

A Guide to Legal Forms for Social Enterprises in South Africa

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**BERTHA CENTRE FOR
SOCIAL INNOVATION &
ENTREPRENEURSHIP**



A good legal form for a social enterprise is generally one that allows it to combine multiple sources of capital, private and public, philanthropic and commercial, in order to advance and scale the impact of the enterprise. While South Africa does not have a dedicated legal structure for social enterprises, the current structures allow for significant flexibility.

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Please note that this is a living document. We invite you to comment and provide feedback. Please contact Tine Fisker via email at tine.fisker@gsb.uct.ac.za or landline +27 21 406 1258.

The guide is meant as food for thought, not as a replacement for professional legal advice.

Cover image: Pathways to Funding Do-ference 2015

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Introduction: Choosing a Legal Form

Social enterprises exist to address a social or environmental problem. By pursuing a social/environmental purpose while using revenue, even profits, as a key driver of their business model, they represent a convergence between traditional businesses and non-profit organisations.

Social enterprises exist to address a social or environmental problem. By pursuing a social/environmental purpose while using revenue, even profits, as a key driver of their business model, they represent a convergence between traditional businesses and non-profit organisations. In South Africa, these trailblazing enterprises make it their mission to create employment opportunities, uplifting products, or a greener tomorrow. They are the likes of The Clothing Bank that helps unemployed women establish micro-enterprises, and Silulo Ulutho Technologies that is bringing ICT skills to South Africa's townships.

While social enterprises are developing new, inclusive ways of doing business, social investors are working alongside them to create flexible financing solutions to help them grow. This guide aims to help social entrepreneurs match their legal structure with their business model and the available funding streams.

A good legal form for a social enterprise is generally one that allows it to combine multiple sources of capital, private and public,

philanthropic and commercial, in order to advance and scale the impact of the enterprise. While South Africa does not have a dedicated legal structure for social enterprises, the current structures allow for significant flexibility. Understanding those are the building blocks of this guide. The individual strategic choices are the mortar that holds these together.

According to Social Enterprise UK, a social enterprise meets the following criteria:

- Have a clear social and/or environmental mission set out in their governing documents
- Generate the majority of their income through trade
- Reinvest the majority of their profits
- Be autonomous of state
- Be majority controlled in the interests of the social (or environmental) mission
- Be accountable and transparent



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Key considerations

While some social enterprises rely on both donations and income for their revenue, others may generate all their income through the sale of goods and services.

Other factors that influence the choice of legal structure include the size of the enterprise (staff size, turnover), the requirements of investors/donors, customers (from trade activity) and beneficiaries (the persons for whose benefit the social enterprise operates).

As will become evident from the six steps of the guide, and the table below, social enterprises with a **for-profit legal form** have significant flexibility in terms of sources of finance and

private ownership, but might find the brand value of a for-profit entity stifling. Additionally, they will not have easy access to charitable donations and grants. Social enterprises with a **non-profit legal form** can, however, engage fully in business activities while leveraging grant funding, but these choices may have consequences for taxation, which will be discussed further in this guide. Non-profit legal forms are also more restricted by ownership and governance regulations. Another main difference between for-profit and non-profit legal forms in South Africa is the distribution of revenue/profit. For a social enterprise, revenue/profit goes back into the business.

		FOR-PROFIT LEGAL FORMS				NON-PROFIT LEGAL FORMS		
		Sole proprietorships & partnerships	Private company	Trusts	Cooperatives	Non-profit companies	Voluntary associations	Non-profit trusts
BUSINESS MODEL								
Revenue models (not limited to the examples listed here)	*Donations	✓	✓	✓	✓	✓	✓	✓
	Fee for service	✓	✓	✓	✓	✓	✓	✓
	Trading activities	✓	✓	✓	✓	✓	✓	✓
FINANCING								
External finance	Donations	✓	✓	✓	✓	✓	✓	✓
	Loans (secured & unsecured)	✓	✓	✓	✓	✓	✓	✓
	Equity		✓					
	**Revenue-participation	✓	✓	✓	✓	✓	✓	✓
***GOVERNANCE								
	Broad-based				✓		✓	
	Individual	✓	✓	✓				✓
	Small group	✓	✓	✓		✓		✓

- * All legal forms can receive donations, but these are more likely to occur when the receiving part is registered as a non-profit with Donor Deductible Status (DDS).
- ** Revenue-participation agreements are, generally, available to all legal forms. However, it should be verified on a case-by-case basis that the agreement is in line with potential accreditations and relevant legislation.
- *** These should be read as generic guidance, as governance can be amended on case-by-case basis within each legal form. For instance, a cooperative can appoint a managing director, and a private company can appoint a more broad-based management group.

STEP 1: Understanding South African Legal Forms for Social Enterprises

Step 1 provides an overview of the relevant legal forms for social enterprises in South Africa.¹

For-profit legal forms	Non-profit legal forms
Sole Proprietorship / Partnership	Voluntary Association²
Private Company	Non-Profit Company as defined in section 1 of Companies Act
Business Trust	Non-Profit or Charitable Trust
Co-operatives*	

*Co-operatives operate for the benefit of members, which means they are seen as for-profit. However, their objectives and membership can be structured to achieve 'non-profit' goals.



ALANA BOND FROM SIMANYE PRESENTING ON ENTERPRISE DEVELOPMENT FUNDING AT PATHWAYS TO FUNDING 2015.

¹The non-profit company has replaced the section 21 company, which was the non-profit company form under the old Companies Act. All section 21 companies have transitioned to non-profit companies. The close corporation is being phased out, but old close corporations continue to exist. Personal liability and public companies have been omitted as they are not appropriate for social enterprises. Although trusts and partnerships are not generally recognised as legal entities, or legal persons, we have referred to them as 'legal entities' in this guide for convenience.

²For tax purposes, these are described as "association of persons"

	PRIVATE COMPANIES	NON-PROFIT COMPANIES	CO-OPERATIVES
Formation formalities	Filing notice of incorporation at CIPC	Filing notice of incorporation at CIPC	Filing application at CIPC
Constitutive Document	Memorandum of Incorporation	Memorandum of Incorporation	Constitution
	Shareholders' Agreement (optional)	Members Agreement (optional)	Members Agreement (optional)
Key Participants	Shareholders	Members (optional)	Members
	Directors	Directors	Directors
Minimum formation requirements	1 director and 1 shareholder (can be the same person)	3 directors (no requirement to have a member)	5 natural members (primary co-operative)
Principal Source of Law	Companies Act	Companies Act	Co-Operatives Act
Governance	Shareholder meetings Board Meetings	Members Meetings	Member Meetings
Proprietary interest	Securities (shares)	None	Shares or Patronage participation
Participation distribution method	Dividends	None	Surplus Distribution
Capital Raising Method	- Securities (shares, debt instrument)	- Membership fees - Donations	- Share Subscription - Member contribution
Governance Level	High	High	Medium
Governance Requirements	<ul style="list-style-type: none"> • Where of a certain size - audited financial statements (depending on size) - annual general meetings (depending on size) - social and ethics committee (depending on size) - company secretary (optional) 	<ul style="list-style-type: none"> • Annual members meeting • Audited financial statements (if assets exceed R5 million) • Independent review of financial statements (if not audited) - social and ethics committee (depending on size) - company secretary (optional) 	<ul style="list-style-type: none"> • Annual member meetings • Audited / Reviewed / Unreviewed financial statements • Auditor appointment (if audited financials required) • Activity plan
Formalities	Annual filing with the CIPC Maintain registered address	Annual filing with the CIPC Maintain registered address	Annual submission to CIPC Maintain registered address
Management	Board of directors	Board of directors	Board of directors
Existence	Perpetual Succession	Perpetual Succession	Perpetual Succession
Winding Up	Distribution to members	No distribution - assets transferred to similar organisation	Variable but distribution to members default

PARTNERSHIPS	VOLUNTARY ASSOCIATION - INCORPORATED	TRUSTS
No formal requirement	No formal requirement	Registration at Masters office
Partnership Agreement	Constitution	Trust Deed
Partners (and possibly general partner)	Members	Founder
		Trustees
2 partners	3 members	1 settlor, 1 trustee and 1 beneficiary (cannot be the same person)
Common Law	Common Law	Trust Property Control Act
No requirement	No requirement	No requirement
Partnership Interest (not unitised)	Members Interest	None
Profit Distribution	None	Capital or income distribution
- Capital Contribution (committed capital)	- Membership Fees - Member contribution	- Initial donation (Settlor)
Low	Low	Low
None	None	None
None	None	None On request by the Master of the High Court Trustees maintain address
No requirement	Member management	Trustees
No perpetual succession	Perpetual Succession	Perpetual
Distribution to partners	Distribution to members	Distribution to beneficiaries

Relevant For-Profit Legal Forms for Social Enterprises

Potential advantages and disadvantages when adopting a for-profit legal form for a social enterprise:

Potential advantages	Potential disadvantages
Can potentially access capital via traditional markets such as debt and equity	Limited access to tax benefits (compared to non-profit entities with PBO accreditation)
Can rely on internal funding from profit-making activities to finance business operation and expansion	Does not have easy access to donations/grants or state subsidies
Can access Enterprise and Supplier Development (ESD) funding via B-BBEE (Broad-Based Black Economic Empowerment), provided the social enterprise is majority black owned	May need additional branding/certifications to be perceived as a social enterprise

Sole Proprietorships and Partnerships

The sole proprietorship and partnership are not generally considered appealing for social enterprises due to the disadvantages listed below. In a sole proprietorship, a single trader owns all the assets of the business and is personally liable for all the debts and liabilities of the business. Although simple and inexpensive to setup with limited registration and auditing requirements, the fact that the sole proprietor is personally liable for the liabilities of the business is, generally, enough to dissuade entrepreneurs from using this structure. Other disadvantages include the fact that sole proprietorships are taxed at higher rates than companies, and that there is no legal continuity if the sole proprietor dies or is incapacitated.

Advantages	Disadvantages
No registration and auditing requirements	Higher taxation rates
Easy and inexpensive to set up	No legal continuity
	No limited liability

Ordinary **partnerships** are arrangements, usually documented in formal partnership agreements, where investors make capital contributions in order to acquire and co-own assets forming part of a business. Partners are jointly and individually liable for the debts and liabilities of the partnership. Any profits of the partnership are shared in a ratio specified in the partnership agreement. It often compares a partner's capital contributions to the combined contributions of all the partners. Partnerships are unappealing for similar reasons to sole proprietorships. Partnerships do not generally have separate legal personality. There are a few minor exceptions, namely that a partnership can

bring litigation in its own name under insolvency rules. Also, partnerships can be wound-up and if there are sufficient assets, then compensation will not necessarily follow to the individual partners. Like sole proprietorships, partnerships do not enjoy **perpetual succession**; if there is any change in the membership of a partnership, whether due to partners exiting or joining, this results in the automatic dissolution or formation of a new partnership. Partnerships must have **profit making as an objective**, which makes them unsuitable for pure non-profit activities. Unlike trusts, they cannot ever be formed purely for a charitable or social purpose.

The Private Company

A private company³ exists for the purpose of making profits for its shareholders. It may be incorporated by one or more persons and there is no restriction on the maximum number of shareholders who may participate in the company.

Advantages	Disadvantages
Limited liability protection	Complicated set-up procedures
Tax advantages ⁴	Maximising shareholder value might compromise the pursuit of a social/environmental mission
One of the most suited legal structures for raising capital such as debt and equity	
Flexible in terms of pursuing a social/environmental mission	

One of the key attractions regarding private companies is the fact that they offer investors limited liability protection. Shareholders are not liable for the debts and liabilities of the company. Directors are also protected from liability unless they breach their duties as directors. The company is a separate legal person to both its shareholders and its directors, which means that the company owns the business and the assets, which are registered in the name of the company rather than in the names of its shareholders or directors. The company can sue and be sued in its own name and has **perpetual succession** or **legal continuity**. If its shareholders or directors are replaced, the company can continue indefinitely. Private companies may therefore be hundreds of years old. Shareholders are able to participate in the profits of the company through dividends and lenders are able to put in place various security

arrangements by, for example, taking security over the shares of the company and/or the assets of the company.

There are tax advantages to setting up a company. For example, companies are currently subject to a maximum corporation tax on income of 28% rather than 41%, which generally applies to sole traders, partners (as individual person) and trusts. Private companies must register their governing documents, Memorandum of Incorporation (MOI), with the Companies and Intellectual Property Commission (CIPC). This information is publicly accessible. Private companies may not offer their shares to the public.

The name of a private limited company must end with the words 'Proprietary Limited' or abbreviation '(Pty) Ltd'.

³ There are four types of companies, which can have a for-profit objective but of these, the private company is the only relevant structure for social enterprises.

⁴ Please note that the Income Tax Act has various tax exemption initiatives for small business entities as well. For instance, the Small Business Funding Entity, through which South African corporates can channel their enterprise and supplier development initiatives

CASE STUDY

VULA EYE HEALTH MOBILE APP

The Vula Eye Health mobile app aims to change the way that primary health workers access information, carry out eye tests, connect with specialists and make referrals.

Legal form:

Single for-profit entity (private company)

Why?

Vula wanted to help beneficiaries by treating them as customers and gain income through paid-for services, rather than relying on grants (potentially less sustainable) or revenue generation through subsidies (more uncertain).

Advantages/opportunities:

As a private company, Vula is able to easily merge with other companies as well as raise capital (through equity as well as debt forms). It is also easy for the founder to exit through a share sale.

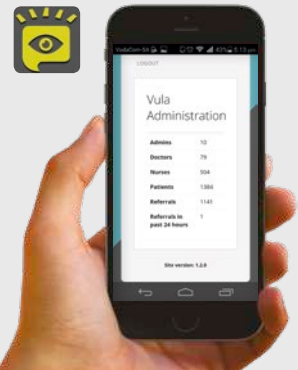
Disadvantages/challenges:

Some grants and donations are reserved for NPOs and PBOs, making these inaccessible to Vula. However, an increasing numbers of grants are available to businesses that operate as social enterprises.

How Vula is mitigating these challenges:

Some funders/donors allow access to Vula's services/products for free by making payments on behalf of third parties. Vula was able to obtain research grants during its start-up phase and has won a series of innovation awards. These awards provided funding as well as exposure.

www.vulamobile.com



Trusts

Advantages	Disadvantages
Low governance requirements	Not freely transferable interest
Beneficial when administering (large) assets for beneficiaries	

A trust is generally applicable for social enterprises that provide services to beneficiaries. In other words, a social enterprise that does not depend on, for instance, trade activity as its core business. Typically, trusts are set up to manage rather large pools of capital for beneficiaries.

A trust is created through written agreement. The founder of the trust, known as the 'settlor', hands over control of assets to another person known as the 'trustee'. The trustee administers those assets for his/her beneficiaries, who are identified in the written agreement. Trusts have been used to preserve wealth and to protect assets from the claims of creditors. A business trust, unlike an ordinary trust, authorises the trustees to use the trust assets for the purpose of continuing a business activity rather than just protecting the trust assets. However, the trustee always has fiduciary duties to act in the interest of the beneficiaries and cannot benefit from the trust assets.

The object of a trust will determine whether it is a for-profit or non-profit trust. For-profit trusts are often referred to as 'business trusts' whilst non-profit trusts are often referred to as 'charitable trusts'.

Business trusts were once popular because of the tax advantages associated with them, but these advantages have increasingly decreased to the extent that business trusts now generally pay higher rates of income tax and capital gains tax than private companies. From a regulation perspective, business trusts are less regulated than companies, but more regulated than partnerships, since trusts must be registered with the Master of the High Court and adhere to the requirements of the Trust Property Control Act.⁵ The Master of the High Court exercises a high degree of supervision over the appointment of trustees and may call trustees to account for the administration of trust property. A Trustee can be removed if he/she has acted in bad faith, breached his/her fiduciary or statutory duties, been sequestrated, or convicted of an offence that involved dishonesty.

Co-operatives

Advantages	Disadvantages
Operate for the gain of its members	Cannot obtain PBO and NPO status
Can obtain limited liability status	

Co-operatives must be registered with the Companies and Intellectual Property Commission (CIPC) and are governed by the Co-operatives Act,⁶ which defines them as: "An autonomous association of persons united voluntarily to meet their common economic, social or cultural needs and aspirations through a jointly owned and democratically controlled enterprise organised and operated on co-operative principles"

Members pool resources together and/or apply labour for their collective benefit and may be provided with products and/or services from the co-operative. Co-operatives always operate for the gain of their members. Importantly, they cannot obtain Public Benefit Organisation (PBO) or Nonprofit Organisation (NPO) status as set out in the Income Tax Act⁷ and Non-profit Organisation Act (the NPO Act).⁸

A co-operative may, in its constitution, provide for the benefit of limited liability, or its members may be exposed to personal liability depending on how the co-operative's constitution is drafted. All co-operatives must include the words "co-operative" or "co-op" as a part of their name and where the liability of the co-operative is limited, the words "limited" or "Ltd" must also be used at the end of its name. Co-operatives must maintain a registered office (and notifying the CIPC of any changes) and keep an up-to-date register of members, membership shares, directors and directors' interests. A co-operative cannot issue different type of membership shares, though certain co-operatives can apply weighted voting rights to membership shares.

An example of a co-operative is an agricultural co-operative whose members are local farmers. The co-operative's objective is to supply the farmer members with agricultural tools and fertilisers. Each farmer member contributes a sum of money on formation followed by monthly contributions. The co-operative enables its members to 'bulk purchase' using economies of scale which the individual members would otherwise not have had. The farmer members pay for the services and goods received from the co-operative. The profits are distributed (subject to a requirement under the Co-Operatives Act that 5% must be retained in a 'reserve fund') in line with the 'patronage proportion' of each farmer member; the greater the farmer's contribution, the greater his share of the profits.

HOW FOR-PROFIT LEGAL FORMS CAN OPERATE LIKE A SOCIAL ENTERPRISE?

- Establish a board to safeguard the social mission
- Change the Memorandum of Incorporation to reflect the dual mission and how profits will be reinvested in the business
- Get an international accreditation as a social enterprise / use international rating systems to measure the impact. For instance, the Trading for People and Planet accreditation by the Social Enterprise Mark, B-Corporation Certification, the Global Reporting Initiative's Sustainability Reporting Framework, or the Impact Reporting and Investment Standards (IRIS) by the Global Impact Investing Network
- Openly share financial statements and social impact reports

For more resources, go to the Bertha Centre's resource page: www.gsb.uct.ac.za/berthacentre

⁵ 7 of 1988, ⁶ 14 of 2005, ⁷ 58 of 1962, ⁸ 71 of 1997

Relevant Non-Profit Legal Forms for Social Enterprises

Social enterprises with a non-profit legal form have significant flexibility in terms of business activity and fundraising. They can generate income from multiple sources and receive various types of investments.

Potential benefits and challenges when adopting the not-for profit legal form for a social enterprise:

Potential advantages	Potential disadvantages
Can access donor funding such as grants, Corporate Social Investment (CSI) and government subsidies	(Often) depends on grants/donations
Will (often) align with donor objectives and stakeholder expectations	Limited access to traditional, commercial sources of capital
Can receive tax exemptions if accredited as PBO with Donor Deductible Status (DDS) status. This applies to Voluntary Associations, Non-Profit trusts and Non-Profit Companies and is outlined in Step 2.	More restrictive governance and ownership regulations



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Non-Profit Company

The term non-profit company is a misnomer because non-profit companies are not prohibited from making a profit. They must state their public objective in their MOI either as:

- a public benefit object (social/environmental mission); or
- an object relating to one or more cultural or social activities, or communal or group interests.

We generally use the term **public benefit object** to refer to both. This is often referred to as the social/environmental mission or dual purpose of a social enterprise. Non-profit companies may be engaged in trade consistent with, or necessary to, their stated objective. They can also hold shares, as well as other instruments, in for-profit companies, including public companies. Non-profit companies are not automatically allocated tax relief or any accreditations and must register to obtain pbo and npo status.

Unlike a for-profit company, a non-profit company does not have shares or shareholders but it may elect to have 'members' who may be natural or legal persons, including for-profit companies. If the non-profit company has members, they may or may not be permitted to vote. It is quite common for large donors to be granted member status and voting rights to permit them to monitor the performance of the relevant non-profit company, take part in the decision making process and to contribute to the management of the non-profit company. Voting rights can be equal between members or weighted in the MOI resulting in some members having more say than others.

NON-PROFIT COMPANIES NEED TO APPLY FOR NPO OR PBO STATUS TO GAIN BENEFITS SUCH AS TAX RELIEF.

Whereas a private for-profit company can have only one director, a non-profit company must have at least three directors.

A non-profit company is obliged to apply its assets and income to its public benefit object(s). The income and profit of a non-profit company cannot be distributed to incorporators, members, directors or any of their related persons. These persons cannot receive any financial gain from the company other than reasonable remuneration for work performed or reasonable payment for goods delivered to the company by or on behalf of these persons. Directors are also entitled to reasonable payment or reimbursement for expenses incurred in order to advance the objects of the company. When winding up of a non-profit company, any assets or amounts remaining must be distributed to another non-profit company, voluntary associations or non-profit trust with objects similar to the non-profit company being wound up.

There are certain restrictions on non-profit companies, which are intended to prevent non-profit companies being abused. These include that a non-profit company may not:

- amalgamate or merge with a profit company;
- convert into a profit company; or
- dispose of any part of its assets, undertaking or business to a profit company, other than on arms-length terms in the ordinary course of business.

Like private companies, non-profit companies are obliged to register as a company with CIPC and comply with certain other formalities under the Companies Act, such as:

- keeping accounting records which must in certain cases be audited;
- including the directors' names on all letters, catalogues and circulars distributed or published, whether electronically or by hardcopy;
- ensuring that proper minutes and attendance registers are kept of directors' meetings and members' meetings, if applicable; and
- filing accounting records at the CIPC.

Non-profit companies must keep a record of all revenue received from donations, grants and members' fees or in terms of any funding contracts or arrangements with any party. The name of a non-profit company must end with 'NPC'.

CASE STUDY

FOODBANK SOUTH AFRICA

Overview

FoodBank South Africa (“FoodBank SA”) is a registered NPC established in 2009 to provide a co-ordinated central logistical infrastructure that collects edible surplus food from manufacturers, wholesalers and retailers, and ensures that this food is redistributed to various registered and verified NPOs that help feed thousands of hungry people every day and offer development / remedial services in underprivileged communities.

Legal form

Non-profit company, registered as a Public Benefit Organisation (PBO) with Section 18A (S18A) accreditation, which grants Donor Deductible Status as described on in step 2. Why? FoodBank chose the non-profit company structure primarily as it served its central purpose of helping to feed South Africans largely through donations.

Advantages/opportunities

As a non-profit company with PBO status, FoodBank enjoys a number of benefits, including not having to pay tax (as long as any profits are reinvested in the company towards achieving its mission), receiving tax rebates on VAT purchases and tax exemptions for donors through the Donor Deductible Status accreditation. Additionally, being a non-profit company, the organisation’s inventory (food) is free (i.e. is donated, contributing to low cost



base) and FoodBank is able to receive grants from the state and philanthropic organisations. Because of partnerships with large retailers, FoodBank SA is able to scale its assistance via its innovative Virtual Foodbanking model. This allows FoodBank SA to link retail stores to Beneficiary Organisations that collect fruit, vegetables, and bakery goods on a daily basis.

Disadvantages/challenges

At the moment the income raised from various sources covers about than 85% of FoodBank SA’s operational expenses. A challenge is keeping costs low, and convincing donors (corporates) to donate towards covering operating expenses. Another potential hurdle is not being able to predict when food donations will be made, and what the variety may comprise. As a non-profit company not engaged in any trade it is reliant on donations and cannot control food items it receives and distributes. A move towards financial self-sufficiency through social entrepreneurship would help alleviate that.

Measures taken to combat challenges

FoodBank SA is trying to diversify its revenues away from just donations, and has built a significant project management function wherein the organisation manages feeding schemes and food-related CSR programmes on behalf of corporates, such as Pioneer Foods and Kellogg’s Foundation, for which it charges a management fee. Beneficiary Organisations that receive monthly food donations from FoodBank SA also pays a monthly subscription fee, although this is a nominal fee merely used to partly offset the organisation’s ongoing operating costs. The organisation has also developed an easy to prepare meal called the Foodbank SA QuickMeal, which it is able to sell to NPOs and corporates who want to sponsor meals. Lastly, the organisation is looking to expand into the micro-retail food trade through a social entrepreneurial venture by setting up social enterprises in poor communities that would sell donated food at a fraction of the price to low-income consumers. This would go one step further in both helping to achieve FoodBank’s mission whilst providing an alternate revenue stream.

www.foodbank.org.za



ANDY DU PLESSIS, MD OF FOODBANK SA

Voluntary Associations

Advantages	Disadvantages
Allowed to have profit-making activities that support the social mission	Profits should not be distributed to members, but it can act in the interest of these, if in line with the association’s objects.
Low governance	

Illustrative examples of voluntary associations: members form a voluntary association for the purpose of training unemployed persons as furniture manufacturers. During the skills training process, the association is entitled to earn profits from the furniture created by the unemployed trainees during their training. These profits can be used to buy further training equipment. Another example is a football club, which operates as a voluntary association earning revenue from entrance fees. The revenue can be used to pay the salaries of football players and coaching staff (who are not members of the voluntary association). The goal of the association is therefore not the making of profit for its members, provided none of the proceeds are distributed to members.

A voluntary association is formed by three or more people with a shared purpose. The people who make up an association are called its members and can be individuals or legal entities. Although a written agreement is not required, it is common practice to make use of a constitution, which sets out the intention and mutual agreement of the members for more certainty. Members of an association may contribute property or monies to the voluntary association, but this is not a requirement.

Voluntary associations must be formed for a purpose, which cannot primarily be the gain of the association or its members. An association of the association. It is permissible for an association to operate for the ‘benefit’ of members, for instance a housing association, which works to protect the value of a property that belongs to its individual members. Associations can be divided into incorporated associations and unincorporated associations. An incorporated

association has separate legal personality and enjoys perpetual succession, whilst an unincorporated association does not. The former arises when the intention of members is that the association has separate personality and is capable of acquiring assets and liabilities separate from its members. The clearest way to establish an incorporated association is to state in its constitution that it is a body corporate.

The name of an association, which is not of political or religious nature, can be registered by applying to the Bureau of Heraldry. The application will only be successful if the association’s purpose does not conflict with the public interest.

Non-profit trusts

Non-profit trusts are often referred to as charitable trusts. As discussed earlier, the key distinction between a business trust and a charitable trust is the trust’s object.. This should be stated in the trust deed. LifeCo UnLtd, which is described in more detail under hybrid structures, is a good example of how a charitable trust can complement a social enterprise.

THE FLEXIBILITY OF SOCIAL ENTERPRISES WITH A NON-PROFIT LEGAL FORM

Social enterprises with a non-profit legal form can do almost everything that a traditional business can do. For example, they can sell their goods and services directly to their beneficiaries, such as Social Enterprise Academy, Iyeza Express and Hubspace Khayelitsha. They can become suppliers of businesses, government and foundations, such as Greater Capital and the Centre for Justice and Crime Prevention. They can operate as intermediaries in the B-BBEE space, such as the Clothing Bank, Relate and Fetola. Or they can act as intermediaries between businesses and markets as the organisation TRADE-MARK does.

HYBRID STRUCTURES

A hybrid structure can allow for a social enterprise to harvest the benefits of both sides of the not-for and for-profit spectrum. It most often applies to an enterprise that has outgrown its current form and **therefore rarely applies to start-ups.**

The hybrid structure aims to reconcile conflicts between sources of funding associated with for-profit and non-profit legal forms. Whilst non-profit entities can have a right to an advantage, share or interest in the property or asset of a for-profit entity (proprietary interest), a for-profit entity cannot hold a proprietary interest in a non-profit. Also, a non-profit entity may not easily transfer its assets to a profit company. It should be noted that a hybrid structure must not circumvent tax law in terms of accreditations, etc.

A social enterprise with a for-profit legal form might wish to leverage the potential tax benefit and goodwill of a non-profit legal form to attract donor funding. Or it may simply wish to promote a specific organisational culture regarding its for-profit activities. Hybrid structures can be used in these instances to allow the social enterprise to achieve conflicting, yet complementing goals.

The 3 basic hybrid principles:

- A non-profit entity holds a proprietary interest in a for-profit entity and therefore receives profits from the profit entity, such as dividends when the non-profit entity holds shares in a private company;
- A for-profit entity is a member in a non-profit entity and often makes donations to the non-profit entity; and/or
- A contractual arrangement between the non-profit entity and for-profit entity exists, which allows the non-profit to receive income from the for-profit. For instance, the non-profit entity renders services to the for-profit entity or the non-profit entity leases assets from the for-profit entity. In both cases, the non-profit entity receives payment from

the for-profit entity. It is important that agreements between such for-profit and non-profit entities are concluded at 'arms' length'. In many instances it is simply easier for social enterprise with a for-profit legal form to partner with an existing nonprofit organization. It is recommended that a social enterprise seeking to enter into this type of hybrid model obtain legal advice before taking this step.

(Illustrative) example of a hybrid: A non-profit company, **Education NPC**, provides free educational equipment to disadvantaged communities. Education NPC has obtained NPO, PBO and DDS accreditations. During the course of advancing its social mission (public benefit object), it develops valuable intellectual property relating to educational materials and sets up a for-profit company, Education Profits Proprietary Limited, **Education Profits**, to commercialise this intellectual property. Education NPC can either transfer this intellectual property to Education Profits or it can grant a license to Education Profits, which allows it to commercialise the intellectual property. This hybrid structure allows Education NPC to retain its accreditations as well as comply with donor funding requirements, whilst its interest in Education Profits allows it to receive profits from a commercial activity as a source of funding. Education NPC can involve investors in Education Profits by, for example, issuing shares to the investors.

A good South African example of a hybrid structures is NICRO, a non-governmental organization, which provides prisoner rehabilitation and integration services to inmates at prisons across the country. In 2007, NICRO started a for-profit business called NICRO Enterprise that focuses on revenue generating activities by employing former convicts.

WHEN TO SET UP A HYBRID STRUCTURE?

If you already have a for-profit legal form and:

- You need to attract donations to further your cause
- Your various stakeholders are reluctant to work with a for-profit legal entity
- Your social activities require a distinctly different culture and skill set from your standard business activities
- You don't want the business focus to undermine your enterprise's social focus
- Your philanthropic activities need to be housed under a different brand.

If you already have a non-profit legal form and:

- The business activities are not directly related to your core purpose and are starting to take over the organisation
- Your business activities are competing substantially with commercial businesses
- Your business activities need to be housed under a different brand.

CASE STUDY

LIFECO UNLTD SA



Overview

LifeCo UnLtd SA is as a registered Section 21 NPO established in 1997. Its mission is to invest in people for enhanced enterprise and life performance. The NPO always traded for change and never had a fundraising department – choosing to sell impact and measurable outcomes to individual families and companies. It subsequently established a trust and a for-profit investments company in 2008 – to create LifeCo UnLtd Group. 100% of LifeCo UnLtd Investments (Pty) Ltd is owned by LifeCo UnLtd Trust. The trust has only one beneficiary: LifeCo UnLtd NPO. This hybrid structure allows the enterprise to freely implement business principles for social impact. No private individual owns a stake in the investments company – a decision taken in the founding year. This creates no doubt about the enterprises social mission and purpose.

Legal form

1. Section 21 NPO (similar to today's non-profit company), registered as a Public Benefit Organisation (PBO) with Section 18A (S18A) accreditation. 2. Charitable trust, which makes owning stakes in private companies or holding capital for gain possible. 3. A private company – 100% owned by the trust.



Why?

LifeCo UnLtd chose the non-profit / for-profit hybrid structure primarily to finance and fund its social mission. The structure is more complex to govern with many boards, but we manage that comfortably. It creates a transparent through line to social impact uncluttered by personal interest – but still allows many other companies to offer LifeCo UnLtd stakes in the firms – with a win/win outcome for both parties. LifeCo UnLtd is also able to raise capital from the market to finance its investment stakes or finance new ventures. It pays market related salaries for sustainable impact. With over R100m in assets currently and over 60 000 beneficiaries nationally, LifeCo UnLtd is able to develop asset based sustainability for society's benefit.

www.lcu-sa.com

STEP 2: Understanding Potential Accreditations

Social enterprises with a non-profit legal form can apply for NPO and PBO accreditations. NPO status enables the social enterprise to obtain funding from the state and other charitable foundations, whereas PBO status grants tax exempt status to the approved activities of the PBO.

NPO and PBO Status

NPO status requires submission of financial records and activities report to the NPO Directorate, which is available for public scrutiny. PBO status requires submission to the South African tax authorities, South African Revenue Services (SARS). Neither NPO nor PBO status should be confused with any non-profit legal forms discussed earlier in this guide.

	NPO Status	PBO Status
Reason obtained	Availability of donor/charitable funding	Income Tax Relief, Valued Added Tax relief
Source of law	Non-Profit Organisation Act	Income Tax Act, Value Added Tax Act
Registering authority	NPO Directorate	SARS' Tax Exemption Unit
Object requirements	Public purpose	Public Benefit Activity (ninth schedule)
Disclosure requirements	Disclosure to NPO Directorate, which includes broad public scrutiny	Disclosure to SARS

Obtaining NPO status

To gain NPO status the applicant must be able to show that it:

- Has been established for a public purpose;
- Is not for-profit, with the income and property of the organisation not distributable to the organisation's members or office-bearers except as reasonable compensation for services rendered; and
- Complies with other requirements, set out in section 12 of the NPO Act, such as the requirement that the organisation must, on being wound up or dissolved, transfer all of its assets to another NPO with similar objectives.

Obtaining PBO status

To gain PBO status, the applicant must be able to show:

- it is a non-profit company under the Companies Act or a trust or an association of persons that has been incorporated, formed or established in South Africa; or
- a South African branch of any foreign company, foreign trust or foreign association of individuals that is exempt from tax on income in its home jurisdiction; and
- its sole or principal object is carrying on one or more public benefit activities, where:
 - such activities are carried out on a non-profit basis and with an altruistic or philanthropic intent;
 - no such activity is intended to directly or indirectly promote the economic self-interest of any fiduciary or employee of the organisation, otherwise than by way of reasonable remuneration payable to that fiduciary or employee; and
 - such activity carried out by that organisation is for the benefit of, or is widely accessible to, the general public at large, including any sector of the public (other than small and exclusive groups).

Applications for PBO status should be made to the SARS' Tax Exemption Unit. Detailed requirements to qualify as a PBO are set out in section 30 of the South African Income Tax Act (ITA) and a list of permitted public benefit are set out in Part I and Part II of the Ninth Schedule to the ITA. Further permitted public benefit activities are determined by the Minister of Finance from time to time. In general, the public benefit activities are related to the needs, interests and well-being of the general public and include, for instance, welfare and humanitarian, health care, education and development activities.

Certain restrictions and conditions need to be adhered to in order to gain PBO status including:

- On dissolution, the remaining assets of the organisation must be transferred to a similar PBO, exempted institution or a sphere of the South African government. All of these entities must use the assets solely for the purpose of carrying out the Public benefit activities;

- Funds must be used solely for the object for which the organisation is established;
- The obtaining of PBO status must not result in unfair competition to other taxable entities; and
- Perhaps most importantly; the gross income derived from any business undertaking or trading activity cannot exceed 5% of total income or R200,000, with the exceptions set out below. Where it does exceed this, it will be taxed at normal rates applicable to the relevant form of business. The entity will not lose its status as a PBO as a consequence. Any undertakings or trading activity exceeding the 5% or R200,000 limits **will generally remain tax exempt when the undertaking or trade activity:**
 - is integral and directly related to the objective of the PBO;
 - assists the PBO in recovering costs;
 - does not result in unfair competition with taxable enterprises;
 - the undertaking or trading activity is approved by the Minister of Finance; and
 - the undertaking or trade activity is of an occasional nature and undertaken substantially with assistance on a voluntary basis without compensation.

Donor Deductible Status

If a donor wishes for a donation to be tax deductible from its taxable income, it will need to make the donation to an entity which has obtained approval to issue it with a receipt in terms of section 18A of the Income Tax Act. An entity which is registered as a PBO can apply to the SARS Tax Exemption Unit for approval to issue receipts in terms of section 18A Income Tax Act. In this guide this approval has been referred to as DDS accreditation for convenience.

Even if DDS accreditation is obtained, the donations made to the PBO will only be deductible from its taxable income when:

- the donation is made in good faith and the donor is not entitled to receive anything in return for the donation;
- the donation itself is not recoverable by the donor; and
- the donation must be used for a proper purpose.

There are limits on the amount of donations which may be deducted from the taxable income of a donor in a given tax year of assessment. PBOs which have received the approval in terms of section 18A are listed on SARS' website.

This means that a PBO with DDS can engage freely in revenue generating activities, which are in line with its social/environmental mission, while raising tax-exempt charitable donations. Generally, it can also go one step further and obtain a loan from a social investor.

Other

A non-profit may be able to obtain other tax relief, other than in relation to income tax, including from capital gains and donations tax.

Despite qualification as a PBO, an entity will be required to pay Value Added Tax ("VAT") unless a separate VAT exemption is obtained from the Tax-Exemption Unit at SARS. A PBO will always need to make 'pay-as-you-earn' ("PAYE") and 'unemployment insurance fund' ("UIF") payments to SARS if required.

HOW TO POTENTIALLY LOSE YOUR ACCREDITATION?

In general, there are four conditions where a social enterprise can lose its PBO and S18A accreditation:

1. The enterprise is no longer philanthropic;
2. Its primary activities are no longer for public benefit;
3. The business activities are unrelated to the core purpose of the enterprise and start taking over its agenda;
4. The business activities generate substantial income and start undermining South Africa's tax base. If this happens, the enterprise can be argued to have outgrown its legal structure and a hybrid model might be most suitable/ appropriate/ recommended

STEP 3: What is Your Business Model?

Social enterprises in South Africa are creative about their business models, which take on many shapes and forms. As seen in Step 1 and 2, both for-profit and non-profit entities can engage in business-like activities.

Step 3 provides more questions than answers in order not to limit the creativity of the reader. The business model outlines the key revenue sources and therefore helps determine the importance of, for instance, accreditations such as NPO, PBO or DDS. Will those be needed to attract donations, partnerships, etc.? As mentioned earlier, social enterprises with a non-profit legal form can do many of the things that a traditional business can do. For example, they can sell their goods and services directly to their beneficiaries, such as Social Enterprise Academy, Iyeza Express and Hubspace Khayelitsha. They can become suppliers of businesses, government and foundations, such as Greater Capital and the Centre for Justice and Crime Prevention. They can operate as intermediaries in the B-BBEE space, such as the Clothing Bank, Relate and Fetola. Or they can act as intermediaries between businesses and markets, such as TRADE-MARK. The four social enterprises featured here also use slightly different business models to fulfil their mission:

- The for-profit ones: Vula Eye App operates on a fee for service basis, partly making use of donor payments on behalf of beneficiaries. Khayelitsha Cookies, on the other hand, serves clients to help its beneficiaries.
- The non-profit: Foodbank SA is primarily based on donations, but increasingly pursues fee for service models.
- The hybrid: LifeCo Unltd. combines two non-profit entities and a for-profit entity to invest in and support social enterprises.

CASE STUDY

KHAYELITSHA COOKIES

Overview

Khayelitsha Cookies was registered as a close corporation in 2005. (In 2008, the private company replaced the close corporation) The ladies from Khayelitsha Cookies hand bake premium quality cookies; the number of cookies that the ladies bake in 40, can be produced by a machine in one day. The mechanics, however, are not important, as the key driver of the Khayelitsha Cookies is to create employment opportunities for local women.

Legal form

Registered as a for-profit business (close corporation), with a staff trust fund that owns a collective 30% share of the company.

Why?

Khayelitsha Cookies was chosen a for-profit legal form to encourage sustainability and profit-share for employees, which currently counts 91 ladies. Even though profit is core to sustainability, as long as the business can cover its costs, and continues to employ more women, the business is fulfilling its objective.

Advantages/opportunities

Operating with a for-profit legal form, holds the promise of demonstrating that business can be done differently. The Khayelitsha Cookies work to prove that it can be sustainable while steering away from mechanisation, and delivering a quality service and product.

Disadvantages/challenges

Prioritising employment opportunities before profit has been a long journey towards sustainability as the cookie ladies' margins are significantly lower than competitors'. When Adri Williams, who runs the company, discovered years ago it was due to close down due to accumulated losses of R2.5 million, she bought the company for R1, taking over all the debt at the same time, to save the jobs of the 52 breadwinners working for Khayelitsha Cookies at the time. Today, the company supplies to Garden Court and Southern Sun Hotels, as well as Tsogo Sun Casinos. It also sells bulk cookies, under the 'Scrumptious Cookies' brand to Pick n Pay.

www.khayelitshacookies.co.za



Key questions / considerations:

- Who are your beneficiaries? For social enterprises this is not always the customer as in the case of Khayelitsha Cookies.
- How interconnected are the business activities with the social programme?
- How will you distribute revenue / invest your (potential) profits? Will it go towards the members of your organisation or employees?
- Will you rely on grants and donations or other subsidies for regular operations?
- Is it important for your brand to be a particular type of entity (non-profit, co-op, etc.)

PERHAPS USE THE SOCIAL BUSINESS MODEL CANVAS (ON THE NEXT PAGE) TO HELP GUIDE YOUR THINKING.

Social Business Model Canvas

<p>KEY RESOURCES</p> <p>What resources will you need to run your activities? People, finance, access?</p>	<p>KEY ACTIVITIES</p> <p>What programme and non-programme activities will your organisation be carrying out?</p>	<p>TYPE OF INTERVENTION</p> <p>What is the format of your intervention? Is it a workshop? A service? A product?</p>	<p>SEGMENTS</p> <p>Beneficiary</p> <p>Customer</p>	<p>VALUE PROPOSITION</p> <p>Social Value proposition</p>
<p>PARTNERS & KEY STAKEHOLDERS</p> <p>Who are the essential groups you will need to involve to deliver your programme? Do you need special access or permissions?</p>		<p>CHANNELS</p> <p>How are you reaching your beneficiaries and customers?</p>		<p>Impact measures</p> <p>How will you show that you are creating social impact</p> <p>Customer value proposition</p> <p>What do your customers want to get out of this initiative?</p>
<p>COST STRUCTURE</p> <p>What are your biggest expenditure areas? How do they change as you scale up?</p>		<p>SURPLUS</p> <p>Where do you plan to invest your profits?</p>	<p>REVENUE</p> <p>Break down your revenue sources by %</p>	

Source: Social Innovation Lab. Can be found on socialbusinesscanvas.com.

STEP 4: What Sources of Finance are Available – How Might the Legal Form Influence These?

Whether a non-profit or a for-profit entity, you can, generally, take advantage of the innovative financial instruments that are offered by social investors.

Innovative finance as a field works to drive more capital towards social and environmental outcomes. It connects social entrepreneurs and social investors and increasingly blurs the lines between the public, private and social sectors.

Building blocks of innovative finance

Innovative finance redesigns traditional financial instruments such as grants, equity, loans, bonds, etc. to match the needs of these enterprises and interventions.

Loans: Just like a normal bank loan, the appeal for the investor is that they hope to get their money back plus interest.

- It could be structured as a normal loan where the money is paid back over a pre-agreed timeline, with a pre-agreed interest rate. But it could also be structured as a loan where the timeline or interest rate (or both) are significantly altered to be favorable to the organisation, prioritising social return and financial return.
- Alternatively, an investor can guarantee a loan made by another institution in order to limit the partner's exposure and drive down the cost of capital for the investee.

Loans are, generally, available to all legal forms.

Equity: Investors provide capital to an organisation in exchange for a portion of ownership (shares) of the entity. If the company makes a profit, so do the investors.

Equity is, generally, only available to private (for-profit) companies due to the ownership structure.

Revenue participation agreements: are hybrid financial instruments that allow the investor and investee to share the risk and reward of the enterprise more flexibly than debt. The investor obtains a right to a percentage share in the revenue of the enterprise, but does not take ownership shares. The payable amount is normally capped, either at twice the amount of the investment or at a certain time period.

Revenue participation agreements are generally available to social enterprises with non-profit as well as for-profit legal forms. However, it should be looked into on an individual basis due to the agreements' similarity to shareholding, which non-profits are prevented from.

Grants: Funds given with no expectation of financial return (profit) to the investor, the only expectation is social return (impact). This is the traditional donating. They can, however, also be recoverable grants, which can be thought of as no-interest loans, and convertible grants. Impact investors and venture philanthropists provide convertible grants based on the premise that if the enterprise becomes profitable, the grant will be converted into a loan.

Grants are available to all legal forms, but will only be tax exempt when the social enterprise has the proper accreditations, available only to those with a non-profit legal form. Social enterprises with a for-profit legal entities can receive donations, but these must be declared as income. They will be supplementary to income or used in the start-up phase of a social enterprise, when the founders would prefer to hold on to their equity.

BBBEE as source of funding for social enterprises

Social enterprises can also access funding through Enterprise and Supplier Development initiatives under BBBEE. To be eligible to receive this, a social enterprise will need to adopt a for-profit legal entity. It will need to have a turnover of less than R50 million per annum and be at least 51% 'black' owned. Suppliers need to adhere to additional

requirements in order to be considered an 'empowering supplier', which broadly entails buying no less than 25% of supplies locally, employing a work force of no less than 50% 'black' people and processing no less than 25% of raw material locally. Micro-enterprises and start-ups are automatically recognised as 'empowering suppliers'.

For more resources on how to access Enterprise and Supplier Development related funding, please go to www.gsb.uct.ac.za/berthacentre

INNOVATIVE FINANCE INSTRUMENTS

The overview of innovative finance instruments above demonstrates how diverse fundraising for social enterprises is becoming. They can, generally, be accessed by social enterprises with for-profit and/or non-profit legal forms.

Impact investing Investors who intentionally seek measurable financial and social returns. South African players include Futuregrowth Asset Management and Goodwell Investments.

Patient capital Pioneered by the Acumen Fund, this refers to a long-term investment that maximises social rather than financial return. Acumen describes it as "a debt or equity investment in an early-stage enterprise providing low-income consumers with access to healthcare, water, housing, alternative energy, or agricultural inputs".

Venture philanthropy According to the European Venture Philanthropy Association (EVPA), "[it] works to build stronger social organisations by providing them with both financial and non-financial support in order to increase their social impact".

Social venture capital Using the principles of venture capital, social venture capital investors support start-ups / early-stage social enterprises. South African players include Lifeco UnLtd.

Social Impact Bond (SIB) The Rockefeller Foundation defines a SIB as: "an innovative method of financing social programmes in which governments partner with service providers and private sector investors to fund social programmes. Investors are repaid if and when improved social outcomes are achieved. Thus, government pays only if the services are successful at meeting the needs of its citizens".

Development Impact Bond (DIB) A variation on the SIB where private outcome payers, such as Development Finance Institutions (DFIs) or foundations, partner with or take the place of government in funding social impact in developing countries. As in the case of a SIB, investors only earn a return if predefined outcomes are achieved.

Microfinance The lending of small amounts of money to entrepreneurs and small businesses at reasonable interest rates.

Charity bond Pioneered in the UK, this kind of bond gives charities access to medium-term debt finance, allowing for less volatility in cash flow. For instance, a charity could borrow the amount for a project upfront and then fundraise for it while the project is in operation and has results to show.

Crowdfunding Crowdfunding raises monetary contributions from the crowd, typically through an online platform. A prominent South African example is Thundafund.



STEP 5: How Will Your Social Enterprise be Governed?

What level of flexibility will the founders need and how should profits be distributed? These are, to a large extent, personal considerations.

Where the previous steps have been largely fact-based, step 5 is determined by the founders' and/or the beneficiaries' personal considerations and temperaments. In its simplest form, this is a choice between flexibility and control, as well as how to distribute potential profits.

Social enterprises with a non-profit legal form, such as non-profit companies, generally have to adhere to quite restrictive governance regulations and cannot be individually owned or managed. Profits are recycled within the organisation, and financial and narrative reports are made publicly available.

For-profit legal forms, such as the private company, on the other hand, can be privately held and maintains flexibility in terms of profit-share arrangements.

Key considerations:

- Who are the founders and what is your expectation in terms of ownership of the organisation?
- Who will control and manage the organisation?
- What are your personal and financial goals (as a founder) when starting this organisation?
- How long do you intend the organisation to exist and what is your exit strategy (for yourself and for investors)?

As mentioned previously, a social enterprise with a for-profit legal form can increase its credibility as a social enterprise by establishing an external board of advisors. The board can help it safeguard its social mission. This however also applies to social enterprises with a non-profit legal form that is working to improve its business model. In 2012, the World Economic Forum and the Schwab Foundation published a helpful, comprehensive guide on governance of social enterprises and how to set up an efficient board; *The Governance of Social Enterprises: Managing Your Organization for Success*.

STEP 6: What is the Right Legal Structure for a Social Enterprise?

Step 1-5 of this guide have provided an overview of the relevant legal forms for social enterprises in South Africa as well as key considerations. Here is a summarised journey.

STEP 1

Provided an overview of the different legal forms available to social enterprises, for-profit and non-profit legal forms as well as hybrid forms.

Key take-away: Generally, the non-profit company and the private company are good fits for social enterprises.

STEP 2

Provided an overview of NPO, PBO and DDS accreditations. **Key take-aways:** These accreditations are only available to social enterprises with a non-profit legal form, and are particularly relevant to enterprises that work with government or receive donations. Social enterprises with DDS accreditation (donors can obtain tax exemptions) are also able to generate income and take on social investment.

STEP 3

Map the key revenue sources of the enterprise. **Key take-aways:** Do a thorough examination of the business model and options.

STEP 5

How will your social enterprise be governed? **Key take-aways:** Who makes up the organisation – a wider community group or two founders? What level of flexibility will the founders need and how should profits be distributed? These are, to a large extent, personal considerations.

STEP 4

What sources of finance will your social enterprise need? **Key take-aways:** Innovative finance instruments can, generally, be accessed by both for-profit and non-profit legal forms. Loans are accessible to all organisations, as are revenue participation agreements, in principle. Simultaneously, for-profit legal entities can receive grants/donations, although these must be declared as income. Such donations can be seed funding from foundations, social venture capital funds or pitch competitions. The difference is that these are supplementary to income or used in the start-up phase of a social enterprise, when the founders would prefer to hold on to their equity.

STEP 6

Based on steps 1-5, reflect and settle on the best legal form for your social enterprise.



Conclusion

The guide has aimed to demonstrate that there is flexibility within the various legal forms and that the convergence between the for-profit and non-profit sectors can, to a large extent, take place within the current legal environment.

The guide has posed the following questions to you as a reader. As you look (again) at the table below and reflect on the best legal form, it is recommended that you keep these in mind.

- Who are the founders and what is their expectation in terms of ownership of the organisation?
- Who will control and manage the organisation?
- What are the (potential) income sources / the make-up of your business plan?
- Will you rely on grants and donations or other subsidies for regular operations?
- Is it important for your brand to be a particular type of entity (non-profit, co-op, etc.)
- Where will you get your seed funding and working capital?
- Who are your investors/shareholders?
- Who are your beneficiaries/customers/stakeholders?
- What are your personal and financial goals (as a founder) when starting this organization?
- How long do you intend the organisation to exist and what is your exit strategy (for yourself and for investors)?
- What social impact do you want to achieve and how will you measure it?

		FOR-PROFIT LEGAL FORMS				NON-PROFIT LEGAL FORMS		
		Sole proprietorships & partnerships	Private company	Trusts	Cooperatives	Non-profit companies	Voluntary associations	Non-profit trusts
BUSINESS MODEL								
Revenue models (not limited to the examples listed here)	*Donations	✓	✓	✓	✓	✓	✓	✓
	Fee for service	✓	✓	✓	✓	✓	✓	✓
	Trading activities	✓	✓	✓	✓	✓	✓	✓
FINANCING								
External finance	Donations	✓	✓	✓	✓	✓	✓	✓
	Loans (secured & unsecured)	✓	✓	✓	✓	✓	✓	✓
	Equity		✓					
	**Revenue-participation	✓	✓	✓	✓	✓	✓	✓
***GOVERNANCE								
	Broad-based				✓		✓	
	Individual	✓	✓	✓				✓
	Small group	✓	✓	✓		✓		✓

* All legal forms can receive donations, but these are more likely to occur when the receiving part is registered as a non-profit with Donor Deductible Status (DDS).

** Revenue-participation agreements are, generally, available to all legal forms. However, it should be verified on a case-by-case basis that the agreement is in line with potential accreditations and relevant legislation.

*** These should be read as generic guidance, as governance can be amended on case-by-case basis within each legal form. For instance, a cooperative can appoint a managing director, and a private company can appoint a more broad-based management group.



ABOUT THE BERTHA CENTRE

The Bertha Centre for Social Innovation and Entrepreneurship is a specialised unit at the UCT Graduate School of Business (GSB). The Centre's mission is to uncover, connect, pioneer and advance social innovators and entrepreneurs who share their passion for generating inclusive opportunities and achieving social justice in Africa. Established in partnership with the Bertha Foundation in 2011, it has become a leading academic centre dedicated to advancing social innovation and entrepreneurship. Today the Centre is a dynamic space, with three key initiative areas, which include Education Innovation, Inclusive Healthcare Innovation and Innovative Finance with a strong focus on Africa.

Some of the Centre's highlights include integrating social innovation into the GSB's curriculum, establishing a wide community of practitioners and awarding over R3 million in scholarships to African students. Together with its partners it has begun testing solutions ranging from social impact bonds, social franchising, to healthcare innovation hubs.

ABOUT THE INNOVATIVE FINANCE INITIATIVE AT THE BERTHA CENTRE

Working with social finance experts from across the world, the Innovative Finance initiative partners with governments, enterprises, and investors to research, incubate and test promising social financing vehicles across Africa. Recognising the importance of education and field building, the team regularly convenes stakeholders and publishes on the topic of impact investing.



BERTHA CENTRE FOR
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