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SOCIAL ENTERPRISES IN UK AND ITALY: RESOURCE MIX AND LEGAL FRAMEWORK ANALYSIS

Bachelor Thesis | Bilyana Vencheva

Resource mixes within Social Enterprises in relation to the operating legal framework:

Focus on UK and Italy

Bachelor Thesis

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Abstract:

In the recent decades researchers have focused their attention on the increasing importance of the social company which can be considered a hybrid between the traditional business and not for profit sector (Davis, 1997). This relatively new type of venture has assumed the social mission as the leading pillar in its value creation process, incorporating business practices in order to obtain more efficiency in resource utilization. This relatively new type of venture has assumed the social mission as the leading pillar in its value creation process, incorporating business practices in order to obtain more efficiency in resource utilization. Government has recognized the comparative advantage of social enterprises in the provision of certain services. This resulted in the establishment of more institutional arrangements and regulations that aimed at legally defining community businesses role in the society and providing more incentives for future development. As any other enterprises, social companies are concerned with and thus put an uttermost importance on the access to financial and non-financial resources that would enable future development. Resource mix defines the flexibility of an enterprise and proper financial management is essential for sustainability of the social enterprise. Resource mobilization ranges from financial grants and subsidies provided mainly by government in support of the social enterprise mission, to income generating trading activities that facilitate self-sufficiency and independence from the public aid and extend further to include non-financial resources such as volunteering. The scientific publications tend to be more descriptive and only briefly mention on the interrelation between the legal environment and resource mix mobilization. The paper addresses this gap. It aims at combining the available knowledge and introducing a more explicit structure of social enterprise`s resource mixes within which such interactions and their effects can be analyzed. It aims at identifying the main channels through which the institutional environment affects resource mixes utilization within social enterprises, with a focus on Italy and UK.

Key words: enterprise, social enterprise, legal forms, resource mix, UK, Italy

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I. Introduction

The recent banking crisis has shattered the belief in the effectiveness and efficiency of the markets. The general public has challenged the desirability of the system and its implications for sustainability. People have started contemplating the applicability of another model through which wealth creation comes along with consideration for community values. The view of pure profit maximizing behavior of firms has created more pressure in the wake of the economic crisis. It led to heated discussions with regard to the main functions and responsibilities of the contemporary corporations and enterprises. The nascent dispute that an enterprise should be predominantly in service of the community and be able to sacrifice short term profit for the benefit of more stable social environment is beyond the scope of the paper, nevertheless, it proves interesting basis for considering the emergence of new types of initiatives – the social enterprises.

In the recent decades researchers have focused their attention on the increasing importance of the social company which can be considered a hybrid between the traditional business and not for profit sector (Davis, 1997). This relatively new type of venture has assumed the social mission as the leading pillar in its value creation process, incorporating business practices in order to obtain more efficiency in resource utilization. Unlike their commercial counterparts, social enterprises are also likely to flourish in adverse economic conditions which tend to intensify community needs (Austin, Stevensonand Wei-Skillern, 2006). This reflects the idea that they have deep devotion to the desire to improve social wellbeing for the most disadvantaged groups in the community thus serving the social mission undertaken. Indeed, social entrepreneurial activity as opposed to commercial businesses has manifested an increase within the most deprived regions in the United Kingdom (Harding, 2006). Social entrepreneurs engage in all kinds of community programs mainly targeting local disadvantaged groups, minorities, providing training, skills and other services. They contribute to the social and economic improvement of the society in downturns and consolidate social cohesion in when economy is booming. Moreover, the employment of innovative business practices alongside social value preservation can prove to be a source of increased efficiency for social enterprises in the provision of public goods.

Government has recognized the comparative advantage of social enterprises in the provision of certain traditionally state supported services. This is relevant in particular to more developed European countries such as UK, Italy, Belgium and The Netherlands. This resulted in the establishment of more institutional arrangements and regulations that aimed at legally defining their role in the society and providing more incentives for future development. The European Commission (2011), for instance, has launched the Social Business Initiative after recognition that the social economy can prove a valuable addition to eradicating inequalities, unemployment and other social unbalances. The Initiative consists of measures that aim at facilitating the creation of social enterprises and fostering their growth in Europe through suggestions for improved access to funding, more visibility and a better legal environment.

As any other enterprise, social companies are concerned with and thus put an uttermost importance on the access to financial and non-financial resources that would enable future development. Resource mix defines the flexibility of an enterprise and proper financial management is essential for sustainability of the social enterprise. Resource mobilization ranges from financial grants and subsidies provided mainly by government in support of the social enterprise mission, to income generating trading activities that facilitate self-sufficiency and independence from the public aid and extend further to include non-financial resources such as volunteering. Moreover, reforms in countries with established history of social enterprise regulatory stimuli, have facilitated obtaining of external finance from private banks or investment institutions, as opposed to non-repayable allowances from state bodies. Additionally, Scarlata et al. (2012) reveals the growing importance of the Philanthropic Venture Capital as alternative sources of external finance for enterprises that seek to maximize social impact. The paper elaborates on the ability of philanthropic venture capitalists to further social enterprises development through identification of and active engagement in community enterprises with high potential for social impact.

The academic literature has explored to a certain extent resource mix allocation. Nyssens (2006) provides across-country overview on the current resource utilization for number of European Work Integration Social Enterprises (WISE), The State of Social Enterprise survey published by the Social Enterprise Coalition in UK offers similar information on British social enterprises, whilst other publications concentrate on one country, Zhao and Gijselinckx (2011), for example, focus on China. The availability of the resource mixes in essence is indispensably related to the legal rules that apply in the country of origin for the social enterprise. The legal frameworks within which social enterprises operate are explored partially in the publications listed above, as well as in a report prepared in 2010 by the Center for the Study of Financial Innovation, which focuses on British social enterprises and a paper by Borzaga and Santuari (2000), related to Italian co-operatives.

An extensive analysis of the available resource mixes is not readily available. Various academic papers and reports focus on different aspects of the resource mobilization depending on the context within which social enterprises are examined and a coherent framework of resource mixes has not been established. Furthermore, the scientific publications tend to be more descriptive and only briefly mention on the interrelation between the legal environment and resource mix mobilization. The paper addresses this gap. It aims at combining the available knowledge and introducing a more explicit structure of social enterprise`s resource mixes within which such interactions and their effects can be analyzed. Thus, the research question formulated is:

What are the implications of legal framework on resource mix mobilization inside European social enterprises?

It aims at identifying the main channels through which the institutional environment affects resource mix utilization within social enterprises with a focus on UK and Italy. The legal implications refer to identifying the way in which institutional regulations affect the extent to which certain resources are used within an enterprise. The question will be approached and examined with the help of secondary data analysis, available reports and academic papers on the field of interest.

The structure of the paper is as follows. First, a literature review is provided, establishing formally the concept of social enterprise by identifying the crucial relation between business innovation, which is typical for entrepreneurial model, and the importance of the social mission. A definition and main functions of a social enterprise are presented based on various academic sources. Additionally, the resource mix available within social enterprises is considered, followed by overview of the legal structures and regulations utilized. The third part of the paper focuses on the methodology employed and a description on the data studied. The forth section considers the resource mix mobilization within social enterprises in UK and Italy and elaborates on the main consequences of the legal framework on the extent of specific resource utilization practices. It provides evidence on the interaction and builds on the analysis presented in the literature review and concept definition section. The paper concludes with a discussion.

II. Literature overview and concept definition

In order to evaluate the resource mix available to social enterprises a concept definition should be readily available so as to be able to distinguish between different types of enterprises. The academic literature provides extensive discussion on the main characteristics of social enterprises with emphasize given on the distinction between community enterprises and their commercial counterparts. Identification of the social enterprise and its core functions should commence with the examination of the key elements it is comprised of, i.e. the entrepreneurial and social part of the definition that outline the framework of analysis.

This part of the paper is designed as follows. First, the interaction between the above mentioned components is established so as to derive a full workable definition of social enterprises. Second, the various monetary and non-monetary activity-supporting sources available to the unconventional enterprises are examined and thus an overview of their resource-mix strategies is presented. In the last part, legal forms and other regulatory instruments are introduced.

Defining entrepreneurship

The entrepreneurial element in the definition is the main source of difference between organizations that rely excessively on charitable donations and public finance with relatively little importance placed on identification of new income generating activities, as opposed to the ones engaged in active resource management decisions. In the vast amount of literature available, there is a common agreement on the basic elements that define the concept of entrepreneurship. Shane and Venkataraman (2000) emphasize the identification of new markets and products that were not previously explored as a basic constituent. The discovery of unexploited economic opportunity is a core element and relates to the fact that entrepreneurs are in general more risk accepting. They become actively engaged and main contributors to the development of the organization, effectively combining resources and labor for the achievement of its goals. In fact, the different profiles and features of people with entrepreneurial capabilities lead to heterogeneity of their beliefs with regard to what a valuable combination of inputs consists of. This is the main explanatory factor for the existence of various entrepreneurial opportunities (Alvarez and Busenitz, 2001). Cuervo and Domingo Ribeiro (2007) try to reconcile the main elements existing in the theories on entrepreneurship. They define entrepreneurship as a concept that can be examined through four dimensions: entrepreneurial function, factor, initiative and entrepreneurial behavior. The entrepreneurial factor pertains to the existence of entrepreneurial capabilities that add to the value creation process though channels other than the classical that include combinations of labor, land and capital. The entrepreneurial function "refers to the discovery and exploitation of opportunities or to the creation of enterprise". As far as the entrepreneurial behavior, also known as "spirit", is concerned, the existence of a person who is active, open for new initiatives and risk taking, as discussed above, is emphasizes. The expectation of market imperfections and unexplored areas, combined with search for new ways of resource utilization defines the entrepreneurial initiative.

Entrepreneurial activity should be analyzed from a broader socio-economic perspective as it is directly shaped and influenced by the cultural, demographic and institutional environment in which it operates. Various environmental and economic factors that relate to the established market dynamics play a foremost role in the existence of entrepreneurs and define their contribution to the improvement of social wellbeing. The fundamental importance of entrepreneurship in economic progress is manifested through identification of unexplored opportunities by way of creating new firms or revising organization`s strategies and dynamics, thus leading to economic advancement through "innovation, competence, job creation" (Cuervo and Ribeiro, 2007).

Defining Social Enterprise

The second part of the discussion concentrates on analyzing the social dimension in the definition and elaborates on its interaction with the entrepreneurial concept. This section departs from the discussion on entrepreneurship as a general field of inquiry and focuses on firm level investigation that separates social from a commercial enterprise. Taken into account the relatively recent recognition of social entrepreneurship, vast amount of scientific literature created has aimed at properly defining its notion and main characteristics. This resulted in extensive conceptual based approach with regard to the field of social enterprises (Hoogendoorn, Pennings and Thurik, 2010).

Practically, a social venture can be evaluated on two levels, the pure functional form it takes, on one hand, defined by the organization`s core goals and tasks, and the psychological characteristics, on the other, that correspond to the distinctive human factor. The present paper does not strive to discuss in detail the differences between the social and commercial entrepreneurs. The main focus in determining the definition is placed on the distinction of social enterprises goals and methods of achieving them.

What social businesses consist of and their key determinants have been the center of attention as stated above. Despite the various definitions employed in the literature on the topic, most sources agree that the commitment to social mission and community value creation are prominent elements that characterize the social enterprise domain (Peredo and McLean, 2006). The social factor relates to the desire to find better ways to benefit society and increase welfare in the community it operates. The mission-related impact is the central motive for the existence of social enterprises as opposed to the pure wealth creation process the commercial firms are involved in. For social enterprises wealth is just a means for delivering the desired outcome (Dees, 1998). Some may find this distinction inappropriate as mainstream enterprises increase social wellbeing by delivering products and services that are valued by certain groups in the society. Nevertheless, the main discrepancy is related to the idea that for-profit social enterprises reinvest substantial part of the income generated in the further advancement of their core social mission or directly in the community without the requirement to maximize profits for their shareholders or business owners (Harding, 2006). An example of a social enterprise can facilitate understanding of the concept. Paredo and McLean (2006) provide a description of a for-profit social enterprise: Newmans Own, a United States –based company that invest 100% of its after tax revenue in education and support for charitable purposes.

The place of the social enterprise in the economy should be established in relation to the private for profit and the third sector. The EMES Network, one of the key social enterprise research institutions, has explored the concepts of social economy and its relation to the non-profit sector (NPOs). Two of the networks key contributors, Borzaga and Defourny (2001), have pointed out that both concepts can be analyzed within the third sector framework. They underline the importance of the non-distribution constraint with regard to NPOs surpluses, while some forms of social enterprises, such as co-operatives, sometimes do distribute profits among members. They also mention the fact that the established definition of NPOs does not prevent them from profit maximization as long as it is not distributed among shareholders and some production oriented entities within the non- profit sector can be closely related to social enterprises.

Nevertheless, Social enterprises should not be accepted instantaneously as referring exclusively to organizations that are involved in income generating strategies. Importance of the social goal is a key determinant but an appropriate line beyond which the degree of core mission devotion fails to qualify a given company as social is not well defined. Both enterprises which have only social goals and do not engage in trading activities, and those, for which social goals are subordinate to others, have found place in the literature as social enterprises (Peredo and McLean, 2006). This clearly shows that a constant, homogenous profile of the social enterprise is not yet established. On the contrary, the combination of innovation and search for more effective ways to deliver social value, characteristics compatible with social entrepreneurship, can occur within or across the nonprofit, government or business sectors (Austin and Wei-Skillern, 2006). The business model and particular community needs addressed are factors that contribute to the choice of for-profit or non-profit form of social enterprises. The difference resides in the relative significance of wealth versus social value creation. For social initiatives income surplus is by-product, which guarantees the sustainability of the core social mission (Mair and Marti 2004).However, social enterprises are additionally characterized by high degree of autonomy and more economic risk undertaking than other normal nonprofit institutions (Nyssens, 2006).

Social enterprises are considered multi-stakeholder organizations due to the ability to successfully integrate and represent the different needs of their employees, the owners and their respective customers simultaneously. They manage various types of stakeholder interrelations conditional on preserved community values and social mission completion. Social enterprises are complex entities that combine numerous goals that cannot be achieved without accurate communication among all the parties affected during the decision making process. *Table 1* below consists of a concise summary of the main characteristics to be found in the literature, in line with the EMES Network framework, which support this social enterprise characteristics presented so far.

The paper adopts the definition on social enterprise introduced by the Department of Trade and Industry, UK (2002):

"A social enterprise is a business with primarily social objectives whose surpluses are principally reinvested for that purpose in the business or in the community, rather than being driven by the need to maximize profit for shareholders and owners"

Thus a social enterprise is considered a firm that applies for profit business principles and innovative approach that will assist the delivery of its social mission (Pomerantz, 2003). Social enterprises can take numerous legal forms depending on what fits their organizational arrangements and the definition employed is not limited to any particular social enterprise legal structure.

Main characteristics of Social Enterprises	Source/Author
SE usually has complex mixture of goals:social goals, economic goals (related to the entrepreneurial nature of the enterprise) Socio-political goals (SE are usually rooted in a sector traditionally involved in socio-political action).	Evers, A. and Schulze-Boing, M., 2001
Multi-stakeholder ownership hypothesis	Bachiega and Borgaza 2001
Social enterprises combine different kinds of market and non-market resources: trading, volunteering and public financing	Nyssens, M. 2006
To reflect the economic dimension: 1. production/sale of goods/services as a main reason for existence; 2.high degree of autonomy- not managed by public authorities or private org 3.level of economic risk-financial viability depends directly on members efforts To reflect the social dimension: 1.an explicit aim to benefit the community 2.initiative launched by a group of citizens, that shares well-defined need 3.Decision making power not based on capital ownership 4.participatory nature involving the various parties affected by the activity 5. No or limited profit distribution- avoiding profit maximizing behavior	Borzaga and Defourny 2001:16-18
Trade for social enterprises is just a source of income and trading activity and does not in itself matter, however only SE are those which are engaged in trading activities that are directly related to their core missions	Nyssens,M. 2006
Social enterprises influence their institutional environment and have contributed to the development of institutions and public policies.	Nyssens,M. 2006

Table 1: Some important characteristics of Social Enterprises contributed by EMES Network members

Resource mixes inside Social Enterprises

The main objective of this section is to introduce the reader to the various resources mobilized by social enterprises in support of their core mission as depicted in the literature. The resources available are in close relation to the concomitant economic, social and institutional context as it defines the framework in which a social enterprise functions. The legal framework within which these companies operate has significant influence on the possibilities and the extent to which a certain resource type is preferred over another and thus the overall mix distribution. Nevertheless, a more elaborate discussion on the interdependence of legal structure and resource utilization is conducted subsequently.

Social enterprises are regarded "multiple resource" organizations that effectively combine trading and non-trading activities to ensure its long term performance and stability. They sell goods and services in the markets. Social enterprises can take advantage of public funding possibilities to support their public objectives, or can rely on volunteering (Nyssens, 2006). Overall, the variability of resource mixes available to this type of enterprises contributes to a certain extent to their flexibility when deciding upon the ways of supporting their mission. They can find the most effective way to mobilize resources in the social value creation process, depending on the specific socio-economic environment, especially when limited regulatory restrictions apply. Nyssens (2006) argues that social enterprise`s resource utilization is as a direct result of three types of economic dependencies: the market, redistribution and reciprocity. Social enterprises interaction with the market is related to the utilization of monetary resource, those that can be easily measured and quantified. The proceeds from sales, grants and subsidies, including government and non-government, as well as, gifts fall to this category. On the other hand, an emphasis is placed on the importance of non-monetary resources used. Despite the relative difficulty of their accurate evaluation their role should not be underestimated. The redistribution and reciprocity forces fall into this category. Indirect subsidies in the form of tax reductions and social contributions reductions for employees pertain to redistribution, whilst reciprocity is directly related to the availability of volunteer workers.

In the paper, the investigation of the resource mixes extends further to the separation of the various financial resource mixes available to social enterprises. The financial resources consist of:

- Internal resources
- External resources

The difference between internal and external resources lies in the fact that the former is entirely as a result of within-firm processes and the latter refers to those sources that are provided by agents outside the firm. The sources of internal funding include, as mentioned above, the economic surpluses generated though trading activities in the normal course of the enterprise operations, proceeds from sales of goods and services fall into this category. Additionally, the internal resources can be divided as sales of the social venture products to government or other public institutions, sales to private sector, i.e. other business entities or to households.

Depending on the provider of the funds, the external resources can be further split into:

- Grants
- Subsidies
- Donations
- Debt: such as bank loans
- Equity capital

The common factor that combines grants, subsidies and donations is the non-repayable clause. External funds in the form of government grants and subsidies, as well as individual member donations are main access to external resources for charitable and voluntary organization. Although, they do not have to be repaid, stricter conditions usually apply in order to ensure that the funds are used according to their initial purpose (Bank of England Report, 2003). Grant funding is typically short lived and applies to specific projects. It restricts the use of funds which may in turn lead to inflexibility in the range of actions available to a social enterprise. The debt and equity capital, such as bank loans and share issuing respectively, differ in the importance attached to ability of repayment by the social enterprise. They have the advantage of being longer term than grants and thus allow an enterprise to freely choose the business model it would like to develop.

A representative overview of the various resources available to social enterprises is exhibited in *Figure 1* at the end of the section.

The resources employed are implicitly embedded and conceptualized in relation to the economic reality and accordingly, would differ across countries with diverse social and institutional arrangement. However, even if resource mixes of social enterprises in one country are analyzed they would differ depending on the stage of development of the social enterprise itself. In case of start-ups, the main resources used are more likely to include readily available credit such as government grants and subsidies, various donations. They are more likely to rely extensively on volunteers and family/friends financial and non-financial support as well (State of the Social Enterprise Survey UK, 2011). With the increase of the age, social enterprises try to incorporate income generating strategies to ensure self-sufficiency of the organization which in turn reduces the need for non-refundable funds or volunteer resources mobilization. Established social enterprises seek other types of external financial resources in the form of bank loans, overdrafts or even equity finance, as pointed out in the survey of 2011. Social enterprises can benefit from equity finance for two main reasons: reduces debt obligation and induces early stage growth (Equity finance for Social Enterprises 2006 SEJ). The relative advantage of external finance through equity issue rather than debt is related to the fact that borrowing costs are usually higher and may be even higher for social enterprises due to the specific social impact nature of the business. Thus Social Enterprises may need to make higher profits to meet the costs of serving the debt. Equity finance can prove interesting due to the fact that many socially oriented investors are in search of social return and if they support the social objectives of the enterprise, interest rate-like returns are enough.

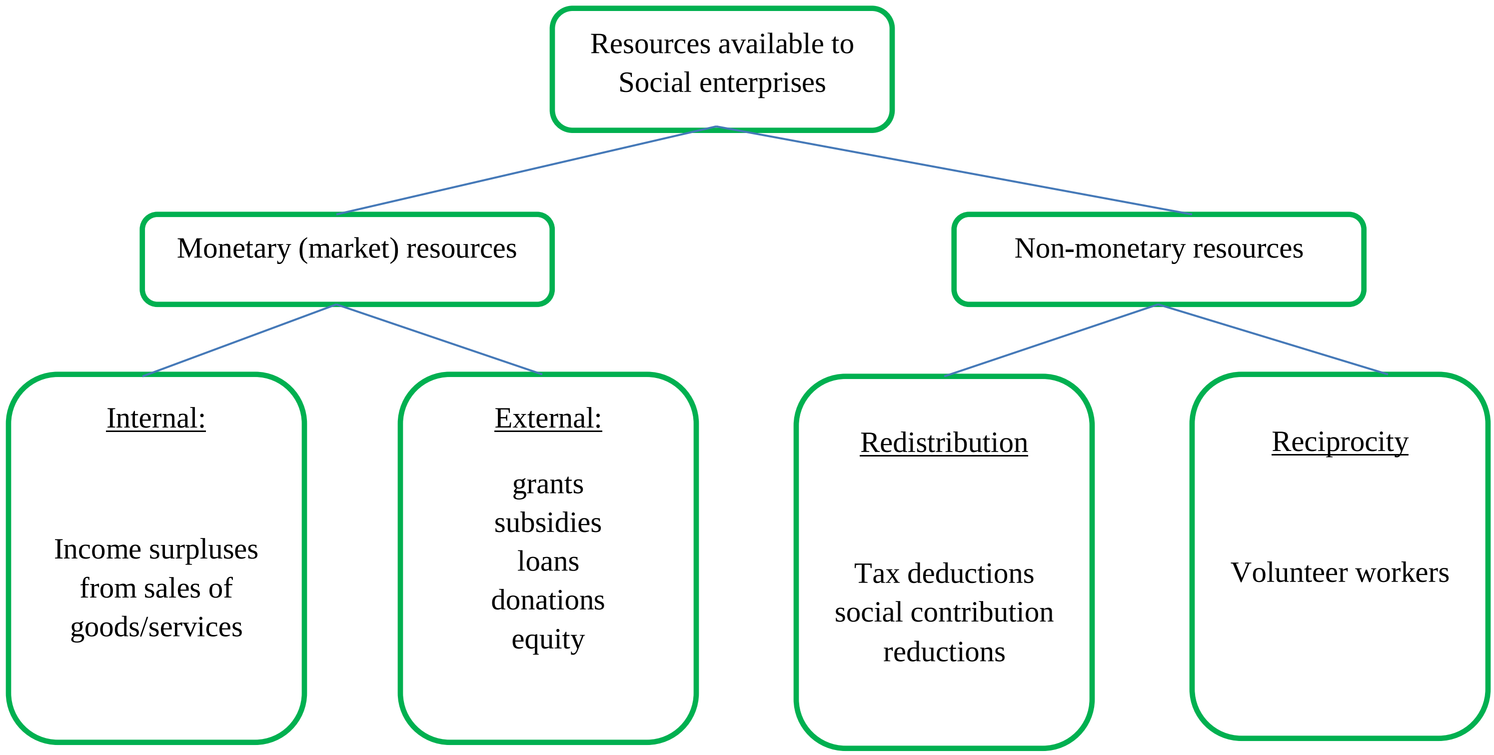

Figure 1: Diagram of the resources available to social enterprises as discussed in the paper

Legal structures for social enterprises

The objective of this part is to summarize and describe the legal environment in which UK and Italian social enterprises operate and thus examine any possible relationships with respect to the resource mixes mobilization.

The legal form adopted is decisive for resource mix allocations of social enterprises since it defines the institutional arrangements according to which they can obtain certain types of funding or take advantage of non-monetary sources. The resource framework discussed above will serve as a base to which possible interactions between resources mix utilization and legal rules will be presented. These fostered relationships are directly related to the state of government engagement in the development of social enterprises.

A strong state can promote social entrepreneurship through various initiatives. The UK government for instance is a vivid proponent of social enterprises and this is demonstrated by the fact that by 2005 it launched various projects, such as the Community Development Finance Institutions or the “Future Builders”, a program that enabled the community sector participation in public contracts bidding (Harding, 2006). Nevertheless, the government has achieved much more by nurturing appropriate legal environment. Harding (2006) also indicates that the UK government, for instance, has extended the Small firms Loan Guarantee to include social enterprises with explicit implications on external credit availability to social enterprises. It has introduced the Community Interest Company –a legal form specifically designed to represent the social enterprises and ensure that revenues from sales remained within the firm and cannot be distributed among shareholders.

The following section examines briefly the different government regulations. The appropriate legal forms are presented first and eventually other incentive altering rules are considered.

Not surprisingly, the legal forms that social enterprises take vary widely across countries. Even on country level comparison between different community enterprises, a clear pattern of what is predominantly chosen as a structure cannot be instantaneously established. Even individual social enterprises that operate in similar fields may have different goals and more importantly, different business models and ideas of how to pursue them more effectively. In principle, once a legal form is adopted, it does not mean that the enterprise should permanently adhere to it. Evidence to the contrary will be presented later in the paper. The most common legal structures include:

- Community Interest Company (CIC),
- Industrial and Provident Societies (IPS)
- Social Co-operatives

The first two are of particular importance in United Kingdom, while the Social Co-operative is the main established form in Italy (Nyssens, 2006). Their main characteristics are summarized in *Table 2* at the end of the section, however, the discussion now elaborates on the topic.

The report by Bridge et al. (2009) provides a detailed description on the CIC. The type of legal structure was accepted in UK in 2005 as a part of a government plan to provide better suited support for social enterprises. It is established as an alternative to the limited liability companies (LLC) and charities institutions. In comparison to LLC, it allows for lock on assets, which indicates that investors are prohibited from sharing any residual assets in excess of their shares in the company in case the enterprise is liquidated. It is designed to assure that the economic surpluses remain in the social enterprise itself without being distributed to shareholders. At the same time it has upper limit on the dividends payable to its owners and the voting rights are on one person-one vote basis and do not depend on the capital contributed initially by the owners. Community Interest Companies are liable to pay corporate tax and cannot take advantage of tax reliefs even on expenditures on community purposes. They do not have the tax advantages of charities, however, they can issue public shares and have access to external financial resources. In 2010 a legal regulation has increased the dividend cap of up to 20% on the value of share (Heaney and Hill, 2010).

The second type of social enterprise form that is considered is the IPS. In general, it has non redistributive clause for the members, although some of them do distribute income (Heaney and Hill, CSFI, 2010). IPSs have a maximum amount of shareholding per member allowed (around 20 000 pounds) and contributed funds by the shareholders can only be withdrawn under certain circumstances. Similarly to CIC, they are subject to corporate tax on profits earned and have the ability to issue shares with investors eligible to take advantage of equity based tax relief.

The social co-operatives are of particular importance in defining the legal regulations related to social enterprises in Italy. Borzaga and Defourny (2001) also enlist other legal forms available to social organizations in the country such as: charitable institutions, associations and voluntary societies, as well as the traditional co-operatives. Nevertheless, the social co-operative proves to be directly associated with the characteristic of a social enterprise. The Italian co-op role in the social service sector is legitimately established in 1991 (Borzaga and Santuari, 2000). Two categories of social co-ops emerged as a result of the Act:

- Co-ops that are active in the health, educational and social sectors (A-type co-ops)
- Co-ops that aim at labor market integration of disadvantaged people (B-type co-ops)

It is enacted that the voluntary participation cannot exceed 50% of the overall membership of the organization. They were granted tax benefits mainly in the form of VAT reductions on sales of goods and services. Moreover, a provision was established according to which up to 20% of the public demand for services can be directed to those social cooperatives under certain conditions (Borzaga and Satuari, 2000). The Act does not prohibit profit distribution, although some restrictions applied, as the overall amount could not exceed 80% of total earnings. The structure of the enterprise is based on one-person-one-vote democratic principle and is characterized by limited liability of the owners and no assets can be distributed in case the co-operation is liquidated.

While charities do not fit the working definition of a social enterprise in the paper, it is worth mentioning some of the main features of charitable incorporated organizations (CIO) since most of the UK social enterprises indeed choose to take on this legal structure in the start-up phase due to substantial institutional advantages (Bank of England Report, 2003). Although trading activities are only possible if directly associated with the charitable missions, CIOs benefit directly through considerable tax reliefs on income generated. Additionally, donors (private corporations or individuals) can benefit from tax reductions as well. The adoption of charitable status, however, entails restrictions on external finance availability in the form of equity issue. Possible implications for resource mix utilizations with respect to UK social enterprises are discussed in *Section 4.*

Legal structure	*Country*	*Ownership & Governance*	*Benefits to the owner/manager*	*Assets locked-in*	*Other important characteristics*
Community Interest Company (CIC)	*UK*	*Flexibility over internal rules but subject to regulations to ensure community benefit; Limited member liability*	*Available, but must benefit the wider community. Limited dividends can be paid*	*Yes.*	
Industrial and Provident Society (IPS)	*UK*	*One member one vote principle, regardless of size of shareholdings; Limited member liability*	*Available to some, but usually not as a result of shareholding, but usage of facilities etc.*	*Yes*	*Max amount of shareholding is limited; Equity based tax relief for investors*
Social Co-op	*Italy*	*One member one vote principle; Limited member liability*	*Profit distribution possible, though must not >80% of earnings*	*Yes*	*Voluntary participation≤ 50%; VAT reductions on sales of goods/services*

Table 2: Main features of legal forms discussed in the paper

III. Methodology of the analysis

The method used to explore the research question about *the implications of legal framework on resource mix mobilization inside European social enterprises*, relies exclusively on the usage of secondary data sources. The relatively recent growth of the interest in social entrepreneurship is able to explain the fact that most of the academic literature available concentrates on conceptualizing and theorizing rather than hypothesis testing (Hoogendoorn, Pennings and Thurik, 2010) and not much empirical research has found its place among the scientific inquiries. The main sources used in the current work are existing academic papers published in Europe, as well as reports conducted by non-profit organizations mainly with the support of government institutions. Data was gathered separately on the resources available within European social enterprises and the most commonly utilized legal structures. Eventually numerous academic papers were examined to develop a more precise framework of the resources employed within British and Italian social enterprises in order to establish an interaction with the legal environment.

Most of the used reports are based on individual case studies and/or interviews and are country-specific. They fail to provide detailed information on the resource mixes used by social enterprises conditional on the respective legal forms adopted thus rendering the analysis more descriptive and analytical and less empirically reliable. The fact that the data analyzed in the literature used is not made public and the lack of common international datasets of social enterprises prohibits the use of statistical methods for more reliable cross-cultural estimates of the various effects of legal environment on resource mix mobilization.

The next section proceeds with analysis organized as follows: first, general remarks based on the economic theory and enterprise behavior within certain legal context are proposed. It is followed by projections on the resource mixes utilization that is expected to prevail in England and Italy in relation to the legal forms presented in *Section 2.* Finally, examination of number of scientific papers and reports on the respective European countries are presented to establish the relationship between the legal environments and resource mobilization and provide a comparison to any predictions made.

IV. Establishing the interactions between resource mix and legal environment: evidence based approach

The establishment of the resource mix and legal structures available to social enterprises in England and Italy provides the opportunity to a more detailed discussion on the interaction between the two components.

General remarks and implications of legal framework on resource mix

In order to promote the expansion of the social enterprise sector, the government can introduce fiscal policies such as tax reductions or subsidies availability to some enterprises in combination with the appropriate legal form. This type of institutional regulations has an effect on the incentives which enterprises or parties in a direct relationship with the company face.

Tax reductions can influence the amount of trading activities undertaken by enterprises. In case the direct customers of the social venture products and services are exempt from payment of VAT then, everything else equal, it is more likely that the demand for the production of the social enterprise will increase and thus the proceeds from sales. This implies a direct effect on the internal resources available to the company and can lead to growth and expansion in case the retained earnings are reinvested for further support of the social mission instead of being divided among shareholders, which is the case for social enterprises.

Additionally, tax deductions have an effect on external monetary resources mobilization. Most of the contemporary tax schemes related to equity investment in UK are directed at incentivizing short and medium term equity investments, for example, through tax relief programs (Heaney and Hill, CSFI 2010). The launch of Community Investment Tax credit (CITC) aims to encourage investment in both profit seeking and not for profit enterprises in disadvantaged areas, including social enterprises. It is available to individuals and companies that invest in accredited intermediary organizations which in turn provide funds and loans to enterprises that operate within disadvantaged communities. This encourages the growth of the Community Development Financial Institutions which specialize in investing in social and community enterprises. The tax incentive is a form of tax relief which reduces the investors` income tax or corporations tax liability.

It can be concluded that tax reduction policies positively affect non-monetary redistribution resources described in the *Literature overview* section and also can have an indirect positive effect on the financial resources, both internal, through sales increase, and external when tax relief is introduced to investors or intermediaries that allocate grants and loans among social enterprises.

Government grants are part of the financial resources and thus have a direct effect on their respective share in external resource mobilization. The more grants are available to a social enterprise, the more likely it is to take advantage of this cost free capital. At the same time, grants may have indirect effect on other types of external financial resource utilization. A grant dependency may lead to weak financial discipline (Bank of England Report, 2003) and decrease willingness of the social enterprise to generate surpluses through higher trading activities or achieve higher efficiency in its operations to reduce costs.

Other types of policy regulations may aim at influencing the level of human resource utilization. An example can examine the reduction in social contributions required for employees coupled with restrictions on amount of volunteers, as it is the case for Italian social co-ops. This type of legal rules may lead to permanent change in the human resource mobilization within certain types of social enterprises.

Certain legal regulations have direct effect on the external equity finance available to social enterprises as well. The incentives to invest and purchase shares of a social enterprise are directly related to expected return that an investor wishes to realize. The expected return is dependent on the risks associated with the business that the provider of funds faces. Social enterprise sector is not readily understandable by investors due to the nature of the business and lack of available information (Bank of England Report, 2003) and the outcomes are social rather than strictly financial which makes difficult the accurate assessment of the company and its value. In addition, the non-distribution constraint and the lock on assets that are typical for some social enterprises with certain legal forms provide further risk for investors` inability to realize expected returns. This contributes to higher costs of investments and more uncertainty with regard to performance results and thus negatively affects the willingness to invest in social businesses. This feature is not only common among individual investors but may be relevant even when a social enterprise applies for a bank loan. Legal and institutional framework, however, may provide some solutions that would decrease the uncertainty and costs associated with investment in community businesses. Besides the investment tax relief program discussed above, an increase in the UK max dividend rate paid on social investments may prove to be an interesting way to attract equity finance to social enterprises in the country.

The observations that certain legal regulations may influence the relative resource mix facilitate the ability to make certain predictions with respect to resource mixes expected to prevail within social enterprises in Italy and UK. The following part discusses the predicted implications of the legal structure on the extent to which certain resources are utilized.

Expectations on Italian co-ops resource mix

After the legal amendments in the Italian system from 1991 which led to the establishment of the social co-operative as a major form of social enterprise, certain changes in the resource mix mobilization can be expected. Due to the constraints on volunteering that should not exceed half of available personal the relative importance of unpaid labor is likely to diminish. A change in the relative human resource mix is expected to favor an increase in the paid working staff relative to volunteering members thus decreasing the share of reciprocity based non-monetary resources. This is further stimulated by the introduction of lower amount of social contributions that are to be paid per employee of a social enterprise. Additionally the provision of VAT reductions to sales of goods and services is likely to rise the trading conducted by the social co-operatives and thus lead to a higher share of internal financial resources relative to external. The provision in law that up to 20% of the state demand for goods can be directed at those social enterprises may contribute to an increase of the public funds available to social co-ops and thus render the sector more dependent on the government as a main purchaser of services and main trading partner relative to the private sector and households.

Expectations on UK resource mix

Compared to other European countries, UK government has substantial contribution to stimulating the growth of the social enterprise sector through increase access to external capital markets. The legal environment has provided not only appropriate legal structures, such as the CIC, but introduced various incentives based regulations that facilitate the flow of financial resources to the social enterprise sector. The launching of Small firms Loan Guarantee to include social enterprises is likely to lead to increase in the loans issued to the sector and thus to changes in the relative importance of repayable external finance. Additionally, the increase in the share cap rate of up to 20% as discussed is expected to have direct implications on equity investors` willingness to buy shares of social enterprises. The combination of increased return on equity and the advantages of Investment tax reliefs for those who invest in Intermediary Institutions which support social enterprises will probably contribute to an upsurge in equity investment. Investment in social enterprise is likely to become more attractive and may be expected that this type of external finance will eventually become common within the British social enterprise sector.

Evidence from Italy

This part examines the available evidence in the literature with respect to Italian social co-ops and resource mixes utilization and origin. The main focus is on the analysis and reports by Defourny(2001), Borzaga (2002) and Loss (2003) and as main contributors to the field of research in Italy.

Borzaga and Defourny (2001) and Loaa (2002) state that 70% of the co-ops in Italy are type A and 30% are type B or WISEs - Work Integration Social Enterprises. The latter are engaged in activities that facilitate the work integration in the local labor market of socially disadvantaged people. In addition, Borzaga and Loss (2002) indicate that WISEs were primarily dependent on public sources to support their activities as the projections would suggest. Nevertheless, a significant change in the origin of the resources in those co-operatives is present. There have been alterations in the dynamics within those social co-ops resource utilization with more focus placed on increased trading with the private market, especially relevant for co-ops providing services. Nowadays, the resources mobilized may vary in origin and come from public and private market transactions alike with relatively less dependence on grants and subsidies.

In fact, the Italian experience shows that since 1994, most of the revenue was derived from increasing trading activities, with respective contribution from the sale of goods and services of around 86.7%, public and private grants were not substantial, comprising 13.3% of the total amount. As the hypothesis stated earlier would suggest, co-operatives` goods and services were mainly purchased by public authorities (57.7%). Nevertheless, 29.0% of the trades were conducted with private users as well. This signifies that social enterprises are increasingly gaining more autonomy from the public authorities (Borzaga and Defourny, 2001)

There has been a change in the membership structure, positively affected by the legal regulations from 1991 as the previous section supposed. It can be deduced that a general tendency towards volunteer reduction is present and the growth of members is entirely due to employment of paid labor. Contrary to the survey of years before the act was enacted, the membership of social enterprises today consist mainly of paid workers. In 1996, more than half of the co-ops examined did not have volunteer members (CGM 1997). Where those were present they rarely numbered more than 10. From 1993 to 1996 in the co-ops examined, the number of volunteers halved within this three year period and the rise in the members was entirely due to the increase in the paid labor. This can be due to the increase in the demand for services by social co-operatives from the public authorities. This induced a fast creation of new co-ops which had to rely more on paid jobs than volunteers, because the mobilization of volunteers is usually as a result of long term investments in social capital and cannot be achieved within a short period of time. According to audit proceedings collected by Italian Ministry of Labor on 1134 co-ops in 1994, 91% were worker members and 8.4 were volunteer members. According to another source (CGM, 1997) on a smaller but more homogenous group of 260 social co-ops, the number of volunteers in 1990 was 14.1% while in 1995 it had decreased to 12.3%. Therefore a general tendency for reduction in volunteer utilization is depicted.

According to other sources, the estimated number of paid workers was 8.3 times higher than the volunteers and in 1996 more than half of the social co-operatives examined did not have volunteer members (Borzaga and Santuari, 2000). Drawing on different statistical resources, a total number of at least 100 000 members, of which 9000 are volunteers and 75 000 are paid workers can be estimated. Type A have about 75 000 members of whom 6000 are volunteers and 60 000 are paid workers. The others are referred to as supporting members. About 90% of the social co-ops have fewer than 100 members and 70% of them fewer than 50. There are only a few large co-ops with some hundreds of workers.

Borzaga and Defourny (2001) provide an overview of the financial resources mobilization and composition as well. In 1994 the average income per co-op was approximately 464,811 euro, of which major part (97%) was derived from trading activities, i.e. the supply of goods and services to public authorities or private individuals and just 3% from public funds and grants. This signifies that the role of the internal financial resource mobilization has increased as expected. The major clients of A type co-ops were public authorities (77%), followed by private individuals (4.7%), other non-profit organizations (5.9%) and private for profit companies (3.1%). It is indicated that the majority of social co-operatives income is still somehow connected to the public authorities, 61.2% is obtained through purchase of services.

In general, a trend towards more self- sustainable practices has emerged thus increasing the role of internal financial resource mobilization via more trading activities. Although the main trading partner has remained the public sector, there are relatively more transactions held with private parties, which signifies the diminishing dependence on public spending. As far as the role of the non- financial resources is concerned, volunteering has been replaced by a rapid employment of paid labor. To a certain extend it can be explained with the enacted law, which restricts the amount of volunteers allowed, nevertheless, the role of more prominent socio-economic factors should be taken into account. The rapid increase in paid labor relative to volunteers is more likely due to the rise in the social enterprise sector in general with limited number of volunteers available per co-operative.

Evidence from UK

The resource mix analysis on UK is mainly based on reports by Harding and the Bank of England, which, derived from case studies on social enterprises, summarize the situation with respect to various types of resources utilized within the sector. Both sources definition of social enterprise is consistent with the one employed by DTI and thus also with that adopted in the paper, so further distinctions are unnecessary.

As opposed to Italian social co-ops, the main concern for British social enterprises in their struggle for further growth and development is access to external sources and especially external capital in the form of loans and credits (DTI, Strategy for success, 2002). The report by the DTI mentions the fact that a lot of social enterprises are undercapitalized and cannot obtain commercial capital especially in their early stage when they try to diminish the role of grants and public support.

The resource mixes within UK social enterprises are reported to vary mainly in relation to the stage of enterprise` development. Most publications show comparisons in resource utilization between well-established social enterprises and "baby" ones. This, combined with information on legal forms adopted provides useful insights into the interrelation between legal framework and resource utilization. The Social Enterprise Monitor (2006) reports that 34.8% of the newly initiated social enterprises take the form of charities, while more established ones are more likely to take the forms of CIC and IPS. The choice of legal form for young enterprises may be related to the fact that external finance is usually very difficult to access due to risks embedded in new ventures on one hand, and the very nature of the social business on the other. Additionally, social enterprises are more likely to be established in disadvantaged communities and thus have the government as the main trading partner. In fact, 51.6% of the "baby" social enterprises are exhibited to gain more than 50% of their revenue from public source, compared to 37.5% of the established social enterprises. This is evidence that the longer the enterprise has been in operation, the more likely it is that it will be self-sufficient and independent of public sources. The report states that the pattern of external funding for social start-ups is similar to the one observed by their mainstream counterparts. More than 11.0% of baby social enterprises tried to obtain bank loans compared to 14% of the established well developed social enterprises. However, 10.3% of the start-ups failed in their attempts to access bank loan, although only 5.0% of the established had the same problem. The nature of the business is the most cited reason for failure to obtain external finance for 42.4% of the baby enterprises. Usually, the government is the main sources of finance for start-ups with 51.6% of the baby businesses having more than 50% of their revenue from public sources compared to 37.5 of the established ones. Trading activity is the main source of income for some 46.4% of the UK social enterprises in the survey with more than 50% of their revenue obtained through sales.

The findings reported by Harding (2007) are similar, with 55.0% of the start-ups expected to have charitable status at initiation. The author points out that approximately 58.0% of the UK social enterprises receive greater than 50.0% of their funding from public sources, of which 34.0% are start-ups. Additionally, it states that 20.2% of the revenue for social start-ups is dependent on government grants, compared to 14.9% for the established social business. This indicates that the importance of external non-repayable resources diminishes and thus the established social enterprises become more independent. In fact, 43% of these social owner-managed entities have mainly commercial revenue stream. From the social enterprises envisaged in the report, 52% are expected to generate revenue primary through sales, for 26.0% of which internal resources, i.e. trading, contributes more than 90.0% to revenue. As expected, the legal structures adopted by social enterprises in UK enable some of them to take advantage of shares issuing. The report elaborates on the increased importance of investments by unrelated to the company investors and further states that equity finance is has been used by 5.9% of the start-ups and 6.4% of the owner managers.

The State of Social Enterprise Survey (2011) provides similar results indicating that quite a few of the social enterprises in UK are trying to increase the provision of goods and services to private companies and consumers, thus decreasing the trading activities with the public authorities. Although half of all social enterprises in the survey trade with the public sector, for just 18% of them it is the main trading partner, while 37% of the social enterprises indicate that mainly private consumers purchase their products. Social enterprises surveyed rely mainly on internal resource mobilization with 76.0% of their income coming from trading activities, although new firms are observed to seek readily available credit in the form of grants. Additionally, the report states that social enterprises have three sources of trading income on average based on the trading partners. As stated, majority of social enterprises (37%) trade with the general public, although for 18% of them, main trading partner is still the public sector and for 13% main source of trading income is the private sector. As little as 9% of the social enterprises rely extensively on government grants. As far as the external resources utilized are concerned, the report confirms the hypothesis that UK social enterprises will be more likely to explore external finance opportunities. In fact, at least 47% of the social enterprises surveyed have sought external finance from different sources. The likelihood of en enterprise to apply for a bank loan increases with turnover, with 52% of those with turnover of 250 000 pounds or more seeking external finance. In comparison to the Social Enterprises Survey of 2009, approximately

4% of the social enterprises sought finance through equity issuing which is in accordance with the predictions made earlier.

In general, the social enterprise sector in UK is undergoing rapid development (Harding, 2007). The legal framework within which it operates significantly contributes to and facilitates the resource utilization practices available mainly through the recognition of the social enterprise as an income generating entity. The importance of the legal environment lies in the willingness of the UK government to make this social structure more explicit with certain laws and regulations that define the scope of its operations. The allowance for income generation within CIC and IPS legal forms contribute directly to the increased trading activity. This influences the resource mix utilization in two ways. On one hand, the relative importance of internal financial resources increases and thus a higher share of the resources mobilized are concentrated there. On the other hand, the increase in the trading activity has consistent consequences for the willingness of banks and other intermediaries to issue loans to social businesses. As a result the ability of the enterprise to seek external financial resources is directly affected. Additionally, the legal regulation that allows for share issuing and provides tax reductions for investors in the sector has implications for the increased number of social enterprises that take advantage of this external finance.

V. Conclusion and final remarks

Social enterprise sector provides significant opportunities through employment, support and training to the most excluded and disadvantaged groups in their communities. Local people become actively involved in designing and implementing solutions to fit their own, community needs. Social businesses are increasingly growing and even outstrip their commercial counterparts in confidence and innovation indicators (State of Social Enterprise Survey, 2011). Nevertheless social enterprises are not yet properly understood outside the networks of those within the sector. Many of them have difficulties in accessing appropriate finance, due to lack of track records, difficulties in assessing their risk profile, no assets to be used as collateral and many are unaware of their funding options.

The main contribution of the paper lies in the explicit identification of the various monetary and non-monetary resources available to community businesses as presented in the academic literature. Furthermore, the paper enlists the most common legal structures employed by Italian and British social enterprises and specifies a framework within which interactions between resource utilization and legal environments should be analyzed.

From the analysis conducted it can be concluded that the legal framework has implications for the resource mixes mobilized. It defines to a certain extent the relative importance that both monetary and non-monetary resources play. Tax reduction policies positively affect non-monetary redistribution resources and also can have an indirect positive effect on the financial resources, both internal, through sales increase, and external when tax relief is introduced to investors or intermediaries that allocate grants and loans among social enterprises. Government grants have a direct effect on their respective share in external non-repayable resource mobilization. The legal structure of the Italian social co-operative and the accompanying regulations have been able to explain the decrease in the usage of volunteers and the fact that the main trading partner remained the public sector. This resulted in less reciprocity based non-monetary resources utilized and a higher share of internal monetary resources contributed mainly from sales to government institutions. In general, however, a tendency can be noticed in both British and Italian social enterprises towards more self- sustainable practices through trade with private parties and thus independence from government funding. The allowance for income generation within CIC and IPS legal forms contribute directly to the increased trading activity. The relative importance of internal financial resources increases and a higher share of the resources mobilized become concentrated there. The increase in the trading activity of UK social enterprises has also consequences for the willingness of banks and other intermediaries to issue loans to social businesses. This results in more UK social businesses seeking external finance to support their operations. Additionally, CIC and IPS legal structures enable shares issuing and as a result equity finance becomes more accepted gradually and UK social enterprises are more likely to explore these financial opportunities. Nevertheless, it should be noted that many social enterprises point out that the legal structure they employ is just a vehicle and not a defining feature for their operations (Bank of England, 2003).

The limited access to common social enterprises datasets proves a significant barrier to a more elaborate estimation of the interaction between the aforementioned components. The research paper is strictly descriptive and does not rely on statistical estimates and thus its limited applicability. Another limitation is the lack of generosity in interpreting the conclusions since the paper is restricted to Italy and UK only and generalized conclusions cannot be reached for other European countries. Furthermore, the paper focuses on just a few legal structures within UK and Italy due to restricted amount of information and thus deep country specific analysis cannot be conducted.

Future research in this domain should focus on addressing those gaps. Gathering more information on social enterprise legal structures and respective resource mixes utilization can prove useful for identification of a more precise relationship between the two. A time-series analysis that follows the change in the most adopted legal structures and the resources mobilized can lead to good insights in this direction as well. Moreover, a comparison of legal structures and resource mix utilizations in developed and developing countries may prove interesting and contribute to expansion of knowledge with regard to possible interactions.

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