Developing useful legal frameworks also demonstrates the government’s willingness to support and encourage the establishment and operation of social enterprises, and recognises the contribution that they can make to improved economic and social wellbeing. The goal must be to make it just as easy – if not easier - to establish and operate a social enterprise as it is for a traditional company. When faced with rising social problems, we must be open to new ideas and be willing to affect structural changes.

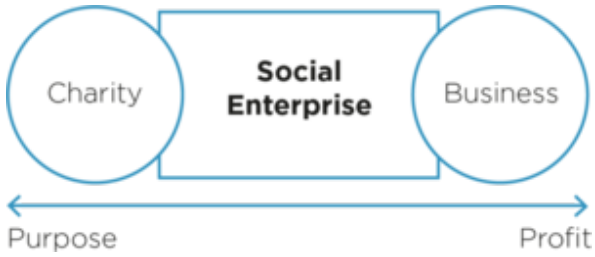
Word count

The text of this paper (excluding table of contents, footnotes, appendix and bibliography) comprises approximately 11,853 words.

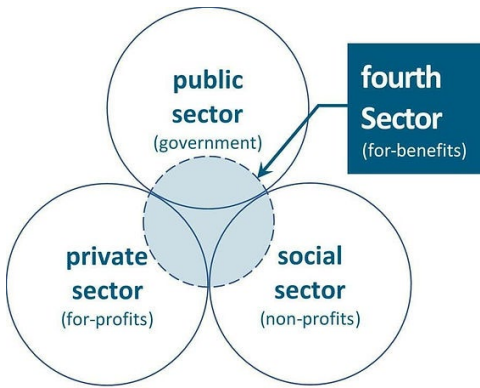
350 Boeger and Villiers, above n 155, at 4 and 284.

IX Appendix

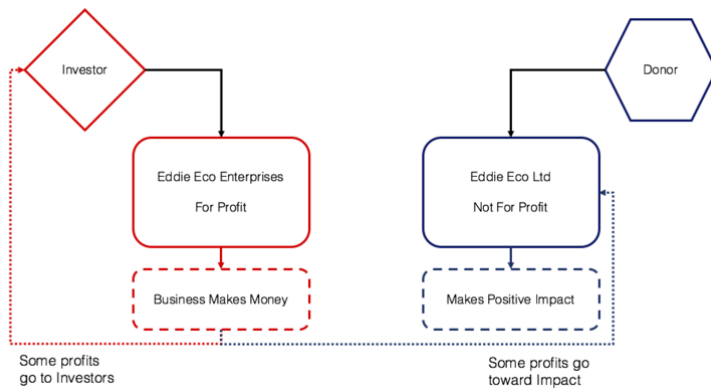
A Continuum Model³⁵¹



B Venn Diagram: Four Sector Economy³⁵²



C Dual Entity Structure Example³⁵³



351 Ākina Foundation, above n 26.

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