Business acquisition in the community sector in New Zealand

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Abstract

The community sector in New Zealand is diverse, and organisations within it receive their income from a variety of sources. Those sources of income are not currently enough to meet real, perceived, and anticipated need. This research looks at one potential strategy which has not been widely used to date, that of business acquisition, in order to explore if it could provide a viable additional source of revenue for community organisations, and in what circumstances. Using a transdisciplinary approach, the research considers the use of business strategies not commonly found in the community context.

The research is based on interviews with eleven chief executives, senior managers and consultants in the community sector who had experience with or interest in the strategy. In particular the research focussed on organisations that had already adopted business-like practices and met the broad definition of social enterprise. The participants were asked a range of questions designed to address:

1. What conditions need to be in place for a social enterprise to acquire an existing for-profit business?
2. To what extent is it necessary for an acquired business to have aligned purposes, values or outcomes to those of the social enterprise?
3. What conditions need to be in place for a social enterprise to successfully run an acquired business long term, and to ensure its on-going profitability and sustainability?

The research found that the strategy of business acquisition could produce a viable source of revenue for community organisations provided a number of relatively complex criteria were met. Three stages were identified for the strategy including getting investment ready, due diligence on an acquisition, and then the effective running of the acquisition. All three stages needed to be done well. In particular the need for skilled governance, a thorough understanding of business practices, and access to affordable investment capital, were essential to even considering the strategy.

The research also found that if the identified criteria were not met then the strategy of business acquisition carried the very real risk of undermining the organisation, even to the point of closure. Exploration of risk factors was integral to the research, both the risks involved in the strategy, and the risks involved in doing nothing. Regardless of whether this strategy was undertaken by an organisation, the research found that reaching and maintaining a state of investment readiness was important for organisations to enable them to be proactive and creative in meeting their mission.
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Chapter one – Introduction

The community sector in New Zealand is a widely diverse combination of organisations, ventures and people, which include those who focus on recreation, arts and culture, health, education, religious purposes, advocacy, social services and community development. It is also known by other names such as the third sector, the non-government (NGO) sector, the voluntary sector, and the non-profit or not-for-profit sector (NFP). (Sanders, O’Brien, Tennant, Sokolowski, & Salamon, 2008) This sector in New Zealand includes more than 97,000 organisations whose paid and voluntary contributions to the national economy equate to $9.8 billion per year or 4.9% of GDP (Sanders et al., 2008). In all parts of the community sector, issues of organisational structure, business models, income, purpose, and ownership are as relevant as in other sectors. One model which is gaining recognition and support is social enterprise.

The term social enterprise is relatively new in New Zealand, although it is well recognised in many countries around the world. In broad terms, though there is no single definition that is universally accepted, social enterprises are organisations in the community sector which blend business skills with achieving social good. As Social Enterprise UK puts it, a social enterprise is an organisation that “trades for a social and/or environmental purpose” (Social Enterprise UK, 2013a, p. 3). They usually have charitable tax status and often hold public sector contracts to deliver services. Typically they have a limited range of income sources such as contracts, grants and donations, all of which can be vulnerable to sudden changes outside of their control (K. Alter, 2004). While the term social enterprise is only slowly growing in currency, it is clear that a portion of the community sector meets this definition, whether they use the term or not.

As the Chief Executive of a medium sized social enterprise in the city of Auckland, New Zealand, the author is continually faced with the challenge of finding the financial resources to enable the organisation to meet its core purposes. That challenge can be summarised in the chain of logic below:

- It takes money and creativity to address social issues.
- In relation to money, the traditional and familiar methods of fundraising have become more difficult to access in light of the global financial crisis and the level of overall demand.
- In relation to creativity, external contracts for service provision are more and more constrained by complicated accountability and compliance mechanisms.
- In addition, internal and external stakeholders are rightly asking questions about outcomes, what works to bring about social change, and whether our limited resources are deployed in the most effective and efficient ways.
- It is therefore valid to consider whether more sustainable sources of income are available to social enterprises in New Zealand.

Although there is a life cycle in community organisations as in any business (McMorland & Erakovic, 2013), the current economic and funding climate is contributing to the demise of well-respected and long standing organisations such as the Eden Counselling service (Engage Aotearoa, 2012). In the current environment, there are clearly apparent risks with having “all your eggs in one basket”, as changes in Government policies, contracts and funding leave many organisations vulnerable to rapid shifts in policy and income. This reality provides the impetus for organisations to look at ways to diversify their income to ensure long term sustainability, and the social enterprise model of combining business skills with meeting social outcomes provides insights and tools in this direction.
The number of social enterprises is significant and growing worldwide. Social Enterprise UK estimates there are 68,000 social enterprises in the UK (Social Enterprise UK, 2013b), although the UK Social Enterprise Live website indicates that there could be between 68,000 and 232,000 social enterprises, depending on the definitions used (Hampson, 2010). For those organisations, securing or generating adequate income is essential. A recent report by the New Zealand Charities Commission has revealed that 39% of all registered charities generate income from services and trade (Charities Commission, 2013). In Australia, it is estimated there are 20,000 social enterprises (Barraket, Collyer, O’Connor, & Anderson, 2010) with 29% of charities deriving some income from a business venture. Many other countries round the world have some variation of social enterprise, and there are few who do not need to wrestle with the issue of diversified income sources.

This research focuses on two separate contexts that historically have largely been seen as mutually exclusive, that is “business” and “community”. The traditional priority of business has usually been creation of value for shareholders, while for the community sector the emphasis has been the common good, preferably delivered at as little cost as possible. More recently there has been research (Cheng & Ludlow, 2008) that suggests the inclusion of a social outcome in business objectives can become a key factor in differentiating that business and providing both advantage and scope for innovation. For some time now there has been a growing acknowledgement that the sustainability of an activity focused on social outcomes is improved when there is a reliable source of surplus or profit (Hayssen & Viravaidya, 2001).

Diversification of income sources is a key strategy to ensure the sustainability of the organisation. In the for-profit sector, typical private enterprise businesses follow a “user pays” model, where the customer pays for the service or product they receive (see Figure 1). To increase nett income, the for-profit business needs to reduce its costs and/or sell more of its product or service. But, for many community groups, costs are usually at the minimum possible level, and the person receiving the service does not always pay for it – this could be called a “society or community pays” model i.e. a third party pays for the service to be provided. For a social enterprise to diversify its income streams, it needs to either find ways to encourage its current customers to pay for their services (unlikely, at least initially), find other third party payers who will fund the work (difficult in the current economic climate), or find new ways to generate income (either through current or new business streams). While each of these has possibilities, none will provide instant income and all will require long term strategies to achieve.

In recent years, the author’s attention has been increasingly drawn to the potential of business acquisition as a legitimate strategy for many social enterprises. In this context, the term “business acquisition” covers a range of scenarios where one business entity purchases all or some of another entity – this may involve a division of a company, a product line, an income generating asset, or a whole company (Snow, 2011). This research takes as a given that purchasing an existing profitable venture will involve an extended process of due diligence prior to the purchase, and then the mobilisation of a wide range of skills to continue to run that business profitably (Snow, 2011).

Transferring ownership of a for-profit business into the hands of a social enterprise raises many questions. These include the nature of the due diligence required, as well as the other necessary or desirable structural, governance, and management practices to ensure business acquisition is a viable strategy to resource social enterprises to better meet their social objectives.
The specific research questions that underpin this thesis are designed to identify the skills required, and factors involved, for a social enterprise in acquiring a for-profit business. In particular:

1. What conditions need to be in place for a social enterprise to acquire an existing for-profit business?
2. To what extent is it necessary for an acquired business to have aligned purposes, values or outcomes to those of the social enterprise?
3. What conditions need to be in place for a social enterprise to successfully run an acquired business long term, and to ensure its on-going profitability and sustainability?

The sustainability of social enterprises is a complex issue, possibly more complex than sustaining a regular for-profit business, as there are multiple accountabilities and outcomes required. The financial sustainability issue alone is complex and, in turn, purchasing a business is only one strategy to achieve financial sustainability. In focussing on business acquisition, this research recognises that there are other aspects of sustainability which will fall outside of the scope of investigation (e.g. environmental sustainability), as well as other strategies that could also contribute to that financial sustainability (e.g. business start-ups, or mergers).

Previous conversations with people who have a genuine interest in this topic have suggested that there is significant value in the concept under review, and significant interest in the applicability of findings. As well as being of practical interest and value to the author’s organisation, the outcomes of this research will also be useful to other social enterprises who may be seeking other forms of sustainable income. Ultimately, the identification of key ingredients involved in making a successful business acquisition for social enterprises provides something of a blueprint, or at least a general guide, for groups to use. It may be that, in order to be accessible to other social enterprises, a further report may need to be written that summarises for a non-academic audience the key findings and recommendations. As such, it is suggested that this research
contributes in some small way to the transdisciplinary dialogue needed to help solve complex social issues through this new and relatively untried combination of previously disparate approaches.

By combining a range of opinion obtained through a secondary review of existing literature, and primary data collection through interviews, the research brings practical, experientially based perspectives to the challenging task of how to provide the economic resources needed to solve complex social issues. The exploration of the experiences and views of those with a range of perspectives supports the possibility of new knowledge and solutions emerging.

Chapter 2 of this thesis examines a range of existing literature sources, both from New Zealand and overseas, in order to explore what is already known in this field and to identify gaps and areas for exploration.

Chapter 3 outlines the methodology used to gather primary data on the value and parameters of business acquisition as a strategy that social enterprises can use to support their sustainability. The process of data collection and analysis is described and explained.

Chapter 4 covers the presentation of the data, purely from the point of view of the contributions and views of the participants.

Chapter 5 follows with a discussion and analysis of what those data suggest in the light of the research questions, including recommendations for each aspect of the stages of acquisition.

The final chapter provides an overall summary of the research, including recommendations, and looks at the implications for practitioners who may be considering the strategy of business acquisition for social enterprises. It concludes with identifying some potential areas in which follow up research would be useful.
Chapter two – Literature review

2.1 Introduction

Within this chapter a range of literature sources is explored, to both identify something of what is known in the area of study, as well as to identify gaps in relevant knowledge that this research can make a contribution to addressing. The first section explores the broad characteristics of the community sector, including a focus on New Zealand, and on the place of social enterprise within that sector. The next section looks in more detail at the nature of social enterprise, including an exploration of some of the different views that are held about social enterprise, and on the nature of income sources that social enterprises have available to them. This is followed by a discussion of the issues related to diversification of income, and then an exploration of the issues related to the strategy of acquisition. The final section summarises what is known and unknown, and further articulates the research questions that stem from that summary.

2.2 Community sector profile

2.2.1 From charitable donation to community organisation

The community sector is an umbrella term for a broadly diverse range of people and organisations seeking to serve the common good in equally diverse ways. In addition to the range of names for this sector referred to in the Introduction, the community sector is also referred to by the descriptors: more than profit, not-for-personal profit, third sector, civic society, common good, and the charitable sector. Regardless of the descriptive term used, most groups operating in the community sector are likely to have some kind of charitable status or tax benefit that recognises their contribution to the common good. This section examines some characteristics of the community sector from the perspective of those who are involved.

While a detailed analysis of the origins of charity is precluded here, it is important to note that variations of charity have been present in many societies for hundreds of years. While some see charity as the obvious and natural way to care for the most vulnerable, others such as Pallotta (2008) have a more critical or cynical view of the origins and outcomes of charity. Pallotta believes charity in its current form is an outcome of Puritan ethics, and is a way for those who make money exploiting others to salve their consciences by giving a small proportion of their money away to those in need, while not recognising that this very need may have been caused by the same money making ventures that created the surplus funds in the first place.

To balance this, it is also important to note that there are not only a wide range of motivations to be involved in charity, but also that all societies have, both pre-charity and more recently, developed ways to care for each other, and particularly the most vulnerable. (Ashton, 2010) says “industrialisation, urbanisation and economic migration have disrupted the natural way of things. It’s one of the reasons we now have social entrepreneurs, to reconnect people with humanity” (p.254). Charity is also a strong component of all the major faith traditions, and often goes hand in hand with matters of social justice (Fiorenza, 2000).
A comparison of what are sometimes called the Karpman or Drama triangle, and the Winner’s triangle (Depression Support Network, 2013) sees elements of these two perspectives played out in many community sector organisations i.e. is the motivation in helping others to rescue or to empower? Is it primarily for our benefit or the other’s? Individuals themselves can operate from a rescuing or an empowering stance as can organisations. (Frances, 2008, p. 26) says “Generally, people did not give to charity out of love, but as a way of making themselves feel better.” When the root causes of the need for charity are addressed, and when charity is seen as an important precursor to the more complex tasks of equity and justice, then charity has a rightful place. If it becomes an end in itself, it can remain part of the forces of injustice. (Fiorenza, 2000, p. 91) argues for a “complementary rather than contrasting, dualistic relation between charity and justice.”

![Image of the Drama Triangle and the Winner’s Triangle](image)

**Figure 2.** The Drama Triangle and the Winner’s Triangle (Depression Support Network, 2013, para. 3)

Nevertheless, for all the good that charity has done and continues to do, it needs to be acknowledged that the divide between rich and poor continues to widen in many countries, and the implications of this are far reaching (Pickett & Wilkinson, 2009). It also needs to be noted that there are those who see social enterprise as buying into a capitalist system that is itself the cause of social ills. This is discussed more thoroughly in section 2.3.2. In this respect, social enterprise can be an alternative approach to address some of the underlying issues that keep people disadvantaged and in poverty.

Community sector organisations are seen by some as part of the same tradition as the missionary and colonial movements, which seek to share or impose their sometimes altruistic solutions on communities (Gregor, 2013). Gregor suggests as an alternative that, if we choose to see low income people as customers rather than as beneficiaries, we will listen to what they believe are the solutions and find out what they want to purchase or receive. Others would call this a community development approach and have promoted the view for many years that solutions come from communities themselves. Chavis and Wandersman (1990, p. 56) suggest that “the building of a sense of community acts as a mechanism to stimulate the healthy development of the environment and the people who inhabit it.”

The motivations of those who establish and then maintain community sector organisations, regardless of type, location or context, provide a legacy that often becomes embedded in an organisation. It can take a range of factors, and often a crisis, (McMorland & Erakovic, 2013) for a group to re-examine their underlying motivations and assumptions in order to establish if they continue to be appropriate in serving the common good.
2.2.2 The community sector in New Zealand

From very early in New Zealand’s colonial history, there were examples of people organising community efforts to assist those in need; or to gather together around specific purposes such as social, sporting, cultural, educational or faith based activities (Anglican Diocese of Auckland, 2013). Some of the benevolent societies began as early as the 1840s (Tennant, 2012), and there have been a wide variety of types of groups that have come and gone since.

Māori society in Aotearoa, pre European contact, was organised on communal lines, and there were a range of support structures available based on hapu and iwi characteristics (Tennant, 2012). While these have to some extent weakened over time, they are often still the preferred way of meeting social and community needs for Māori, and recent government policy has focussed on strengthening and resourcing these.

It has been difficult over the years to quantify the size and nature of the community sector until the establishment of the Office of the Community and Voluntary Sector, and the Charities Commission (now both incorporated into the Charities Services section of the Department of Internal Affairs). Recent estimates put the number of registered charities at 26,786 (Charities Services, 2015) and the overall number of community groups as significantly more.

The community sector in New Zealand includes a broad spectrum of types of organisations, from those who function solely with voluntary support and limited funds, through to those who have significant assets and funding and a large professional workforce. There are a range of models that examine the typical lifecycle of an organisation, looking at factors such as size, purpose, and funding, as well as developmental issues such as growth and decision making (McMorland & Erakovic, 2013). Social enterprises typically arise either as a way to structure a new endeavour, or as a transition from, or addition to, an existing organisation which is seeking to find different ways to work or fund itself.

2.2.3 Social enterprise in the New Zealand community sector

As mentioned earlier, there are many third sector/community sector groups in New Zealand who already incorporate elements of social enterprise, or indeed fit one of the many definitions of social enterprise. The need to secure a diversified range of income sources, and/or the increasing growth of an organisation, are often precipitating factors in becoming more “business like” (McMorland & Erakovic, 2013, p. 110). This process involves the adoption of a more professional approach, and provides the capacity to become more creative and to expand.

There are several pieces of current and recent research aiming to quantify and qualify the nature and extent of social enterprise in New Zealand. The Office of the Community and Voluntary Sector, now part of the Department of Internal Affairs, conducted a social enterprise mapping exercise in New Zealand in 2012 (Department of Internal Affairs, 2013a). Although the sample size of 421 was by no means comprehensive, the survey concluded there is a mature social enterprise sector with more than 70% of those surveyed having been in operation for more than 10 years. However, it was clear that not all of the participants were using the language of social enterprise despite meeting the definition.
Inspiring Communities (2012), in a project supported by the Department of Internal Affairs and Creative New Zealand surveyed businesses on the nature of their involvement and collaboration with charities and found that, while there are a range of ways that businesses are involved with community organisations, this involvement was usually small in nature and potentially extendable. There is a current PhD thesis being written on “Transitioning from Not-for-Profit to Social Enterprise: A Complexity View” (Fitzgerald, 2012), and an extensive survey of 100 social enterprises in New Zealand has been completed with support from Lotteries Community Research Funding and Unitec. In the summary of the literature review from this survey, Jennings (2012a) synthesises clearly from a range of sources the diversity in terminology, values, beliefs, and practices that exists in the social economy in New Zealand.

The Department of Internal Affairs note on their website their acknowledgment of and support for the growing social enterprise sector (2015). They also recognise there are challenges for social enterprises particularly related to their business and funding needs. Although some community organisations have always derived some component of their income from trading, sales or other business activities, and although many community organisations have sought to run in business-like ways, it is only very recently that we have begun to explore the language of social enterprise in New Zealand as applied to these aspects of organisations (Kaplan, 2013).

2.3 Social enterprise profile

2.3.1 Key characteristics of social enterprise

There are significant variations in the definition of social enterprise around the world. Barraket and Collyer (2009) look at the breadth of possible definitions and some of the issues involved in narrowing this down to any readily agreed definition. Even within countries there is seldom consensus around how to align social enterprise with factors such as overall purpose, legal forms, governance, the proportion of surpluses which must be re-invested, the nature of the activities, tax issues etc.

Peattie and Morley (2008) looked at 150 sources and concluded that the hybrid and diverse nature of social enterprises creates a series of paradoxes, which make it difficult to both define and research social enterprise. Often disagreements around definitions centre on outcomes and the extent to which, whatever the nature of the business, social outcomes are directly or indirectly achieved (Cheng & Ludlow, 2008). The strong values component in most NGOs, and social enterprises in particular, means there is an inevitable emphasis on the extent to which the organisation’s values are evident in any business or trading activity. In their report to the Small Business Service in the UK, Smallbone, Evans, Ekanem and Butters (2011) say about social enterprises that “their key distinguishing features are their social aims and social ownership, combined with trading viability” (p. 4).

One definition of social enterprises, by way of example, used by Social Traders Australia (2013) is that they:

“a. Are led by an economic, social, cultural, or environmental mission consistent with a public or community benefit;
b. Trade to fulfil their mission;
c. Derive a substantial portion of their income from trade; and
d. Reinvest the majority of their profit/surplus in the fulfilment of their mission”
Part of the reason for the confusion around definitions of social enterprise stems from the understanding of what constitutes trading and the scale of that trading in relation to the organisation’s overall income. For some, this term only applies to tangible sales and commercial activity, usually separate from the core business of the entity (McMorland & Erakovic, 2013). With this understanding, few New Zealand community organisations would meet the common definitions. The alternative understanding is that trading applies to any sale of goods or services to an external customer, which can include a government or local government contract (Social Traders, 2013).

Those who adopt the former understanding often see social enterprise as something separate from, or to be added to, the parent organisation. Those who adopt the latter understanding tend to see social enterprise as a way of defining a type of organisation within the community sector. Such community organisations approach everything they do from a businesslike perspective to meet their social outcomes, whether they identify part or all of their entity as operating more intentionally in a businesslike way. These organisations may start off as intentional social enterprises, or may evolve in this direction as time goes on. The author will adopt the second of these understandings throughout this research, as it appears to fit more closely with the New Zealand context.

Several years ago, global social entrepreneur Nic Frances (Frances, 2008) said that a continued focus on finding one agreed definition of social enterprise may be an unnecessary distraction, and that we are better putting our energies into thinking outside the square in terms of solving the world’s complex problems using both a business and a social focus combined. While acknowledging the efforts of others to define social enterprise, for the purposes of this research the author will accept the Department of Internal Affairs definition three paragraphs above as providing a broad framework to guide this exploration.

2.3.2 Philosophical conflicts and opposing views

This research focuses on two separate contexts that historically have been seen as mutually exclusive, that is “business” and “community”. The traditional priority of business has been the creation of value, usually profit, for shareholders, while for the community sector the emphasis has been on providing for and strengthening the common good, preferably delivered at as little cost as possible. More recently there has been research that suggests the inclusion of a social outcome in business objectives can become a key factor in differentiating that business and providing both advantage and scope for innovation (Cheng & Ludlow, 2008). There is also growing acknowledgement that the sustainability of an activity focused on social outcomes is improved when there is a reliable source of surplus or profit (Hayssen & Viravaidya, 2001).

Alter & Dawans (2006) explore the different perceptions of how the term social enterprise is used. For some, it is applied to a whole organisation that makes the transition from a traditional community organisation; for some, it refers to a business unit incorporated into the not for profit which may have a blended focus, or alternatively a focus purely on creating income; and, for others, the term applies to a completely separate business unit. Alter & Dawans believe that, by definition, if a business unit or a whole organisation has as its primary purpose the generation of income, then also by definition it cannot be a social enterprise. Once again it would seem that the conversation about definitions can risk distracting us from the focus on the outcome of generating enough resources to address the social issues at hand.
Social enterprises seldom make significant surplus income – they aim to meet multiple bottom lines well, and orient an organisation to a more businesslike way of operating, but they are unlikely to be a cash cow. Despite the growth in numbers of social enterprises in the UK reported in the State of Social Enterprises Survey 2013, the median revenue of social enterprises decreased from £240,000 in 2011 to £187,000 in 2013 (Social Enterprise UK, 2013b). One commentator noted in relation to these figures that “most social enterprises are small, shrinking, vulnerable, low margin businesses with little cash. Not exactly a target rich investment environment!” (Black, 2013, p. 1)

Many attempts are being made to reduce the vulnerability of social enterprises, including scaling up, tendering for a wider range of public sector contracts, and developing new endeavours. Some interesting dialogue is happening at present on social enterprise websites, particularly in blogs, around the ethics of these types of approaches. Cox (2013) discusses the ethics of intellectual property and the issue of ownership of any value that has been added in the course of doing business. Some would say that intellectual property issues are no different than those in the public or private sectors, and others cite the values base of the community sector as evidence of why the common good trumps business principles; therefore, intellectual property should be freely shared.

Well known website TED (Technology Entertainment and Design), which regularly features topical video commentary online, hosted TED Global 2013, as part of which two key business professors from Harvard debated the place of the market in solving social problems (Porter & Sandel, 2013). They each have differing views – Sandel believes we need to keep the market in its place, and Porter that we should use markets to solve social problems. Interestingly in the debate, there was agreement between them on the need for more public debate on the place of markets. In addition, despite scepticism about the ability of markets to solve social problems, Sandel was very open to finding ways for markets to do so - if there could be a focus on multiple outcomes which didn’t create further social problems.

Porter & Kramer (2011) discuss the economic theories which have held precedence over the last few generations, and point out how these have created the view that any involvement in resolving social or community issues will have a detrimental affect on economic success. They identify Corporate Social Responsibility (CSR) as a response by businesses to public pressure for them to be seen to be adding value, but see that as somehow separate from, rather than integrated with, their core outcomes. Until recently, most businesses have seen social and community needs as falling outside their scope. Porter & Kramer propose instead the notion of Creating Shared Value (CSV) as an alternative to CSR, and as a model that will improve business and social outcomes.

Given that most if not all organisations in the community sector are strongly influenced, if not driven, by their values, it is not surprising that the notion of incorporating business strategies or values into community organisations is seen as problematic by some and anathema to others. This is largely due to the sometimes implicit, sometimes explicit suspicion of business by those in the community sector, and sometimes vice versa. Many hold a position that you have to choose business or community, and the combining of the two creates dilution or corruption.

The issue of profit can be somewhat fraught for the community sector, and often people see the concept of charity as being contradictory to the notion of profit. However, the key to social enterprise is the intention behind generating profit (or surplus), often the way the profit is generated, and the way that the profit is
then distributed. If the intention is to create profit in order to ensure sustainability, and in order to reinvest in the provision of services, this is a very different prospect than generating profit for individual shareholders. Lynch and Walls (2009) ask the question “what if profit were not the point of business but the means by which the point of a better world were achieved?” (p. 5). At a social finance seminar in New Zealand, visiting US Philanthropist Clara Miller said “Not for profit is a tax status not a business model.” (Miller, 2011)

Becoming more enterprising, and developing an enterprising focus, involves becoming more familiar with notions of markets, marketing, sales, and promotion as well as more sophisticated business, investing, and financial tools. As long as the pursuit of profit is a means to a charitable end, is pursued within a range of accepted organisational values, and the bulk of any surpluses are reinvested in charitable purposes, then the charitable status of the organisation is likely to be secure under current New Zealand tax laws (Department of Internal Affairs, 2013b).

Dey (2013, p. 4) comments that “Social entrepreneurship has been criticised for being a neoliberal strategy for social service provision”. Douglas and Grant (2014) note the serious concerns of some practitioners that governments promote social entrepreneurship in order to shift their responsibilities for the social good to the social sector. So, rather than addressing why problems exist, the focus shifts to how to find the resources to address them. This situation itself begs the questions of whether:

- we need to know why problems exist in order to remedy them?
- a social solution is superior to an economic one?
- a hybrid solution might be better again?

Other authors express a range of sometimes contradictory views. Senker (2011) believes that purely generating a surplus is not justification enough for a not for profit to own and run a for profit business. He thinks change and social benefit also need to be created. Alter (2009) has concerns that, if the generation of income happens largely separately to the delivery of social outcomes, it is critical to ensure that the finances generated will be in fact be used for social purpose. Chernega (2007) suggests that there are difficulties for social enterprises when they aim to use the tools of capitalism to solve social problems.

Douglas & Grant (2014) also believe that the promotion of social entrepreneurship by governments is designed to create competition, and the adoption of entrepreneurship by community groups as a necessity to cope with shrinking resources and greater social need. Dey (2013, p. 9) suggests this is designed to have us realise that “the best way forward as a charity manager, social leader, and community activist in the age of austerity is to believe in the ideas of management and business entrepreneurship, that is, to freely endorse them in the conduct of oneself as a responsible subject.” Dey also comments (2013, p. 11) that “social entrepreneurship leads to a subservience of the social to economic rationalities, which in turn marginalise practices and values pertaining to, for instance, solidarity, participation, trust, dialogue and exchange.” This perspective aligns with Collins (2006, p. 1), who says “we must reject the idea – well intentioned but dead wrong, that the primary path to greatness in the social sectors is to become more like a business.”

On the other hand, entrepreneurs and philanthropists like Richard Branson, quoted in The Economist (2012, para 2) are actively exploring how to combine business and social outcomes. His new creed is now
“do good, have fun, and the money will come” rather than the earlier “have fun and the money will come.” Frances (2008, p. 57) comments “Social business is about using market values: identifying a problem, understanding the costs and benefits of both the problem and the solution, and selling the benefits at a greater value than the costs. He goes on to say (2008, pp. 66-67) “The challenge for social entrepreneurs is to deliver the mix of social and other goals they want in a market driven economy. The process will have to be more complex than in a purely for-profit business, or a charity with no imperative to operate profitably.”

Another school of thought has developed in recent years called Conscious Capitalism. It sees itself as a new business philosophy, which draws from the origins of capitalism while also reorienting the fundamental drivers and outcomes of business towards a better society. Mackey and Sisodia (2014), in their book of the same name, discuss the idea of multiple types of wealth, and share examples of businesses they see as more successful than solely profit driven businesses, because they focus on more than just financial wealth.

In the context of this research, and the range of views expressed in the literature about combining business and social outcomes, it is to be anticipated that the data gathered from the primary interview sources are likely to reflect a similarly broad range of views.

2.3.3 Sources of income

As identified in the Introduction, the community sector has some unique challenges in relation to income generation. Unlike a regular business, which is generally user pays, in the community sector those receiving the benefit of the service often cannot or do not pay for it. This creates what can be called a community pays model, in that other third parties cover the cost of the services in some way e.g. through grants, donations, and contracts (see Figure 1). Sometimes, when organisations are searching for how to fund their services, they explore ways that they can sell some aspect of these services to groups who can pay for them, as a way of cross subsidising their core services (Hayssen & Viravaidya, 2001). This carries the risk of diverting the organisation from its core business, particularly if it needs to use existing staff to provide the user pays services.

The traditional sources of income for the community sector have been donations, grants, sponsorship, subscriptions and contracts. More recently there has been exploration of strategies used overseas, such as social lending and social bonds. In general, none of these are fully reliable, and all require significant time, effort and often cost to secure and maintain. Fluctuations in policy, markets, and community values can shift the predictability of any given source of funding. In addition, each type of funding brings with it a range of compliance issues. If a familiar source of funding dries up, this usually provides an impetus to explore alternatives and, if an organisation is being proactive, it may seek new forms of funding before being forced to.

While not usually acknowledged in these terms, a community organisation faces similar issues to a for-profit business where income is concerned. Both need to generate enough income to meet their primary purposes and to ensure their sustainability. How that income is generated, and how it is distributed and to who, become the distinguishing factors.

A potentially risky strategy is to seek contracts that will bring in cashflow (McMorland & Erakovic, 2013), without anticipating the strategic implications of work that may not be fully aligned with the organisation’s
core values and purposes. This is often called mission drift and, unless consciously and intentionally agreed to by the organisation, it can lead to confusion and conflict, as well as creating difficulties with existing funders.

Social enterprise, whether as a way of transforming an existing organisation, starting something new, or adding a venture onto an organisation, usually includes in its goals an ambition to at least break even, if not to generate some level of surplus or profit for sustainability and growth purposes. Any of these approaches requires funding and, while some of the traditional philanthropic funders are exploring the value of social enterprise, few are making this a priority. The 2013 survey of national grantmaking practices in New Zealand (Greatbanks, 2013) indicated that, while funders are becoming more interested in funding operational and multi year costs, they are still not investing significantly in social enterprise.

In contrast there are examples in other countries where central and local governments have invested heavily in social enterprise for scoping, start up, and ongoing costs. In Scotland, £1.5million was made available from 2008 – 2012 by the Scottish government to fund the establishment of new social enterprises (The Scottish Government, 2013). The lack of government funding to date to support the development of social enterprise in New Zealand makes comparison with other countries problematic. The development of this sector overseas has often been closely linked to significant funding from government and/or the philanthropic sector. The lack of this funding currently in New Zealand means there is a need to look at alternative ways to initiate this approach.

One of the issues which often concerns people when they begin to explore alternative ways of achieving their desired social enterprise outcomes is how they will need to structure their endeavours, both from a legal and a tax perspective, particularly in order to protect income. A recent New Zealand report (Department of Internal Affairs, 2013b) has recommended that the currently available legal and tax structures provide enough options for social enterprises in New Zealand to preserve their income for whatever purposes are desired. In general terms, as long as the purposes for any money generated are charitable, then the owning or income generating entity can have charitable tax status.

2.3.4 Importance of diversification

Diversification of income is a commonly accepted practice in any business context, whether it is for-profit or not-for-profit, primarily as a strategy to reduce risk if something were to affect one or more sources of income. However, the range of options in any given context may well be limited by a number of factors, including the philosophical starting points of those in that context. Historically and currently, as touched on in 2.3.2, there are those in the community sector who believe that it is unhelpful or even contradictory to use market based strategies. For those who hold that view, the range of options for income generation are limited to the traditional philanthropic scenarios which are as vulnerable, if not more so, to changes in the market.

Northwest Center in Seattle, Washington is an interesting long term example of an organisation that recognised the challenges brought by traditional funding practices, and decided early in its history to diversify and aim for significant independent income. In an article written about their journey, the first CEO Jim McClurg (Veljee, 2009) is quoted as saying “Typical non-profit executives find themselves consumed by fundraising to keep the doors open. That can be very distracting and demoralizing.” (p. 23) He goes on to
say “The transformation of an organization can take a long time, especially when it involves a complete cultural reformation and a shift in perspective.” (p. 23). The author notes, in relation to Northwest starting up a range of social enterprises, that “most Board and staff members still saw earned revenue as no more than an adjunct to fundraising. Only a handful of people pictured it as the future of the organization.” By 2007, this organisation operated 16 social enterprises, providing employment for 350 people with disabilities. The sales generated of $35.3 million represented more than 99 per cent of the organisation’s cash receipts.

2.4 Diversification alternatives

In general terms, the key options for diversifying the income of a community organisation beyond the traditional philanthropic sources involve some variation of:

- Public sector contracts
- Social firms or supported employment
- Partnership with for-profit organisations
- Business start ups
- Business acquisition

While each of these have some aspects in common, this section will explore some of the differences in turn.

It seems important at this point to clarify the use of the word business. The Concise Oxford Dictionary defines business variously as trade, definite purpose, buying and selling, engaged in commerce (Fowler & Fowler, 1964). Business occurs in both the private and the social sectors, and describes the transactions between the relevant parties. Most commonly in a private enterprise business, the transactions are relatively straightforward between those providing the product or service and those who purchase that — usually termed customers. Any profits are distributed to the eligible stakeholders. In a social enterprise business, the relationships are more complex.

The Department of Internal Affairs, in its report on sustainability, explores the issues of values and methods of achieving one kind of sustainability (e.g. financial) at the expense of another (e.g. environmental). (Department of Internal Affairs, 2011) They note that factors such as empowerment, community development, and consistency with community and cultural values are important. They also note that a paradigm shift is required to bring about innovation and creativity. They suggest that larger organisations may be better placed to leverage off their current resources in order to create alternative income sources. However, this can bring the disadvantage that the diversity of the sector can be lost, as only larger organisations may survive. This report points to the issues of scale, organisational size, and existing resources, and how these factors may influence the effectiveness of social enterprise.

There is another section of the New Zealand economy which uses a range of business tools, including acquisitions, to meet a variety of blended outcomes including profit and social, namely the Māori economy. Nana (2012) outlines that there were $36.9 billion of assets in the Māori economy in 2010. This economy includes Māori entities, as well as businesses owned by Māori employers, and businesses of self-employed
Māori. He points out that having an asset base is only part of the picture; improving the performance of, and the income from, that asset base is crucial too.

Much of this asset and business base has been generated and grown as a result of Treaty of Waitangi settlements. However Maori have been entrepreneurs and traders for much of their history, so it can be argued that the growth of the Maori economy in recent decades sits on the shoulders of a significant heritage. Many tribes such as Ngai Tahu (Te Runanga o Ngai Tahu, 2015) had specialist areas of trade for hundreds of years prior to colonisation. For Ngai Tahu that was pounamu (greenstone), and then post colonisation they had significant involvement in the whaling and agriculture industries.

Each iwi currently has its own way of investing its assets. For most this involves a diversified portfolio of commercial investments, often based around land and natural resources. For Ngai Tahu this includes investment in fisheries and aquaculture. For Ngapuhi their investment includes commercial property and fishing (Ngapuhi - Te Runanga A Iwi O Ngapuhi, 2015). Some of Ngapuhi’s recent investments have clearly had combined social and financial goals such as the acquisitions of a service station and a book shop, both of which provide employment and training opportunities for the local communities.

Tainui is another tribe which has had an intentional and active policy of investment and acquisition. In their case this has centred around property investment (Tainui Group, 2015). They have built and acquired significant land holdings, including several large hotels. Like some of Ngapuhi’s acquisitions, Tainui’s hotels are not only commercially successful, they also provide a training ground for iwi members.

Not all iwi investments have gone so well. Ngati Tama made a series of investments which failed (Anthony, 2012) losing most of their Treaty settlement. Their investments took the form of shares in an eclectic and wide range of companies. There were a range of factors which seemed to contribute to this outcome, including limited governance oversight, unmanaged conflicts of interest, and poor investment decisions.

Each iwi continues to make a variety of business decisions to maximise the benefit from those settlements. Some of those decisions have included acquisitions, although at a significantly larger scale than most social enterprises are likely to be able to aspire to. Additional investigation into this area, beyond the scope of this work, may well establish some principles that may be transferable to the wider social enterprise sector.

2.4.1 Public sector contracts

Given that most community organisations focus on some aspect of social good, and that the public sector is usually charged with meeting social outcomes also, it is common for the public sector to contract out a range of services to community organisations. There generally needs to be a degree of capacity and capability in those organisations for this to occur (McMorland & Erakovic, 2013). In section 2.3.1, the author adopted the understanding that public sector contracts are a form of trading.

Public sector contracts are often the lifeblood of many medium to large community organisations. They can be a mixed blessing: while they can provide steady funding for one or more years, they are rarely guaranteed, are usually compliance heavy, and often do not fully fund the work contracted at a rate that allows for realistic infrastructure and development costs. Over time, organisations can find that the work
they want to do, or believe will bring about the most change, is not always the same as what the funder will pay for.

As mentioned in 2.3.3, there is a risk of mission drift if organisations seek contracts primarily for the income they will bring in, if the work is not closely enough aligned with their core values. On the occasions when a contract is clearly defined, well funded, has realistic compliance requirements, and is designed well, then it can be a great asset to an organisation and its community. If not, then in the author’s experience it can absorb resources out of all proportion to what it contributes.

2.4.2 Social firms and supported employment

Within the broad social enterprise field there are a range of models. At a seminar run by ASB Community Trust and Philanthropy New Zealand (ASB Community Trust, 2012), Kevin Robbie talked about the concept of “enterprising charities” which use a blended approach to strategies for income generation, including direct sales and contracts for service delivery with government and others.

One significant model within the social enterprise field which does this is the area of Social Firms (UK term) or Affirmative Businesses (USA term). Social firms (Social Firms Europe CEFEC, 2013) are specialist types of social enterprise that seek to employ people who are otherwise disadvantaged in the regular labour market. This model generally needs high levels of subsidies to be sustainable, and tends to steer the nature of the business in the direction of those which use unskilled or semi-skilled labour. Robbie and Hutton (2007) identified that successful examples of social firms from Europe and the UK were very much dependent on the level of external subsidy available to support the additional needs of vulnerable employees, and noted the huge challenge of achieving both social and financial outcomes. Some social enterprises purchase or create specific businesses for this purpose, and a study in Scotland explored this option (Social Firms Scotland, 2012). Generally, a higher level of staffing and resources are needed to support the employees, and this has an impact on the ability to generate a surplus.

Hughes (2012) and (Community Wealth Ventures, 2010) have identified the most common business or mission areas in which social enterprises operate in Scotland and the US respectively. There is significant overlap between these surveys, and both lists suggest the approach is primarily that of social firms. Kerlin (2006) compares the US and Europe, and identifies that the US context focuses more on income generation as a key outcome in itself. Some of these models do not derive the same tax benefits that the New Zealand context currently provides.

So, while social firms are recognised as an important and useful social enterprise model to create employment and meet social outcomes, they may not necessarily generate surplus income for reinvestment, as well as for long term sustainability and growth. The key focus of this research is on acquiring and running a profit generating business to create income that can be used for social purposes. This will also allow reflection on the need to hold in tension the extent to which it will exercise socially responsible policies, systems and processes in the operation of that business.
2.4.3 Partnership with for-profit organisations

Historically, many for-profit organisations have had a relationship with and/or supported one or more community endeavours. Sometimes this is driven by a personal interest of a staff member or owner; other times it is part of an organisation’s commitment to Corporate Social Responsibility (CSR). It may take the form of cash, sponsorship, mentoring or volunteering. The usefulness of these relationships depends on a range of factors, and this approach largely falls into the charitable framework.

Inspiring Communities (2012) notes that the various sectors of government, community, and private business all contribute important and different elements, and by working together more effectively each can improve their outcomes. In the business sector, this approach has been termed Creating Shared Value (CSV) and recognises the need for a useful synergy or partnership between business and community. It incorporates the notion of multiple bottom lines in a for-profit business, and identifies that this will result in a more sustainable and profitable business when it seeks to meet outcomes beyond solely that of profit (Porter & Kramer, 2011).

It is worth noting that the balance of power in both CSR and CSV still largely lies with the for-profit business. Even if a community organisation seeks a relationship with a for-profit organisation, the type and level of support and the nature of the relationship is ultimately in the hands of the for-profit group. As models and examples of CSV evolve with a more expressed partnership intention than CSR, it will be interesting to observe if this balance of power changes. In the meantime, it remains an unpredictable source of income for community groups.

2.4.4 Business start-up or business acquisition?

The remaining strategy that social enterprises typically consider when seeking to find additional income is to initiate something new. This can be by way of a start up or an acquisition. There are considerably more examples of social enterprise start ups than of acquisitions, possibly due to the lower capital investment required, and the potential of using some degree of voluntary labour. The majority of the examples of acquisitions are of those organisations which have purchased a business in order to change it into a social firm.

In the case of a “start-up” business, where an organisation either develops some of their existing expertise for additional markets, or chooses to develop a new idea that may enable them to generate extra income, there is significant variation in the figures quoted for their success or failure rate. It is not uncommon to read data such as “according to Statistics New Zealand, an analysis of business start-ups recorded in 2001 showed only 34% were still operating in 2009” (Triegaardt, 2010, p. 1). Because of the high rates of failure often quoted for start-ups, and the usually low risk tolerance and limited leeway of social enterprises to sustain potential losses, this research focuses on acquisition rather than start up. It seeks to identify if acquisitions are a viable strategy alongside start ups, or other strategies, and what might need to happen to ensure this is so.

Robbie & Hutton (2007) have a particular focus on the strategy of acquisitions to create social firms, and comment that one “key area of development is the need to fast track social firm start-up. Buying existing businesses and transforming them into social firms is one way of being able to grow the social firm sector,
and support more people who are currently excluded from the labour market to experience the benefits of working” (p. 3).

Bearing in mind some of the points raised in 2.4.2, in considering ways to ensure the financial sustainability of social enterprises, one significant question is whether it is possible or helpful to have an aspect of the work that can focus largely or solely on income generation as a means to providing some financial resources to achieve social outcomes. Rather than trying to manage the tension of meeting both social and financial outcomes from all activities, it may in fact be more straightforward to separate out the means of achieving each set of outcomes, and to not expect each aspect of the social enterprise business to meet blended outcomes.

In recent years a New Zealand initiative was created entitled Acquisitions 4 Good, which sought to assess if community organisations were ready and able to undertake a business acquisition, and to mentor them through this process. This initiative appears to have disappeared, or at least gone dormant, and no current references have been found. Without further information, if is difficult to surmise why this might be so.

Of the few examples of social enterprises acquiring businesses the author could find, Grant & Kinley (2010) write about a New Zealand example of a business acquisition by a small social enterprise. They document the progress of national network Jigsaw, from an NGO towards becoming a social enterprise. Pertinent to this case study is how they purchased the franchise rights to a product with symbols and values aligned to Jigsaw’s core values. Later enquiry indicates that this venture has not developed as anticipated, and further investigation proved difficult due to a turnover of staff.

Whyte (2009) refers to the example of a large community transport company operating as a social enterprise in England, which purchased other associated businesses in the late 1990s to early 2000s. While this led to an initial leap in scale, it also meant being over-extended, which quickly led to a drop in profits. Factors such as a lack of appropriate governance skills, inappropriate financial models, and not focussing on core purpose led to the sale of two major acquisitions by 2008 in order to survive.

Hayssen & Viravaidya (2001) outline examples from Bangladesh and Thailand, and conclude that commercial business development by an NGO is a long term strategy that works well if it is started small, grows gradually, utilises existing staff skills, and is aligned with the NGO’s purpose. They also cite examples from Romania, Brazil, and Namibia which illustrate NGOs marketing some of their services to a user pays demographic to cross subsidise those who can’t pay. They also note that it is unlikely to succeed if the business activity is in contradiction with the NGO’s purpose, e.g. an alcohol or gambling outlet. They raise the issue of culture clash between the for profit and not for profit activities of the NGO, and suggest that this may lead to setting up different structures to mitigate potential conflict.

Jennings (2012a) has reviewed a social enterprise technology start up in the Waikato, which failed. The report is a useful summary of the factors which went well, along with what contributed to its failure. There are also recommendations on how to avoid a similar outcome in future. There was a significant range of factors including a values clash, issues with management and leadership, finance issues, as well as growth that was too sudden and unsustainable. This mirrors the example from Whyte (2009).
The closest model found to the focus of this research is a three year pilot project in Scotland that was completed in late 2012 (Anderson, 2012). This project, Acquiring Business 4 Good, aimed to support organisations to purchase businesses that could be converted to Social Firms and thus become vehicles for employment of vulnerable people. One of the key findings from the Scottish project is that the component of due diligence, both pre and post purchase, is critical to ensure the on-going sustainability of the acquired business. It is not clear whether the nature of this due diligence needs to vary at all, between regular acquisitions and those undertaken by a social enterprise, and this is explored further in the data collection phase of this research.

2.5 Key components of acquisition

2.5.1 Investment readiness

It is unlikely that any social enterprises who might decide to undertake a business acquisition would be immediately ready to do so. Therefore, some process of becoming investment ready would be needed prior to enacting this strategy. This research seeks to identify what the elements of investment readiness might be. While the steps might vary by organisation, they would include having access to appropriate funding; having in place governance structures, policies and people who could plan, implement and oversee this strategy; having the management skills and personnel to ensure the acquisition runs optimally; and being able to undertake the relevant due diligence on any given acquisition to ensure it meets the criteria sought (Snow, 2011).

Few social enterprises are likely to have significant amounts of capital readily available to undertake a business acquisition at short notice. Generally, an organisation would need significant assets or the ability to borrow up front before undertaking an acquisition. The exception might be if a funder was willing to provide a loan or a grant for the purchase. The degree of readiness might vary with the size and nature of the organisation, of the acquisition, and the existing resources available.

2.5.2 Governance, structure, policy and strategy

The majority of community organisations in New Zealand are structured as charitable trusts or incorporated societies. Both have governance structures which commonly involve a voluntary board that seldom meets more often than monthly. Well functioning boards take responsibility to set strategic direction and policy, usually in conjunction with the CEO and staff (McMorland & Erakovic, 2013). The process of change is often slow, due to the need to engage multiple stakeholders in decision making and the limited levels of delegated authority. The process of acquisition, while ideally undertaken with care, can require quick, informed decisions by people possessing a range of business skills. Boards of community organisations often lack these skills, and their structures do not allow for rapid change.

One option is to establish a separate board with the relevant skills to purchase and govern the acquisition. This raises a number of questions in terms of to what extent and how will the owning entity retain control of its asset, what accountability and reporting mechanisms will be in place, and to what extent will the values of the owning entity be expected to be evident in the work of the acquisition?
Once the acquisition has taken place, the owning entity needs to be clear how decisions will be made in the business and by whom. Sufficient delegated authority needs to be given to those responsible for the day to day management, while still ensuring that strategic decisions are made by those responsible for them. Clarity over roles and authority is critical.

The business world is well used to creating appropriate legal and tax structures to facilitate the nature of the business undertaken. Some community organisations in New Zealand have experimented with structures other than trusts or incorporated societies. The most common other option is the formation of a limited liability company to operate as a separate profit generating entity. A recent New Zealand report into legal structures for social enterprises (Department of Internal Affairs, 2013b) suggests there is currently no need to develop new structures, as the existing ones allow enough flexibility. At present, any business that is owned by an organisation with charitable status, and that returns its profits for charitable purposes, can itself have charitable tax status.

2.5.3 Management, tactics, and skills

One of the reasons cited for the failure of acquisitions by social enterprises in the few examples found to date is inappropriate management. The temptation can be to either use existing management resources in the acquisition, or to minimise the management allocation to save costs. Even if the core businesses of the owning entity and the acquisition are closely aligned, the nature of the business models will be different due to the primary orientation of each – one to social outcomes and one to profit. Management strategy will inevitably be different in each.

Anecdotally, on a study leave visit to the UK in 2011, the author heard variations on a consistent message: it is easier to bring a business person who has social values on board to help run a social enterprise, than to try and teach a community worker business skills. While this comment was often made in relation to the scenarios of establishing a social enterprise from scratch, or acquiring a business to run as a Social Firm, it nevertheless underscores the different skill sets required in different types of businesses, and the transferability of some being more practicable than others.

As mentioned in 2.5.2, it is important that there are clear boundaries and roles between management and governance in regards to authority, autonomy and decision making. While this is true of any organisation, it is particularly true when mixing business models and philosophy.

2.5.4 Due diligence

This phase of the acquisition process has been well documented in a large body of literature, and the author’s view prior to undertaking the interview stage of the research was that the due diligence phase undertaken by a community organisation would be very similar to that for an acquisition by a commercial business. A typical due diligence process would likely involve an extensive checklist of steps. A summary adapted from Snow (2011) identifies the following headings:

1. Company information
2. Operations
3. Finances
4. Sales and marketing
Each one of these steps will have multiple sub headings, some of which will be essential for all business
types, and others which will be particular to different business types. Identifying the steps needed for each
acquisition will be essential early in the process, to ensure a fair and robust due diligence process takes
place. The research sets out to establish if these steps are the same when a community organisation seeks
to acquire a business, and whether there are any additional steps that may also be required.

2.6 The research question

2.6.1 What do we already know?

In considering where to focus this research, it has been important to identify what appears to be known,
accepted or not in dispute. We know that the community sector in New Zealand is a significant part of the
economy (Sanders et al., 2008); that income sources for that work are finite and often unpredictable
(Lewis-West, 2015); and that there is no shortage of social issues that need attention (Dale, O’Brien, & St
John, 2014). We also know that there are some social issues that appear to be somewhat intractable, such
as poverty, as well as some which might be termed more straightforward, such as caring for people with a
disability. Both issues need funding to address them; however, the more intractable the issue, the more
creativity and probably funding will be needed. The intractable issues are complex, and the term “wicked
problems” was coined in the 1970s (Rittel & Webber, 1973) to describe issues like this which are difficult
and often resistant to solve. This does not stop people attempting to do so. We know that people are
creative, and continually seek for new ways to address dilemmas, particularly complex ones (Hutchinson &
NZ Social Entrepreneur Fellowship, 2011). In recent years, social enterprise as a discipline and a practice
has begun to take shape, as an attempt to both address complex issues and to find new ways to fund
responses to those (Goldstein, Hazy, & Silberstang, 2009).

We know that people are developing hybrid models (Prahalad, 2009) to combine the best of business with
the needs and contribution of those affected by wicked problems. However we also know that many social
enterprise models often struggle financially when blending social and financial goals (Social Enterprise UK,
2013b). It is also clear that parts of the community sector continue to hold a degree of scepticism or
mistrust of business or capitalism.
This research recognises the backdrop of an ongoing reduction in existing funding sources. It seeks to explore a potential alternative way to fund both regular, everyday needs, as well as wicked problems that are not yet solved.

### 2.6.2 Where are the knowledge gaps?

Social enterprise as a model seems to appeal to many people, either because it puts the heart into business activities and/or it puts a business approach into heart activities. Social enterprises emerge as a response to meeting a range of needs, or as a response to what are perceived to be gaps in society. Behind these usually more localised needs and gaps, there are a range of related issues which we haven’t yet solved e.g.

- How to deal with wicked problems e.g. poverty, family violence, terrorism, etc.?
- How to ensure a fair distribution of resources to enable all people to enjoy an acceptable, safe and healthy standard of living?
- How to fund a broad based social net and, within that, how to fully and sustainably fund the work of essential community organisations?
- How to fund creative delivery of social change unencumbered by unworkable levels of funder compliance?

New solutions require innovation. Tapsell and Woods (2009) discuss how innovation happens when there are new combinations of existing resources. In the particular scenario they discuss, innovation happened when traditional leadership that provided stability and wisdom (which they call heritage), was combined with youthful risk taking and enthusiasm (which they call opportunity). This research seeks to explore whether it is possible to also combine existing resources and skills in a different way.

### 2.6.3 What is the research question?

While there are many interesting and worthwhile angles that could be researched here, this particular piece of research focuses specifically on the issue of income generation to fund social change. This in turn is narrowed down to the strategy of business acquisition as a tool to generate independent income, which in turn would allow social enterprises to pursue their core business of social change and community good.

The specific research questions that are explored have sought to identify the skills and factors involved. In particular:

1. What conditions need to be in place for a social enterprise to acquire an existing for-profit business?
2. To what extent is it necessary for an acquired business to have aligned purposes, values or outcomes to those of the social enterprise?
3. What conditions need to be in place for a social enterprise to successfully run an acquired business long term, and to ensure its on-going profitability and sustainability?
2.7 Conclusion

This cross section of literature illustrates that there is useful material available on topics related to aspects of business acquisition for social enterprises. This sample of literature also identifies some of the potentially contradictory views that exist in the cross over space between profit-seeking business and social outcomes. Further chapters of this thesis have set out to uncover and/or develop clarity in terms of how this approach to business acquisition for social enterprises is useful, and what will make it successful.
Chapter three – Methodology

3.1 Introduction

The literature review in the previous chapter has identified that, while there is a significant range of associated research and resource material related to the separate realms of business acquisition and of the community sector, there is very little that has looked at either the theory or the practice of a linkage between them. This chapter explains the methodology that was used in this research to explore the potential offered by this approach, and then goes on to outline the process used for recruiting participants, and the data collection and analysis methods used. It concludes with an exploration of the ethical issues that are relevant, and some comments on the possible limitations of this research.

3.2 Methodological Approach

There are potential complexities and inherent contradictions when working in a field of research that incorporates both business and social world views. For some, this complexity includes apparent paradoxes, such as how to combine social outcomes with social justice, while also focusing on doing business and making a profit.

The author’s goal was to identify insights, tools and results that will have practical application in developing sustainability for community organisations. Given that the literature review found few working examples of the business acquisition approach being considered in this research, the research process sought to explore connected and related experiences and examples. This led naturally to a qualitative approach, to enable a narrative exploration with participants who had this related experience, and who were then able to explore those ideas and extrapolate from these.

Initially the methodology of grounded theory was explored, because there were few specific examples identified related to the research topic. However, further exploration led to ruling this approach out, on the basis that the starting point for this research was not a true blank canvas. This research steps away from dualism and accepts that any sustainable activity requires some profit or surplus to reinvest – for maintenance, for growth, and for innovation. While this is not a universally accepted position by all in the community sector, it has been treated as a given for the purposes of this research. The need to have surpluses for sustainability implicitly blends business tools with social outcomes. This research seeks to explore this blending more explicitly.

A constructivist paradigm was therefore chosen to reflect the subjective nature of the topic area, and to acknowledge that there is unlikely to be one single answer or perspective in this area of enquiry. Constructivism concerns the making of meaning (Krauss, 2005) and the identification of the world view, philosophy and perception of the participants. As an approach, it holds that all reality is socially constructed and takes cognisance of the complex web of relationships inherent in each context. Given the potentially varied perspectives that were likely to exist in the range of participants in this research, using constructivism as an approach supported an analysis of those dynamics, and an exploration of the relevance of how those perspectives would impact on existing and potential structures.
The constructivist paradigm, and the need to explore the topic in partnership with participants, led in turn to the choice of semi-structured in-depth interviews as the method of data collection.

3.3 Recruitment and data collection

3.3.1 Interview design

In developing the interview questions, the author reviewed a range of examples from other research which used similar methodology, as well as reflecting on her own experiences of being an interviewee and what had been helpful. Consideration was given to structuring the flow of the questions from the broad to the specific, while also building initial rapport. The questions were designed to be open ended, in order to allow the participants to expand and add as much of their own insights and experiences as they wished. The questions also needed to ensure the key research outcomes identified in Chapter 1 were met. The guideline set of questions is included in Appendix 1.

The same base set of questions was used as the framework for each interview, although additional probing questions were asked as each interview unfolded. As the schedule of interviews proceeded, these additional questions reflected the uniqueness of each setting, and served to supplement the questions initially devised. The questions developed for the interviews included some designed to listen for contributing factors and values which inform the choices the organisation had made or was planning to make. During the interviews, there was a conscious choice to listen for any factors that were unique to any organisation.

The initial questions were developed as a guide, while allowing the interviewees space to narrate their story (Community Sustainability Engagement: Evaluation Toolbox, 2010). Using rapport building strategies, active listening, and open ended questions, the participants were asked to begin by describing their context and their general experience. Then an exploration followed of their experiences and views on business acquisition. Towards the end of the interview, participants were asked questions which led them to evaluate and predict in relation to the topic, including suggesting potential solutions.

Most of the interviews were conducted face to face at a location suitable to the interviewee. Consideration was given to finding a quiet place with no interruptions, and this was often the interviewee’s or the interviewer’s office. In one case the interview took place via Skype due to the distant location of the interviewee. Most interviews were close to one hour long, and each was recorded in full, and then transcribed within a short time to enable an initial check to be done while the interview was relatively fresh. Only one of the interviewees chose to view a copy of the transcript, and they did not request any changes.

3.3.2 Sample selection

Because limited examples had been identified of the actual strategy being investigated, it was important to intentionally choose participants who could reflect on aspects of this study from personal experience. Recruitment of participants in qualitative research, especially when the sample size is small, creates issues of how to ensure diversity and avoid bias. The use of purposive sampling involves the choice of participants by the researcher in order to seek diversity and to ensure a wide range of views is captured. In turn, it risks
reflecting conscious or unconscious biases of the researcher. Barbour (2001) suggests that the key to avoiding bias and homogeneity with purposive sampling is to not only seek to choose a diverse sample, but to also ensure that the methods of comparison and analysis purposively explore the data. The exploration of the views of “outliers”, and the careful analysis of differences, provides rich data from a range of angles. Stating the views and biases of the researcher, and exploring how these interact with and influence the data interpretation, also mitigate against bias.

Participants were sought who were chief executives or senior managers of community organisations, or were involved in support or mentoring of community organisations, and who:

1. Had some prior knowledge of, or interest in, business acquisition.
2. Had an interest in and/or were pursuing an acquisition strategy.
3. Had tried the approach of acquisitions within social enterprises, or given it serious consideration either as purchasers or as funders of an acquisition.

A range of methods were used to recruit participants:

1. Personal networks of the researcher.
2. Recommendations from colleagues.
3. People/organisations identified during the literature review and an internet search.

Primarily, the methodology determined the sample size i.e. a qualitative, constructivist approach seeking in depth narrative data based both on peoples’ experiences as well as on their own theories about what would work. In-depth interviews were conducted with eleven individuals from eleven separate contexts. Only one person declined to be involved due to work commitments; however, this person still expressed a genuine interest in the research. A broad variety of views and experiences were sought, and no inducements were offered to participants to take part, nor was any provision made for refund of participant expenses. Ten of the participants were from New Zealand and one was from overseas. Three of the New Zealand participants were from out of Auckland, but were all able to include time for the interviews as part of a scheduled work visit to Auckland. All participants were provided with the requisite paperwork prior to the interviews, and each knew what the nature of the interview was and that it would be recorded (see Appendix 2).

The author believes that, because there is a significant amount of entrepreneurship in the Māori economy, including some with the aim of meeting social needs, there are additional and potentially unique research opportunities beyond the scope of this research, especially in those iwi and organisations which are resourced by Treaty settlements. The scale of entrepreneurial activity, including acquisition, occurring in some iwi organisations also raised questions as to whether any principles identified would be transferable to smaller contexts, and those larger organisations proved difficult to access.

Two of the research participants were Māori; both from place-based local organisations. One was from an organisation that identified itself as tikanga Māori, and one from an organisation that was more mainstream, while still embodying tikanga principles. In neither case did the participants identify any unique principles that would apply to business acquisition other than the embodiment of cultural values.
One non-Māori participant reflected on an example of an acquisition considered and discounted by an iwi they were connected to, due to a values clash. This is discussed further in the findings section.

3.4 Data analysis

Qualitative research invariably includes explanation and exploration of the contribution and impact of the researcher on each aspect of the research (Johnson & Onwuegbuzie, 2004). There is a need to be aware of the researcher’s own beliefs, starting points, behaviours and biases. The greater the level of awareness, and ability to analyse any impact this may have on the research process and outcomes, the greater validity the research will have (Barbour, 2001).

The author is the Chief Executive of a medium sized community organisation in New Zealand that, like many other organisations, faces sustainability challenges. An ongoing shortage of resources to extend the organisation, as well as a desire to explore innovative practice, led the author to the current research. A saying attributed to both Winston Churchill and Ernest Rutherford is “we have run out of money: now we have to think.” Shortages of money can also lead people to make hurried decisions without all the relevant facts, and this is an issue the researcher is mindful of. While aiming to stay open to the outcomes the research presented, the author was also aware of some hopes that the research process would provide validation of the approach being researched. Again, by remaining aware of this, the author was able to identify and avoid influencing the findings, and in fact the outcomes of the research were somewhat different than the author expected. The author intentionally chose not to use the organisation she is employed by, in order to remain as impartial as possible and to avoid any potential conflicts of interest.

As each interview was completed, it was transcribed in order to begin analysing and organising the data. This involved elements of thematic analysis using the general inductive approach (Thomas, 2003). Thomas identifies a number of steps involved in data analysis:

1. Multiple readings of the data in the light of the research objectives.
2. Coding of data, which includes making decisions about what is included and excluded.
3. Categories developed from the raw data that then lead to identifying key themes.

The identification of patterns, meanings and themes then led to the development of a set of guiding principles. Each participant was interviewed only once, and it was not necessary to seek further clarification post interview for any participant.

Consideration was given to methods of cross checking the transcripts and the data analysis. While sometimes research participants are invited to do this either individually or in focus groups, given the busy nature of the roles of the participants it was felt that including this in the research process would likely reduce the willingness of people to participate, and therefore the sample size. The research supervisors provided a cross checking of the data analysis, and participants were given the opportunity to review their transcripts if they wished – only one chose to do so.
3.5 Ethical issues

This particular research was relatively straightforward from an ethical standpoint, as the subjects of the research were not seen as vulnerable from most perspectives, and there were limited if any power imbalances between researcher and participants. The exception to this was in terms of confidentiality and commercial sensitivity. Confidentiality was addressed in the participant agreement and this is included as Appendix 3.

The identity of participants and the organisations they worked for was concealed, as was any information that may have been seen as commercially sensitive by either party. Participants were able to view the transcript of their interview if they wished, and to withdraw from the research within a reasonable timeframe. No participants withdrew. Although eight of the eleven participants were known in some way to the author prior to the research, this prior knowledge did not result in any changes to the way that data were collected.

While this research did not follow Kaupapa Māori research principles, two of the participants were Māori. In each case, the interviews took place in locations determined by those participants. Neither of the Maori participants identified any specific cultural issues related to the research questions; however, one of the non-Maori participants attributed investment decisions he had observed in a Maori organisation to Kaupapa Maori values.

In relation to the ownership of the intellectual property of this research, this remains with the author. However, there are a number of stakeholders who will have an interest in the process and outcomes of the research e.g. the author’s employer, participants, Unitec, and the provider of a study grant received towards this research through the Anglican Church. In order to avoid any potential conflicts of interest, none of the people interviewed had a material connection with any of these stakeholders other than the participants themselves. The research and any subsequent reports based on it will be freely available to anyone who is interested.

3.6 Conclusion

The process of exploring this research topic, through the literature search and the previous experience of the writer, identified that there were limited examples of the strategy to be researched. This could stem from a variety of scenarios, including that the strategy is relatively new and untried, that the strategy is unworkable and has been left untried due to insurmountable factors, or that where the strategy has been tried it has been described or framed in different terms and language than that chosen in this research.

The research sample of eleven inevitably means that there are limitations in the ability to generalise from the data. Nevertheless, the process of analysing in depth the experiences and opinions of those interviewed has provided a range of insights into the validity and applicability of the strategy being researched. While there was variation in the views, opinions and experiences of the participants regarding business acquisition, a clear picture emerged once all the data were analysed and compared.
Chapter four – Results

4.1 Introduction

The starting point for identifying and exploring the findings from the interview phase of this research was the original three research questions:

1. What conditions need to be in place for a social enterprise to acquire an existing for-profit business?
2. To what extent is it necessary for an acquired business to have aligned purposes, values or outcomes to those of the social enterprise?
3. What conditions need to be in place for a social enterprise to successfully run an acquired business long term, and to ensure its on-going profitability and sustainability?

An overlay to this was provided by the more detailed questions which were used with participants (Appendix 1). These questions had been designed to move from the more general to the more specific. What happened in practice was that most participants tended to do this by following a logical progression in their interview, from idea to exploration, to more detailed consideration, to decision.

In deciding on the most helpful way to present the findings, the author has chosen to follow this pattern. In particular, this chapter is based around the stages of due diligence which the participants described they had followed, or would expect to follow, if they pursued the strategy of business acquisition.

4.2 Due diligence – the “getting ready” stage

All of the research participants named and reflected on a range of factors which they thought would be relevant, or would need to be considered, prior to a business acquisition being undertaken, and in some cases prior to even considering this as a strategy. These factors were often considered concurrently, and together contributed to an assessment of investment readiness for an organisation.

4.2.1 Current context and environmental conditions

The environmental conditions that an organisation must contend with, in both external and internal contexts, were identified as central to the need or motivation to consider business acquisition. As might be expected, the nature and types of income sources available to organisations were strong contributing factors to how open or motivated organisations were to look outside their current frame of reference, and seven of the participants commented in some detail about this. While having a range of income sources was identified as being a desirable thing, participants spoke about currently having limited income options, which made them vulnerable to changes in those sources of income.

The Global Financial Crisis (GFC) was mentioned by one, and several others noted that there had been a general tightening of income from their usual sources in recent years. In most cases, those sources were contracts, grants and donations. The organisations with government or council contracts were increasingly finding that those were compliance heavy. The funding often did not cover the full cost of providing the
contracted service, which led to seeking top-up funding from charitable sources. In addition, the parameters which funders put around contracts often meant organisations struggled to meet contract outcomes as specified, or to meet the actual needs of their customers where these were different from what was contracted.

The external contracting, grant making, and procurement environment was mentioned often, with six of the participants referring to overseas contexts where there were seen to be conditions that were more favourable to the development and sustainability of social enterprises. In particular, the Scottish and English contexts were mentioned by several. In those contexts, there have been multiple examples of significant grants being made available to community organisations for feasibility studies, research, and set-up costs, which led to increased income and greater sustainability for those groups. However, the participant who came from this context indicated that there were few of these grants available at present. The other New Zealand based participants were only aware of limited sources of grant income that were available for social enterprise scoping and start up, and none for the purpose of business acquisition.

The nature of the community sector in New Zealand was mentioned by two participants in some detail. They noted that there was not the level of organisation or lobbying for policy and procurement change which has come about in some countries overseas, and which they believed was necessary to bring about change here. The inclusion of local benefit clauses in procurement policy, together with allowing contracts to be apportioned in sizes which social enterprises could manage, were seen by two participants as important steps in growing the capacity of the community sector. They believed that more opportunities for business development and acquisition for social enterprises would be available if procurement policies changed. Provision of contracts which included provision for all the costs involved was also seen by them as desirable.

One of the participants talked at length about the progress many faith based organisations had made in diversifying income sources, even though they did not come from a faith based organisation themselves. They made mention of the resources and assets that many faith based groups had gathered over many years, and how those groups had sought ways to maximise the returns from, and leverage off, those resources for community benefit. This participant noted the irony that faith based groups may often have views which seem anti-business; however, they have still been pro-active in earning income from their resources. Often the initial motivation has been to maximise the use of their premises for the benefit of the community, which in turn has led to the generation of income.

The same participant noted that, in some ways, this mirrors the ambivalence or division that exists in the community sector over the need for strategies which can generate income. Often groups are more open to a financial mission if they see it as a means to meet a social mission. For example, the Living Wage movement was noted as a development which may cause a tension for groups who want to maximise surpluses to reinvest in social aims, and where these surpluses could be diminished or eliminated if a Living Wage was paid.

Even with the focus of this research and the interviews clearly explained, it was interesting that some participants initially grouped start-ups with acquisitions as the same or similar strategies, and sometimes assumed the purpose of an acquisition would automatically be to provide employment for at risk people, as in the Social Firm example. Seven of the participants in some way noted that they had previously, or were
now considering, ways to make money from what they already did – “I think groups are looking for what parts of current service provision, or what intellectual property an organisation may have, with a view to trying to monetise that somehow”.

The heavy workload and stress levels of chief executives and senior managers in the current environment was noted by eight of the participants. The increasing complexity of the funding and contracting context, together with a growing desperation as to how to keep providing services with shrinking resources, were seen as key elements of this. One participant commented that “certainly senior people are racking their brains for options”, and another noted some recent closures of organisations, and was of the view that sometimes closure was inevitable or necessary. This pressure was seen as a motivating force to look at new and alternative sources of income – “I think that there has to be the threat of the organisation ending to propel them to think seriously about other options”.

All eleven participants had either explored the concept of business acquisition for community organisations, or were interested in doing so, with seven having actual experience of some aspect of this. The strategy of purposive sampling was intentionally used in order to identify research participants who did have this experience. Nevertheless, the participants’ actual experience of the value of business acquisition was varied, with several sounding notes of caution. This is explored further in the following chapter.

4.2.2 Governance

Governance of organisations, both of a parent organisation and of any potential acquisition, was the most talked about issue by the research participants, and it was the factor which was most likely to be seen as a make or break issue. The challenges in finding and retaining appropriate Board members, to match the purposes and strategies of each organisation, were significant. Because Boards are responsible for developing and maintaining the mission of organisations, and are the ones to sign off on major decisions, their contribution is critical. The aspects of governance that were seen as important by participants in the preparation phase for investment are covered in this section, and those that relate to the decision and maintenance phases of investment are covered under 4.3.2 and 4.4.

The importance of having a clear direction, as articulated through elements such as the vision, mission and strategic plan of the organisation, was spoken of directly by eight participants and indirectly by all, with one talking about the need for “good frameworks or guidelines”. When clarifying the importance of direction, several mentioned that there would inevitably be a tension between social and business aims, and the relative weighting given to each would need defining. “How social do I want this business to be?” was how one person put it.

Every participant spoke about the skills and expertise that Boards would need, especially if they were going to consider the strategy of business acquisition. Finding those people was seen as another matter. “We’ve had a look at our skills gaps and are very focussed on the type of person that we’re looking for” said one, and “what we want is their expertise and their contacts and business acumen” was how another phrased it. Another was clear that “the right professionals are people who ‘get’ you socially but are real corporate professionals”.

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Most Boards of community organisations are voluntary, which can make it more difficult to find Board members with the range of skills needed to explore new directions, especially for business acquisition. The importance of the “business acumen of the people doing the purchasing” was how one put it. Another said it was critical for Boards to aim for diversity of skills, as well as of age, gender, ethnicity and experience. Acquiring businesses and looking for innovative ways to increase revenue requires an entrepreneurial approach that two participants thought was often at odds with the traditionally conservative nature of Boards of community organisations. “How you bring that entrepreneurial attitude in is hard I think” was how one saw it. The motivation to increase social benefit was what some thought often allowed Boards to see financial return as a valid means to an end, but could also compromise their ability to achieve that return.

If business acquisition is chosen as a strategy by a Board, then three participants thought it was important to ensure that the Board also had access to skills that were relevant to the nature of the business chosen. Another thought that it would be important to either have someone on the Board who understands the acquisition, or for there to be someone who comes with the business who can assist the Board to understand it.

The role of the CEO and senior management, including how they relate to the Board, was raised by four participants. As mentioned previously, because most community Boards are voluntary and can struggle with a shortage of skills, this was recognised as having an impact on the CEO’s workload. It often took a long time to build the kind of Board who could consider and make appropriate decisions on new strategies and, more often than not, the role of the CEO was seen as essential, and central to any change. Usually the CEO was the key driver of this process and had to walk a careful line in taking the Board on a journey of training and “gentle education”, especially given that the Board was their employer. The quality of the relationship between the CEO and the Board was important, along with a high level of trust. It was usually the CEO who realised “we have to find a smarter way to deal with it” and who also had to come up with “a compelling business case that can address all of their fears”, and sometimes engage in some “myth busting” to support the need for change.

The limitations in many Boards were acknowledged, with one participant who was not a CEO saying that organisations are “generally run by a quality of people who sometimes don’t have around them the boards or senior staff that they can rely upon”, and one who was a CEO saying “when I look at the Board’s profile, I’ve got to be mindful that there are people there who probably won’t know much about what I’m talking about”. This pressure on CEOs extended to their support systems, with several commenting on how isolated the CEO often is - “I don’t really have a senior management team” and “it’s just that there’s only one of me and when you’ve got a multitude of contracts it’s hard to find time to pursue new ideas”. One senior manager who was responsible for business development even commented that “every once in a while, to be honest, I need a lie down though because it’s a lot”.

There were a range of motivations expressed for community organisations considering business acquisition as a strategy. For nine of the participants, the primary motivation was financial, including a “tightening of cashflow”, wanting “more control over your income stream”, and “not getting a very good return on their reserves”. The contextual factors mentioned in 4.2.1 often left Boards feeling like they had no other choice but to consider new strategies, while at the same time feeling out of their depth. A degree of naivety and inertia was seen to exist in the sector, with only two participants having examples of organisations who
were pro-actively seeking new ways to generate income without having to face a crisis to create motivation.

Once Boards started to contemplate business acquisition as a strategy, the issue of risk quickly came to the forefront. "Being really confident that their strategies to minimise or mitigate those risks are understood and acceptable" was important to one. Another raised the issue of "what are going to be the ‘gotchas’ for them as a group?" – in other words the non-negotiables or the expectations which would trip them up. Several mentioned that it was important that Boards are able to cope with loss and failure, without putting the parent organisation at risk, and also need to ask themselves “what will make us lose?”.

Two participants noted that Boards are often driven by the interests, views and biases of individual Board members, with decision making prone to being emotive and subjective without necessarily having all the relevant facts. “You can’t over-state the need to understand the personal goals and aspirations of each of the board members” was how one put it. Boards’ “attitude to money” was also an integral part of the process, and having some awareness and clarity around this was seen to be important.

While some saw new income as essential in order to be able to undertake new work, one person spoke of the inevitable infrastructure costs needed in running organisations, which are often under-resourced through traditional funding sources and under-estimated by organisations. That person called this “the hungry caterpillar which at the end of the day needs to be fed”. Once again it pointed to Boards needing to think through their motivation for seeking additional income, and what that income would be used for.

The speed at which Boards were able to move was seen as a critical factor by five participants. Many Boards meet monthly, and the question was asked “is the organisation able to move quickly enough to grab a bargain – the bad outcome would be that you’re only able to buy things that are sitting round on the shelf because that’s the speed you can operate at”. Once again the tension was raised between the traditional social focus of many Boards of community organisations, and the business focus that was needed to actively pursue income generation. One person quoted in relation to this “an African proverb that says if we want to go fast, we go alone; if we want to go far, we go together”. Several additional factors that would assist speedy decision making were noted, such as being well organised and having accurate, timely financial reporting.

4.2.3 Business approach

Factors such as these are only some of the components of being investment ready, and being able to embark with confidence on a strategy such as business acquisition. Most participants saw that the need for operating community organisations in a business-like manner was so self-evident it was difficult to encourage them to elaborate. Two initially interpreted the question on the relevance of business skills as being only related to owning a commercial business. Clarification substituting the term “business-like” quickly saw them identify similar factors or practices as other participants. One participant used the analogy of the well-honed processes and principles that the All Blacks have used to remain successful over time.

The participant who had the most experience with business acquisition in the community sector was, unsurprisingly, the most specific in articulating the components they saw as important to being
businesslike. For this participant, as well as others, many of the factors they raised had to do with aspects of financial management such as managing cash flow, understanding a balance sheet, and tracking sales, costs, and profits. Having up to date information on a day to day basis was mentioned by several, and one said it was important to know “what’s going to force you to make certain decisions”, while another used the analogy of keeping track of things as you would with your household budget. One was as direct as to say “the reason for going into a business is to generate a profit, no matter how the funds are going to be used”, and another discussed how any business has to be able to run competitively in the marketplace.

The particularities of running a community organisation were noted by five of the participants, with a range of perspectives expressed. One of the participants noted that, if Boards have members from a corporate or business background, they often “do not actually understand the challenges of running a community organisation”. On the other hand, two others noted that there was more in common between a commercial business and an NGO than people might think, including many of the basics such as staffing, payroll, rent and tax, while another said that “the skills needed to do good business are probably not too dissimilar from the skills needed to run a really good NGO”. The skill that many community groups have in managing people was seen as a particular advantage by one, with another simplifying good business right down to excellent customer service, and another identifying government contracting as having played a significant role in developing business capacity in community groups.

The issue of scale and capacity was mentioned by, or was a factor for, three participants. They acknowledged that having some existing capacity and resources would be important in order to be able to look at the business acquisition strategy, with one hazarding a guess that they thought a threshold of $3 million annual turnover might be a useful starting point. Two also noted that, in smaller organisations, the CEO and sometimes the senior managers had to cover multiple functions that wouldn’t be the case in a larger organisation – “rather than having an HR department and a sales department and a finance department, you’ve got people playing multiple roles”. In organisations which have been focussed on community issues, one participant noted that it was uncommon for those staff to have business skills, and buying those in if the Board did not have them was costly.

4.2.4 Financial factors

The matter of finances came up consistently, and therefore warrants a separate section. Factors such as financial readiness, investment readiness, and ROI (return on investment) were mentioned often. One participant summed it up when they said “It’s money. It’s always money. They say it’s not everything, but try doing anything without it.”

The need to have a good understanding of the financial factors involved in the strategy of business acquisition was discussed by all the participants, and interestingly those with least experience in investment spent more time discussing these issues. One acknowledged that it is “quite a complex set of metrics to know how to make money”. There were different aspects to this discussion - expectations for returns, where will the money come from and whose money will we use, and how will we balance risk and return, were the most common. One noted the intention to increase income needs to be part of the strategic plan of an organisation. Another participant, interestingly from the largest organisation, raised the question of whether community organisations (including their own) could move from their traditional
budgeting mind-set (where every cent is accounted for and loss not well tolerated), to an investment mind-set where some swings and roundabouts were accepted and some allocation made for investment costs.

The ROI was referred to directly by seven participants. Some had actual figures in mind of what they would expect to get, e.g. 10%, 14% and 20% were named. One thought a ROI of 5% might be acceptable if it “creates wealth and it creates jobs and creates goods and services”. Others began from the point of view of wanting to improve the ROI they were currently getting, usually from having money invested in the bank. Several said they really had no idea of how to understand ROI, and would need to do more homework, and one noted that since the GFC peoples’ expectations for ROI needed to be lowered to what could actually be achieved – “we have to be more realistic and have the ability to make a profit at today’s rate”.

Several other factors related to ROI were mentioned. One of the participants raised the question of what outcome the organisation wanted in dollar terms – were they wanting to generate $10,000 or $100,000? This in itself could determine the nature of the investment as much as the ROI. Another phrased the issue of returns as “if the business is not profitable to pay back a loan, then why are they buying it?”.

The timing of returns was important to some, with one saying “we’re not throwing money at businesses that we have to wait 5-6 years to start getting a return on”. One example was given of a community organisation that was intending to invest in a business primarily to improve their financial outcomes, and then made their final decision based on values. They turned down an opportunity to invest in a franchise business with a ROI of 14-16%, for the purchase of a working farm with a ROI of 1%. They discovered they were somewhat uncomfortable about the business type, and instead decided they would rather have land for their stakeholders, which turned out to be a stronger motivator than money. Another participant noted that they would expect to pay staff more than minimum wages and this would have to be figured into the ROI.

Only two participants were part of organisations that would have enough cash to acquire a business without seeking additional finance. One that didn’t have these reserves said about the strategy of business acquisition “I think it’s great if you’ve got the capital. That seems to be it in a nutshell for me.” Others all noted that capital to buy a business would need to come from elsewhere than reserves – generally a loan or a grant. As mentioned in 4.2.1, grant finance for business acquisition in New Zealand was unknown; however, two thought that it might be possible to look at involving other investors or stakeholders to contribute some of the investment capital. One of those noted that it would be wise to choose partners with a track record and access to cash.

Another scenario is to borrow against an existing asset, most likely property owned by the purchasing organisation. One recognised it was important to balance debt owed against an existing asset and debt owed against a business, and cautioned not to “fall into the trap of gearing this place up so that when that replacement cycle comes along you’ve still got residual debt on the business and you have to borrow again to replace your fixed assets.”

When it came to talking about borrowing in order to invest, one said “there are two kinds of debt; there’s good debt and bad debt – if the bottom line is showing a good return on investment, that’s OK”. Three of the participants referred to leveraging off existing assets as a possible source of investment capital, with one noting that assets are often held by a parent or associated organisation, and the community
organisation may have to negotiate to have access to use the asset for investment purposes. This might mean the parent organisation would need to underwrite the investment or act as guarantor. They were not confident that parent organisations would be willing to share or relinquish control of their assets for this purpose.

The attitude of the purchasing organisation to debt was mentioned in some detail by one. They saw it as important for an organisation to have a good understanding of what they wanted their balance sheet to look like, and what their tolerance to debt was, including when they expected to pay that off. “You could argue that debt is fine if debt is offset by assets; the two nett each other out” was how they phrased it. One commented that “if you’re having to go into debt to buy the business, then that just means the business has to be a bit more profitable”.

Many participants made the link between risk and return, with all accepting that, generally, the higher the risk the higher the potential return; or reversing that, the higher the return the greater the risk, including the risk of losing the capital invested. Various aspects of risk were mentioned, including the overall financial literacy of the parent organisation, and whether the day to day financial management and monitoring of the acquired business would be handled by the parent organisation or the business. The importance of managing margins was raised by one, and another spoke of the importance of working out, before the acquisition occurs, if cashflow will cover debt repayment.

The criteria the lenders would impose, as well as the accessibility of loan capital, were raised by five participants with one asking “can you actually get sufficient low-cost capital to make the thing work?”. As mentioned in 4.2.2, the need for good governance was seen as critical to this strategy, and it was noted by one that lenders may not be willing to lend to groups that did not have strong enough governance for the proposed acquisition to succeed.

The issue of financial failure was mentioned by two participants, with one saying “you’ve got to be prepared to say, well we might actually lose this” and another noting that “NGOs don’t have the capacity to replace lost funds from bad risk decisions”. And amongst the many financial issues that needed to be managed, in the “complex metrics” noted above, was the issue raised by one of ensuring there was not just enough capital to buy a business, but also enough working capital to run it. The example was given of ensuring there was enough capital or income to employ a manager if that was needed.

4.2.5 Acquisition criteria

All of the participants considered it a given that there would be a process of due diligence prior to purchasing a business, and this is described in more detail in 4.3.1. However, even before considering any specific businesses, it was clear that participants expected there would be a process of identifying the criteria that would be used to go about selecting possible businesses to undertake due diligence on, and those factors are described here.

The extent to which an acquired business might have a mission, vision or values aligned to the owning organisation was prompted by a specific question, and covered in some detail by most participants. Some made the distinction between values and aims, and others used these terms interchangeably. One participant provided a useful comment on the nature of community organisations as they consider particular acquisitions. They noted that it may be difficult to get fully aligned aims and objectives between
an acquisition and the community sector, because if that was possible “people would be doing it on a commercial basis and they wouldn’t be having to scramble for grant making”. Their view was that an acquisition needed to be “at least neutral in terms of your mission” and if “you can put a positive spin on it” then that was a bonus.

Opinion from other participants was divided between those who thought it was important to have aligned values, and those who thought it was not a key factor. Six of the participants were very clear that at least the mission, values and ethics needed to be aligned, with one posing a question in the negative by way of clarification “can a co-operative gun running group be considered a social enterprise?”, and another pointing out “they can’t be in conflict”. One was very clear that, when identifying what type of business to purchase, it was important to “start with your mission statement . . . it should naturally fit with who we are as an organisation”. Another, when pondering the issue, wondered how much the word social needed to apply to the acquired business?

Two participants saw that having aligned mission, values, ethics as “allowing you to leverage off the relationship”, while suggesting that this would make it possible to link the branding of the parent and acquired organisations. However, another was not sure if having the business owned by a community organisation would be a motivating factor at all in others choosing to do business with it. The physical location of the business was seen by another as a possible factor in the ability to drive off the brand.

For those who were not so concerned about aligned mission and values, one commented: “at the end of the day I’m trying to make money for charitable purposes. I’m not going to do anything illegal though”. Another said each organisation has to work out its own views on philanthropy, which they saw as a leadership issue. They saw receipt of the profits from a business as akin to receipt of funds from other philanthropic sources – the community organisation needed to determine the boundaries or limits on sources from which they were willing to receive financial support. Another asked “are we trying to reform the industry, or are we trying to earn some money here?” and used the term “moral exposure, or maybe its reputational risk” as a question when considering acquisitions.

One compared it to the limits some investors put on where they want their funds invested, choosing for example not to invest in the production of weapons or alcohol, while another gave an example of an organisation considering purchasing a fast food franchise. While it would have achieved a good financial return, and provided employment opportunities for some of the clients of the parent group, in the end the values clash for a group whose members had a focus on dealing with obesity proved non-negotiable.

One said it was important, if there were different aims, to split those aims into different business interests of the organisation and not try to blend them. Another wanted to follow the Social Firm model of acquiring a business in order to create a vehicle for employing clients. In this case, because those clients had few employment skills and little employment experience, they would be looking for businesses that provided entry level jobs, while also looking for an opportunity to upskill those staff. In this scenario, the participant saw the acquired business as an extension of the parent organisation, and therefore it would have the same values and objectives.

In this process of considering where to look for an acquisition, several thought it was important to use the right professional advisors at the right time, with one noting “they have a sixth sense – they know when a deal is not a good one”, and another noting that having access to a good accountant who can analyse the
figures was essential. Having access to the right people also extended to both the Board of the community organisation (see 4.2.2), and also to the acquired business itself. It was seen by one as critical to find the right people who fit the business in terms of values and skills, and who want to work there - “firstly you get the right people on the bus; then you make sure they’re in the right seats”.

Participants spoke of the existing staff who might come with the business, or need to be found, in order to make sure the acquisition was successful. If an owner/operator type business was considered, then much of the intellectual property and customer base was vested in them, and clarification would be needed as to whether that then came with the business. Two participants spoke of the importance of recognising in those scenarios that the success of the acquisition may be largely dependent on being able to negotiate a long handover, or to keep the previous owner on the staff in some capacity. However, the cost of paying more to a manager than the business owner may have been drawing from the business was also seen as a factor to consider.

The role of assets in the consideration of an acquisition was mentioned by four participants. Assets were seen as including land and buildings, as well as equipment. One suggested that it was important to look for assets which won’t cost a lot to maintain but will appreciate in value; another pointed out that many assets will depreciate, and the ones that may have appreciated in value in the past may not any longer, or not at the same rate. One saw assets that could be bought as part of the business as giving the opportunity to leverage off them for future growth of revenue. One cited a trust in England that was happy to buy almost anything as long as it came with land, regardless of the condition of the buildings. Another described this same process as “asset stripping”, and cited an example of an entrepreneur who had “bought undervalued assets, sold off aspects of those, and then sold the remaining company at a profit”.

Financial factors were also discussed as part of the process of deciding what kind of acquisition to look for. In addition to those mentioned in 4.2.4, several participants had more specific financial criteria they would apply when narrowing down the options for a purchase. One key factor was the nature of the business and how that impacted on its financial management. Two participants thought it was important to look for businesses that were largely cash based, and therefore would not require a process of chasing debtors for several months. Another thought that it was better to steer away from businesses which required a high degree of capital investment.

Looking for businesses that were very profitable was a priority, with three participants spending time on this factor. It was seen by them as critical to be sure a business really was profitable and, if so, why then was it for sale. It may be because the owner had too much cash tied up in the business and wanted to release that to invest in other ways. It was seen as important to determine if there was enough profit to be made to warrant tying up the purchasing organisation’s resources in the venture, or if it was better to put those resources in the bank like the business owner may be going to. However, if a business was not profitable, it may be possible to purchase it at a discounted price. In this case it was important to identify if it could be made profitable, or if the right people could be found to do this.

The location of a potential acquisition was raised by one who thought if it had a physical address, then being close to the parent organisation was probably desirable in terms of monitoring. Factors such as the future prospects in an area, housing growth, zoning, council plans, and projected business growth in the area may all provide “signs that the area is going to take off”.

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A variety of other financial factors were raised by individual participants. One was aware of the need to be willing to work with the market and let it determine the outcome of the business. Another wondered if there was an opportunity to maximise returns from the business e.g. operating it over seven days if it had previously run over five. One suggested including a turnover guarantee in the purchase price, with a sale price adjustment if this was not reached. They saw this as a strategy to ensure the vendor fairly represented the value and potential of the business. Another talked about checking what kinds of businesses have a viable future, and was not relying on processes, products or technology that were likely to become obsolete quickly e.g. video stores.

Knowing in advance, from both a values and a financial viewpoint, what level of wages you would expect or need to pay was seen to be relevant. The owning organisation might find itself in the situation of wanting to pay wages which the acquisition couldn’t afford. One participant raised the issue of working in partnership with other organisations in order to make a joint purchase, and although they emphasised the importance of relationships in doing business, they then made the comment that “I’m not really good at partnerships to be honest”.

One participant spoke at length about the option of franchises. They described those which are well established, have good profit margins, good support systems, and don’t take huge overhead margins, as having good potential for community owners. However, they suggested that the opposite of these criteria – new concepts, low or unproven profit margins, little ongoing support, and/or high overhead payments – should be avoided.

Four participants spoke about the scenario of looking for an owner operated business where the owner wished to sell, and family members did not want to take over the business. The owner might want to release some equity for other purposes, or to leave the business entirely. A range of potential options were raised, from outright sale, to shared equity, to the owner staying on in the business as employee or manager in order to maintain continuity with the intellectual property and customer relationships. One noted that many baby boomers have a fixed skill set that they have spent a lifetime developing and, while happy to keep working in that field, no longer want to have the responsibility of running a business, though their “interest and personal ties and personal relationships” may keep them involved.

Finally, before even beginning to look for an acquisition, it was seen as critical to identify if the purchasing organisation could access and then service a loan. The over-riding issue raised directly by two, and indirectly by the rest, was “where is the capital going to come from?”. The point was made that community groups tend to run on a break even basis, and annual bottom lines often fluctuate. This tends to mean there is little surplus in the balance sheet, and this may not assist them in presenting a case for loan finance.

4.3 Due diligence – the “now we’re looking for a business” stage

Once an organisation has spent time preparing itself strategically and practically for the strategy of business acquisition, and has got some clarity on the parameters for that acquisition, there comes a point when they will either need to start actively looking, or opportunities will present themselves that they will need to respond to.
4.3.1 Due diligence on possible purchases

All but one of the participants had comments to make on the process of due diligence. In most cases, the nature of this due diligence was seen to be the same or similar to that done in a for-profit commercial setting. One described it as the need to undertake a SWOT analysis on potential purchases, with another saying it involved “that magic important ingredient – common sense”. Another noted that, although it was like a typical acquisition in some ways, in other ways it was not because of the type of organisation doing the acquisition. They thought that, because it was a relatively new strategy with few clearly known examples, this might put groups off trying it; once there was data from some examples – both successes and failures – they thought more groups would be willing to consider it. One described this as “swanning around in the dark a bit, hoping we’ll walk into the light switch”. One participant noted an inherent tension between following your intuition and instincts, while also relying on concrete evidence. They also noted that, while the vendor might be trusted, it is also important to know who they deal with in their supply and distribution chains, as they might not warrant the same trust.

The issue of who would do the due diligence was raised by four participants. One, from a large, well resourced, membership-based organisation, expected that they would find most if not all of the skills for due diligence within their own organisation. Others noted they would need to access those skills from outside their organisations. Another commented that trust is such a strong value for community organisations and that, together with their innate risk aversion, this meant they ideally need people to help with the due diligence who will stay close to the purchasing organisation during and after the acquisition. One of the participants thought it was critical that someone involved in the due diligence “understands that business’ processes extremely well”.

Specific components

A range of financial factors were covered by participants. One participant, who had experience with due diligence processes, raised a number of key components that they would ensure were part of the due diligence phase. Initially they would conduct a “light touch” one which they saw as including primarily financial factors:

- Management information
- Accounts, current and back 3-5 years
- Monthly cash flows for the last year
- Forecasts
- Tax returns including PAYE and GST
- Legal contracts
- Staff contracts including wages and Kiwisaver obligations
- Existing equity in the business

If it looked promising then they would explore other elements in more depth. Another who had also been involved in due diligence processes always insisted on a confidentiality agreement, commenting that “it’s really important to be on the same page with each other and what we say to the outside world”.
Value/cost/financial issues

The process of arriving at a mutually acceptable sale price was seen as complex and critical by four participants. One said “people over-sell their business in my experience”. Another actively avoided discussing the value of the acquisition early on. They felt it was important for each party to do their due diligence on the other before laying their cards on the table with price. A range of factors were mentioned as having an influence on price, such as business location, type and level of any valuations, and any valuation rules of thumb which either party might hold or want to adhere to. The value of goodwill was mentioned by one, and they noted that it can be very difficult to agree on a value for this.

Two people commented on the cost of due diligence, including the cost of the fees for due diligence. They noted that some professionals who work in this field have fixed fees, some are percentage based, and some are willing to negotiate as things proceed. They pointed out it was important to know which system was being used up front, as the cost differential could be significant.

One was interested in using a “turnover guarantee” in the sale and purchase agreement, especially in situations when there would be involvement of a previous owner so they were “actually committed to making the thing work”. Another option raised was to ask the vendor to leave some money in the business, and tie this to maintaining returns, or to consider having a 10 year buy-in clause where the purchase price would be paid over that period. If before then the business wasn’t going well, or the owning organisation needed to withdraw for any reason, then it could be possible to find another partner, and the owner may not have lost all their investment. There would also be an advantage for the vendor, in that profits or returns would be shared over this time.

Several commented on the need to be aware of how the balance sheet will look, with the combination of debtors, creditors, stock, assets and liabilities, as well as what the cash flow dynamics were. They saw it as important to have a clear idea of whether the business would need to manage for long periods between bursts of income. In terms of assets, two participants raised the issue of checking not just the value of the assets, but also the replacement cycle of those. Being aware of fluctuations in the cost of raw materials or inputs for the business was noted by one participant, as well as the impact that fluctuations in currency might have on the business, particularly if it relied on importing or exporting.

Some acquisitions might have multiple shareholders and not all might be selling their shares. One person saw it as important to identify whether you would inherit any existing shareholders and, if so, would you have any ability to influence the other shareholders, or would everything be predetermined. In a case where the vendor was a sole trader, there was the possibility that there would be no clear split between the owner’s personal and business affairs. If it was a cash-type business, one participant said that sellers “will try and convince you that they take a lot of cash out of the business”; so if the profit isn’t good, they can attribute that to their cash withdrawals, for which there may be no evidence.

Market issues

The current and potential size of the business, and the potential share of the market, were seen as important factors to consider by one participant. The owning organisation needed to identify if growth potential was desirable, and whether that would increase their general management capacity. In terms of
market share, the participant asked “do you want to be a major player in the sector, or do you want to play a small part?”. They thought it was “much easier to be a small player in a big ball park than a big player in a small sector”, which creates too much vulnerability. Scale was mentioned specifically by one participant, who wondered if it would be possible to make enough profit from small businesses, and noted that it may be necessary to run a business at a large scale to achieve usefully sized profits.

The nature of the business being considered was seen as important by seven participants. One pointed out that “you’ve just got to make sure you’re not going to buy a dead horse”, and went on to note the risks around technology based businesses which can become obsolete quickly, or the scenario where “a big corporate is going to come and swoop in on your patch”. The timing in the economic cycle was also noted by one as being a factor to consider, and whether “it’s something that’s going to survive the test of time”.

Another raised the idea of looking for bargains – businesses that were struggling or being sold at a lower cost for some reason. However they also noted that this was a particularly risky strategy, and would be dependent on having access to skills specific to that business, and strong evidence that it was possible to turn the business around. This participant also noted that community organisations might confuse their aims at this stage in the process, and be tempted to purchase businesses which could provide employment for vulnerable people. They identified that, while this was a valid strategy, if the objective was to maximise income this strategy could compromise that aim.

Staff

Four participants thought it was important to pay close attention to the quality of the staff, and the nature of the relationship between the owner/manager and the staff. They believed that, if the staff worked well and were valued by the manager, then they were likely to care about their work, and it became important to try and retain them. However, if the staff did not look like they would fit with the plans of the purchaser, then it was useful to clarify this, and what would happen to these staff through the acquisition process. One said it was important that “you’re not inheriting staff who could hinder you in the future”. Another participant described this in terms of observing the “people behind the business, their reputation, their business skills, their track record”, while another said it could be helpful to “get a secondment or internship into the organisation so you can see how it runs”, or to look at retaining some existing management for a fixed time to assist the transition.

4.3.2 Organisational issues

Board composition

The issue of which group of people would provide the oversight for an acquisition was seen as important by eight of the participants. While all agreed that relevant skills were important for those who had oversight, what was seen as equally important were the reporting and accountability lines between the owning and acquired entities.

Four participants said it was important to make sure that the people on the Board of the owning organisation, and on any potential management or governance group of the acquisition, have the time and expertise to provide good oversight - “we need to have really good people, top quality people”. They saw this as including good financial expertise, and a willingness to put in significant time, often at short notice if
needed. It was also seen as critical by one that, whatever governance structure was in place, “it’s got to be fast moving” in order to be able to respond appropriately to the context. One said there would likely be a need for a development plan, and ongoing training for the Board “to get their heads around what are they seeing, what do they need to be looking out for, what kinds of questions do they need to be asking?”, while another thought that the board or staff would need “some additional capability around innovation or entrepreneurship”.

**Legal structure**

There was a variety of opinion as to whether there needed to be a new stand-alone board created, or if it was better to be a sub-committee of the existing board. The decision about this was largely seen as connected to how much legal separation there needed to be between the entities. All of the participants indicated that an acquired business would need to have some kind of legal structure of its own, connected and accountable to the owning organisation. The importance of keeping the acquisition legally separate from the owning organisation was commented on by one participant when they said “it’s got to stand alone and if it sinks it sinks. You can’t afford to bail it out or to have a charitable organisation pouring money into something that’s not their purpose”. One was clear that the owning organisation might be quite invisible in terms of the business of the acquisition, and that it was the branding and visibility of the acquisition that was critical – “it’s the business that’s acquired that needs to have the brand”. Others could see potential in leveraging off the reputation of the owning organisation to mutually enhance the outcomes for both.

Another wondered about the idea of a partnership model of ownership, where an entrepreneur would buy in as a joint venture, or perhaps someone who would invest as “a pseudo-philanthropic thing on their part”. This participant also wondered about a stand alone model where “you could set up a limited liability company with its charter to return 50% of their profit to the trust as long as they exist, and then you cut the cord”. They also saw the option of creating worker cooperatives to buy the businesses they work in. In this scenario they saw the vendor leaving in 30-40% of the value as equity; and the workers, including possibly a community organisation, paying off their share over time.

One participant who had worked with several iwi organisations commented that the Crown will not disburse Treaty settlements until strong legal and investment structures have been set up, with good governance in place, in order to ensure positive outcomes in maximising the returns from those settlements.

**Staffing**

Someone who had seen several acquisitions first hand said the common element in those that had challenges or had failed was the staffing – “all those that have gone wrong have been because they’ve had the wrong people, or kept the wrong people, or someone’s got upset and done something to hurt the business”. This participant also recommended hiring a business establishment manager for the initial phase of the acquisition, and then reviewing that decision later to see if a different kind of manager was required.

The day to day management of the acquisition was seen as critical, ideally by someone who also wanted to do this for a good cause - “they need to be driven, and employed not just to manage this business but to grow it ...someone that’s really hungry”. Two participants raised the issue of incentivising staff, with one
drawing from experience in saying “it can work well but it does put a lot of pressure on people ... if you’re working in teams, some people can get their reward without putting the effort in, so it becomes a management thing to actually monitor it and administer it. It can cost more to organise than the benefit of it.”

Those who commented on the staffing needed to run an acquisition had a variety of views, with some wanting people who shared the same values as the parent organisation, and others who saw the priority as those with the skills to do the job. One participant described the type of staff needed in the acquisition as “people who carry the same DNA as what our leadership carry” while another noted that “I can’t see it working unless you’ve got everybody on the staff up to par with the marketplace skills”.

4.3.3 Ideas, examples, possibilities

Eight of the participants had a wide range of ideas or examples of potential acquisitions. Some of these ideas were closely linked to the procurement policies used by the local council or government, which often then created opportunities for community organisations to set up or purchase businesses, or to run ventures previously run by statutory agencies such as libraries or community centres.

Both in New Zealand and overseas, a number of business scenarios become more economically viable when there are government or council training or employment allowances available for business owners. This context tends to steer community organisations towards the kind of businesses that can employ “at risk” people, and produces the Social Firm model. The common options which participants mentioned that community organisations often choose in this scenario are catering, recycling, charity shops, gardening, maintenance, and non-specialist assembly and manufacturing. It was noted that often these are low wage businesses that may also rely on volunteers to remain profitable. One participant was considering purchasing a manufacturing company as a means to be able to provide employment and/or apprenticeships.

An option that one participant was exploring in depth was to franchise or license existing intellectual property or expertise, or to purchase this from another organisation. They had seen several examples where a community organisation had gone to a funder with a proposition to run a range of services that had previously been purchased separately. While this scenario may result in a business which may in turn create a profit, it is more likely to be in the nature of a start up rather than an acquisition. Regular franchises though were seen by six participants as a viable and potentially safer option to purchase – “the franchise model probably in many respects is the easier option to go for... the franchise model makes sense”.

Another model outlined by a participant was one of acquiring or providing a service that required contractors to do the work and source their own customers. They saw this as sharing the risk and incentivising the staff to work hard, while keeping costs down. A further idea was to leverage off an organisation’s brand, and set up or purchase aligned businesses that could use that same brand.

One mentioned companies with long standing reputations that were well known for distributing their profits back for community purposes like Carlsberg Brewery in Denmark. Another thought there might be “an uncontested market” in considering companies in receivership where there “might be value to unlock”, although for others acquiring a company in these circumstances might create a clash of values.
The idea of a group of community organisations getting together and collectively purchasing a business, such as a supermarket, was raised. This same participant thought that getting into the field of providing affordable community housing was also a good idea – “one you can keep an eye on it, two it’s tangible, and three the track record suggests you’re unlikely to lose your shirt”.

Another had an example of some rental units their organisation owned which had not been covering their costs due to the values commitment to low rents. They chose to identify a portion of the accommodation which was renovated to a high level and then rented out at market rents. The surplus created by this strategy allowed them to retain lower rents on the other units, as well as to undertake overdue maintenance on them.

One person described a property renovation business they had been part of which was owned by a community organisation. Properties were acquired, renovated, and then sold. It was successful for several years until the property market changed. The board chose to cease the business at that time, whereas the participant would have preferred the board to revert to rental management of the remaining properties until the market turned again.

Continuing the property theme, another participant worked for an organisation with considerable property assets currently used for only one purpose. They were exploring adding other services or income streams to those premises, including the possibility of extending the premises to create more rentable space.

Smaller communities sometimes manage to proceed with an acquisition when it is an essential community service that would be lost to the community unless someone buys it – a bakery, petrol station, local general store or local transport company are common examples. Often this involves jointly raising the money via a lender, or through community shares, and usually results in a cooperative ownership model.

4.4 Now we’ve bought – the “what do we do now” stage?

Although it was the smallest part of the research, all but two of the participants commented on what they have done, or might do, once an acquisition has taken place. The eight participants who had experience with, or were close to doing, an acquisition, all commented that the work does not stop with the acquisition. The common theme was “it’s like any management – you need good leadership, clear objectives and a plan, good processes. All the normal things that go into running a business.”

Continual monitoring and improvement was seen as critical, as was keeping up to date with the relevant industry, markets, networks, and technology. “Having scrutinising, and monitoring very closely gives the business operator a sense of the importance the Board places on this endeavour”, and there would need to be “lots of focus on targets, and accountability, and reporting, until the Board becomes really confident that, yes, we’re on target here”. The Board and management were seen to have an important role in identifying these clear performance measures, which largely were seen to be about the ROI. Factors to be checked were named as sales, staffing, stock, and marketing.

Communication with stakeholders and/or shareholders was seen as important, although one participant thought it was important to decide if it was wise to market the acquired business as being owned by a
community organisation or not. They saw a risk that “if it’s now seen to be owned by a not for profit, people might think the business should be cutting them some slack or doing them a deal”.

The role of staff continued as a strong theme. One thought it was important to take time to win the confidence of the existing staff as “they will be cautious about the new owner ... you’re buying that group of peoples’ ability so you need to take care of them”. Looking after staff well and looking after your product well was “an awfully good start”. Having a really good manager who can get the best out of the staff, “a humble leader who will carry people with them”, and ensuring there was succession planning for key staff were all mentioned. The need to jointly focus on staff and customers was raised by several, with one saying “once you get the right people, everything flows from there” and also “you’ve got to look after your customers all the time”. The issue of incentivising staff, and/or the payment of fair wages, was again raised as an important factor which could influence staff retention, and might also have an impact on the ROI.

And finally the willingness to continue to seize opportunities was seen as crucial to both maintain and grow the acquisition - “you’ve got to be really aggressive at times about motivating yourself to step out of the square, and push yourself to go and do something and initiate”.

4.5 Conclusion

While, understandably, the interviews with the participants followed the line of the research questions, they also largely followed a similar sequence of thinking to each other, and this has been reflected in the structure of the findings. This sequence and the resulting structure follow the three main stages which are summarised below.

The first stage (Table 1) covers the preparatory work that participants believed would need to be done by community organisations for them to be ready to undertake a business acquisition. The second stage (Table 2) covers the process of acquiring a business, while the third stage (Table 3) provides some thoughts on what to do once an acquisition had occurred. Within each stage there were a number of components, and each of those had several issues associated with them.

The following chapter explores the results under each of these stages, and discusses and analyses the results in relation to the questions raised in chapter one.
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</tr>
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</table>
| Current context and environmental conditions | Philosophical issues  
Motivation for acquisition | Income sources  
Availability of existing income  
Availability of new contracts and grants  
Staff workload and stress | Nature of community sector | Stakeholders to consult  
Opportunities for branding synergy  
Type of business willing to consider |
| Governance                    | Composition of boards  
Vision, mission, strategy  
Skills, expertise  
Entrepreneurial approach  
Motivation for acquisition  
Tolerance for risk and failure  
Focus on core business  
Slow to move | Role of management | | |
| Business approach             |                                                                                 | Business-like  
Financial management  
Accurate, current information  
Scale and resources  
Capacity to manage | | |
| Financial factors             | Influence of values on level of debt and ROI e.g. Living Wage | Financial readiness and literacy  
Investment readiness  
Return on investment wanted  
Scale of investment needed  
Timing of returns expected  
Relationship of risk and return  
Repayment vs returns  
Capital to buy and then run a business | Sources of investment capital  
Accessibility of capital  
Lending criteria | Direct or indirect investment  
Security for loans  
% of own money used  
Timeframe for repayment  
Capital gain potential |
| Acquisition criteria          | Extent of aligned values and aims  
Expectations of social outcomes  
Reputational risk  
Appropriate Board for lenders approval | Role of assets  
Role of cash and cashflow  
Staff costs  
Franchises  
Ability to access and service a loan  
Handover and continuity  
Appropriate staff | Use of professional advisors  
Location  
Opportunity for growth  
Owner operated businesses | |
### Table 2 – Due diligence – now we’re looking

<table>
<thead>
<tr>
<th>Components</th>
<th>Governance issues</th>
<th>Management and systems issues</th>
<th>Other issues</th>
<th>Additional issues not directly mentioned by participants</th>
</tr>
</thead>
<tbody>
<tr>
<td>Due diligence on possible purchases</td>
<td>Who will do the due diligence?</td>
<td>Similar to regular business acquisition&lt;br&gt;SWOT analysis&lt;br&gt;Common sense&lt;br&gt;Cost of due diligence&lt;br&gt;Financial assessment and plan&lt;br&gt;Confidentiality&lt;br&gt;Price negotiation&lt;br&gt;Opportunity for growth&lt;br&gt;Longevity of business types&lt;br&gt;Staffing – existing to the acquisition</td>
<td></td>
<td>Timeframe for due diligence&lt;br&gt;Timeframe for handover</td>
</tr>
<tr>
<td></td>
<td>Role of shareholders</td>
<td></td>
<td></td>
<td>In the acquisition:&lt;br&gt;Stage in growth cycle&lt;br&gt;Cost and value of any IP&lt;br&gt;Compliance issues&lt;br&gt;Customer base&lt;br&gt;Strategic relationships&lt;br&gt;Risk issues</td>
</tr>
<tr>
<td>Organisational issues</td>
<td>Who will govern?</td>
<td>Legal structure&lt;br&gt;Ownership model&lt;br&gt;Management&lt;br&gt;Staffing - needed</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Ideas, examples, possibilities</td>
<td>Access to funding subsidies for staff&lt;br&gt;Use of contract staff</td>
<td>License existing skills or knowledge&lt;br&gt;Franchises&lt;br&gt;Companies in receivership&lt;br&gt;Collective ownership&lt;br&gt;Community housing&lt;br&gt;Property management and/or maintenance&lt;br&gt;Purchase an essential community service</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

### Table 3 – Now we’ve bought – what do we do now?

<table>
<thead>
<tr>
<th>Components</th>
<th>Governance issues</th>
<th>Management and systems issues</th>
<th>Other issues</th>
<th>Additional issues not directly mentioned by participants</th>
</tr>
</thead>
<tbody>
<tr>
<td>Running a successful business</td>
<td>Strong governance</td>
<td>Clear objectives and targets&lt;br&gt;Focus on ROI&lt;br&gt;Good processes&lt;br&gt;Maintain product and service&lt;br&gt;Thorough monitoring and accountability&lt;br&gt;Good communication&lt;br&gt;Continual improvement&lt;br&gt;Strong management&lt;br&gt;Support for staff</td>
<td>Look for new opportunities</td>
<td></td>
</tr>
</tbody>
</table>
Chapter five – Discussion

5.1 Introduction

In chapter one, the following questions were identified:

1. What conditions need to be in place for a social enterprise to acquire an existing for-profit business?
2. To what extent is it necessary for an acquired business to have aligned purposes, values or outcomes to those of the social enterprise?
3. What conditions need to be in place for a social enterprise to successfully run an acquired business long term, and to ensure its on-going profitability and sustainability?

Simplistically from the results, the answers to the three questions could be summarised as “many”, “probably”, and again “many”. Whether community organisations are able to meet these thresholds is a further question to be addressed in the final chapter. In this chapter, the results from chapter four are explored in order to shed light on the questions above. While these questions do not correlate neatly with the three stages of business acquisition presented in the results, each of the questions is clearly addressed through this discussion and analysis. When the questions are discussed, they are referred to by short form titles i.e. acquisition conditions, strategic alignment, and operating conditions. The structure of this chapter mirrors the structure of chapter four to facilitate the reader’s comparison of the data. Where relevant, each section also includes recommendations for exploration or implementation of the business acquisition strategy. Because the tables represent a matrix of results with some cross over, any recommendations which could apply to more than one section are grouped together and presented once.

For the purposes of chapters five and six, the term social enterprise is again used to refer to those community organisations who might actively explore the strategy of business acquisition. While many of the factors considered to date may apply to a wide range of groups for whom the more generic term of community organisation might apply or be understood, the more specific term of social enterprise applies to those that are intentionally exploring business acquisition (Social Traders, 2013). It is also worth noting again that, while the term social enterprise as applied to existing organisations is developing some currency in New Zealand, there is still no clear consensus on its meaning. In discussing the business acquisition strategy (even amongst research participants), the use of the term social enterprise can cause unnecessary confusion, so in the wider context the term community organisation (which includes social enterprises) is more generally understood.

5.2 Stage one - due diligence – getting ready

Participants agreed that there are a range of factors which would need to be addressed prior to a social enterprise undertaking a business acquisition. Stage one (“getting ready”) covers those factors which participants considered would need to be dealt with, even before “going shopping”. While each participant emphasised different elements, all recognised that, like Snow (2011), this was not a viable strategy unless significant preparatory work was done.
There were a few elements on which most or all of the participants commented on or agreed, such as the need for competent governance and access to investment income. This consensus may lead to concluding these elements are essential. However, it is possible these elements could have been cited by all participants for a variety of reasons, such as habit, fear, or convention. There were also other elements that were only mentioned by a few participants. While it might be tempting to assume that this means these elements are less important or relevant, there might also be a variety of reasons why this was so, including the nature of the interview process and what it raised for them, their own preferences and biases, or their own experiences.

It was clear from looking at the responses alongside each other, that the many factors involved in considering the strategy of acquisition are closely connected. For instance, the characteristics of Board membership would affect the recruitment and management of the Chief Executive, which would in turn affect the quality of information and ideas brought to the Board for consideration. And similarly, the nature of the funding and contracting environment for social enterprises affects their ability to build up reserves, which in turn affects their ability to access capital to invest. While all the factors are relevant and are influential, two components stand out from participants’ responses as being of vital importance - governance and financial factors. If these are not adequately dealt with, participants agreed that an acquisition would not be able to proceed effectively.

5.2.1 Current context and environmental conditions

This first stage of “getting ready” extends right back to factors within the context of the social enterprise, both internal and external. Participants agreed that often the motivation to embark on a new strategy such as business acquisition is prompted by some kind of crisis, usually a current or pending financial shortfall (McMorland & Erakovic, 2013). Less commonly, organisations will look at this strategy as a means for growth of income or mission, or to increase current funding sources.

Conventionally, social enterprises have a Board of some description, and it is they who are charged, through the governance processes, with determining the direction of the organisation. It is a rare Board that pro-actively seeks to explore new territory unless propelled to; many Boards tend to be conservative and risk averse by nature, and they are also aware of their responsibility for other people’s money. Whatever the stress or crisis which has prompted the need to do things differently, it will by definition put pressure on the Board. This is not the ideal scenario for exploring a complex and time consuming new strategy, and creates the additional likelihood of risky actions. Although participants did not comment directly on the time needed for this strategy, they did all note the many components of due diligence and the time those would take, which by inference makes it clear that this is not a quickly implemented strategy. The main exception to this would be if an organisation was already investment ready. Further discussion of governance issues is presented in 5.2.2.

Because most, if not all, social enterprises are values based and motivated, and these values are usually well embedded in the organisation, they are unlikely to depart from what they may see as their core business - unless their survival depends on it, or they are highly motivated to be creative and/or grow. In turn, a departure from their core business or approach can create significant anxiety within groups who fear they may lose their way, or may be perceived as having done so. They may though be more...
comfortable with the addition of activities beyond their usual core business. The extent to which those additional activities need to have strategic alignment is explored more in 5.2.5.

In order for an organisation to embark on the strategy of business acquisition, they need to be comfortable with the philosophical notion of making a profit. For groups which describe themselves as a Not-for-Profit, this poses a challenge. While they are likely to understand that to survive they need more money coming in than going out, many groups associate profit with commercial business. They in turn see this as the cause of social problems or inequity, and this is particularly true of those with a social justice focus, and those working directly with people who face the consequences of economic inequity.

Those groups who have transitioned to the term social enterprise, or have adopted business-like practices, understand the need for profit to ensure sustainability (i.e. a surplus over and above all core operating costs). Some are more comfortable justifying the pursuit of profit by requiring social outcomes from the acquisition (Senker, 2011); the subsequent issues associated with doing this are explored more in 5.2.5. Others go through a process of change, often precipitated by the motivations of Board members or senior staff, which results in a broader understanding of mission and the means of achieving it. Veljee (2009) suggests that this kind of change in an organisation is transformational, and can take considerable time. Observations by the author, of organisations undergoing a culture and values shift such as would be needed to accommodate business acquisition, suggest this could take 2-5 years.

Internal conditions which might precipitate change can also come from the process of managing the organisation. Most social enterprises have a range of funding sources, and the balancing of those, as well as the time associated with maintaining them, creates significant work and stress for staff. Few groups stand still and, as workload increases, the demand for income increases. It is often staff who prompt and encourage Boards to consider new ideas for income generation, and in turn it is staff who often undertake much of the work of due diligence on behalf of the Board.

The changing nature of the wider context in many parts of the world in recent years was also seen by participants as contributing to the consideration of new models and strategies for income generation. Many governments have reduced the direct funding available to social enterprises through grants and contracts. The criteria and compliance requirements for those grants and contracts have conversely increased, leading groups to look for supplementary or additional sources of income to maintain their level of services, or face reducing services. Other philanthropic funders have also changed or reduced previous funding sources.

The limited nature of cohesive organising and lobbying by the community sector in New Zealand is a factor which participants saw as a negative impact on the ability of organisations to collectively seek change to current funding regimes, as well as to lobby and influence policy. New Zealand groups, including some of the research participants, often wistfully look at the funding and contracting environments in other countries and wish for the same. What is often missing from the discussion on this is any analysis of the differences between other contexts and New Zealand. Two important factors are the relative sizes of other countries, and the procurement, contracting and funding environments they have. New Zealand has a very centralised funding purse, whereas in many other countries the distribution of government funds is done locally, often via local government agencies or funding intermediaries. Much larger countries usually have larger economies of scale in distributing funding, as well as providing much larger markets for potential income earning strategies. However, for those social enterprises from smaller countries that choose income
generation strategies which are not locality based, the presence of the internet and a global market reduces the need to limit options as it might have previously.

Procurement policies in some countries provide more options for social enterprises to pursue new and larger funding contracts, which in turn usually lead to a growth in capacity and capability. Local benefit clauses require those allocating contracts to ensure that a set proportion of the contract is delivered by local providers, and/or that the contract delivers some or all of its benefits to the local economy. The opportunity to tender for contracts, which can be large and provide some long term sustainability, contributes to organisational and community sustainability.

Recent government policy emphasis on community organisations working more collaboratively can prove challenging, alongside what is often experienced as a competitive funding environment. The characteristics of CEOs – their style, workload and stress – came up several times with participants, which is not unexpected given that seven out of eleven of these were CEOs or senior managers. There was a general perception that workloads and stress levels were high; and so expectations from government to collaborate, while understood in theory, were seen in practice as unrealistic or unachievable. How much this is literally the reality and how much it is a factor of being too busy to step aside and think strategically and proactively rather than reactively, bears further investigation.

The author found that CEOs were torn between their passion for their organisations and their need to look after themselves to avoid absolute burnout. It was also noted by one participant that, by nature, they personally found it hard to work with others. It may be that there is something about the personality and style of CEOs that mitigates against collaboration. It might be a function of being so passionate about their cause that they do not wish to risk watering that down by having to accommodate another organisation’s agenda. And it might be that the nature of the job and the funding environment forces competition rather than collaboration.

The particular context of faith based organisations was discussed in detail by one, and three others echoed it in passing. It was noted that many faith based organisations have significant assets which were built up some time ago. While they may have a philosophical discomfort or mistrust of business and profit, they have often developed income earning businesses either as a direct mission goal e.g. used goods stores, or as ways to maximise the use of their facilities by the wider community e.g. room hire. These tend to be low risk and low return ventures. There is room for those groups to explore their own histories in terms of how they came to acquire their assets, and whether the values and practices that built those assets have a place in developing and pursuing their goals today.

While the issue of values may be seen on the surface to be more the preserve of faith based groups than any other, it is in fact a hallmark of community organisations that they have generally been formed to meet a need that someone is passionate about. Those needs are usually ones that the regular market is not meeting or cannot meet, and the founders have chosen a voluntary or not-for-profit mechanism to meet that need. That founding passion with its consequent values is central to each organisation, and it is therefore unlikely they will stray too far from their comfort zone or constituency, even when seeking to explore new strategies for raising income. The issue of how closely any new venture may need to be aligned with the organisation’s mission is explored further in section 5.2.5.
In considering acquisition conditions, it is clear that, in order for a social enterprise to acquire a for-profit business, there will be one or more precipitating factors, either proactive or reactive. Most commonly, the motivation will be some pressure to find new sources of income; less commonly, although more ideally, the motivation will come from a desire to explore new strategies for the benefit of the organisation’s mission.

5.2.2 Governance

Governance, via a Board, comprises the people and processes which determine the overall strategic direction of an organisation and then ensures it is effective. Unlike for-profit SMEs, which rarely have a Board, these are a given for social enterprises of any size. All participants spoke at length and with some energy about the nature and role of Boards, and their potential to be helpful or unhelpful. Factors as diverse as constitutions, recruitment, motivation, skills, biases, time, remuneration, cohesiveness, vision, planning, and risk profile were discussed by participants as having a direct and usually crucial impact on a social enterprise. Feedback from colleagues in the for-profit SME sector indicates that, for them, these factors are usually inherent in the owner and/or manager, and may not always be consciously reflected on. By contrast, social enterprise Boards and senior managers can spend significant amounts of time thinking and talking, before acting. This may well be linked to their responsibility for OPM – other peoples’ money - as well as attempting to meet complex needs and solve complex social issues.

Time then became a major focus for participants, who noted that not only do social enterprise Boards seldom have time to accomplish their task of governance well, but also that it takes significant time to make changes. The time available to Boards was also seen as a factor. Most Boards typically meet monthly for 2-3 hours, which makes it difficult to cover strategic matters in depth unless considerable behind the scenes work is done, usually by the CEO. Often, especially in smaller organisations, Boards are completely voluntary, which in some cases can impact on continuity of attendance, as well as how much Board members invest in preparation and follow up to meetings. While historically most social enterprise Boards have been voluntary, some are now moving to remunerating their Board members, both to acknowledge the time they need to spend, and also to allow them to recruit people with the appropriate skills for the role. Those Boards who have done this indicate that moving to this model has often caused some challenges, and the model is often adopted reluctantly in order to be able to recruit who they need. On the other hand, remunerating Board members, particularly if meetings are held during working hours, tends to predispose membership towards those who are self-employed, retired, and/or those who specialise in governance. Alternatively, fees for board members who undertake board duties during their regular paid hours can be passed on as a source of income for their employer.

The selection and composition of Boards was commented on often by participants. Many Boards are representational, i.e. their members are chosen by stakeholders of the organisation, and to some degree they are expected to represent the views of the stakeholders who chose them. This is in contrast to those Boards who see their members as appointees, chosen for specific skills and perspective, regardless of whether they were chosen by the Board itself or by external stakeholders. Boards with a representative membership can find it difficult to make decisions, especially if there are competing agendas. They often struggle, more than Boards with appointed members, to gather together sufficient skills for their core tasks, as the selection of Board members is less often connected to actual need. These two types of membership selection did not seem to be correlated with organisational size, and the dynamics associated with each had the potential to slow down any size of organisation.
For either type of membership though, there is the challenge of firstly identifying the direction and tasks of the Board, and then recruiting Board members with the skills and experience to undertake those tasks adequately. Boards without the right skills and experience may struggle to undertake the level of strategic planning required. Even when a clear direction is identified, there can be initial resistance from Boards to consider what skills they need, as this may result in some or all of the Board members being no longer suitable. Then, when a Board has identified that it needs different skills, its Constitution may not afford it a mechanism to select those people from its usual constituency. Changing constitutions to achieve a change in Board membership takes more time. This rather circular dynamic can paralyse Boards from making significant changes if needed, or at the very least slow them down considerably.

The Board’s experience, skills, and beliefs about money and risk were seen as critical by participants. The risk profile of Boards was seen as a key factor, not just in terms of money but also of types of activity. Elements of this are covered more in 5.2.5. Typically, Boards were seen to be conservative by nature. They are charged with upholding and maintaining the values and mission of the organisation, so they are understandably cautious about departing from that or putting it at risk. Participants noted it can be hard to find voluntary Board members with professional skills such as legal, accounting, HR, marketing, and business. If a Board was to consider business acquisition as an income generating strategy, they would likely also need some entrepreneurial input. Some participants thought this was best brought in as needed, rather than have entrepreneurs on the Board. By nature, entrepreneurs tend to be frustrated by the slowness and cautiousness of Boards, particularly voluntary Boards that meet monthly and may be risk averse. Using an entrepreneur as a consultant may be a more practical way to access their skills.

When Boards think about how to meet their financial obligations, they tend to think about how to do more of what they are already good at. However, their ability to grow and/or ensure their sustainability may be constrained by factors beyond their control, such as contracting and funding policies. Often, organisations will look to package up services they already have some expertise with, in order to appeal to a different market. Comments from participants indicated that they knew of few successful examples of this scenario. This approach is effectively a start-up, and incurs all the usual challenges those face, along with the reality that, in order to develop a new service to a new market, it may involve taking resources from current services which are already stretched. In recent years, a few philanthropic organisations have begun to make available a limited amount of start-up capital for this kind of strategy. Observation indicates that the bulk of that funding is going to new ideas from individuals likely to start up new organisations, rather than to existing organisations looking to venture in new directions through acquisition.

Participants acknowledged that undertaking a business acquisition would require Boards to make quick decisions at times. They also noted that this was often difficult for social enterprise Boards, especially those that are voluntary. Several participants commented, with some envy, about the autonomy that they thought SME owners and managers had to make decisions and implement them. The other side of this coin is when organisations are under stress or in crisis, and feel the need to make very speedy decisions out of desperation. This type of speed is unlikely to ever have a good outcome. While the research process did not give scope to explore the issue of speed in depth, it does have implications for the ability of social enterprises to undertake acquisitions. As part of the acquisition conditions that an organisation would need to meet, the ability to move quickly and in a considered way when needed is essential. It would serve a social enterprise well to have considered this ahead of time, and identified how it would do this, if and when the need arises.
The role of the CEO, and his/her relationship with the Board, was also a key component of the governance issues discussed by participants. As mentioned earlier, seven of the participants were CEOs or senior managers, so their insights were largely based on their own experience. The circular dynamic of the Board, setting policy and employing the CEO, who in turn advised and guided the Board on policy, was discussed. As previously identified, Boards often struggle with the time and skills required to engage in complex strategic decisions, and tend to rely on the CEO to undertake the research and bring them recommendations. While this is the CEO’s role, and the participants did not disagree with that, they often felt torn between the expressed governance responsibility to support, monitor, and resource the CEO, and the limitations of the Board to fulfil that. This is what may likely lie behind the wistful envy of SME colleagues who do not have Boards.

There were two factors not mentioned by participants which were mentioned in the literature, and seem relevant to providing a full picture of how governance impacts on the conditions which need to be met for an acquisition to proceed. The first is the tolerance of other stakeholders to any new directions the organisation might pursue. Jennings (2012b) identified that a values clash between various stakeholders was a factor in the failure of a start up by a social enterprise. When perceptions between stakeholders are not aligned, a Board needs to identify how far it can stray beyond past expectations, or what process it needs to undertake in order to renegotiate those expectations if it thinks that a new direction is necessary.

The other factor not discussed by participants in relation to the acquisition conditions was the need to consider at an early stage what legal structures might be needed for the parent organisation and the acquired business. Haysen and Viravaidya (2001) cite experience from other countries which suggests that separate legal structures not only protect the various parties legally and perhaps tax wise, they may also serve the purpose of reducing conflict with stakeholders who may be uncomfortable that an acquisition is undertaken too close to the parent organisation. Certainly, getting an expert opinion on whether any change to legal structures is needed would be important early on, and potentially less expensive than unravelling inappropriate structures at a later date.

5.2.3 Business approach

When interviewing participants, the author needed to introduce the term “business-like”, because the word “business” led to an assumption of for-profit activities. The term business-like was also adopted by McMorland and Erakovic (2013), to refer to the increase in skills and strategies needed by community organisations, particularly in the context of managing complex contracts, and also in seeking to diversify and/or increase income sources. When the term business-like was used, participants had to think hard to articulate what that meant in practice, as they all operated in this way as second nature. Some reflected though that, in smaller organisations or in the early stages of their organisations, they would not have done so.

There were different views expressed about how similar or otherwise the task of managing a social enterprise was to managing a for-profit business. Some recognised that the core skills of running a business well were the same regardless of context. In particular, financial management, staffing, and the ability to monitor and measure the work were seen as essential. Those who noted a difference were focussed more on how Board members from a commercial background didn’t always “get” the organisation. However, these two perspectives may not be mutually exclusive, and it is a common issue for organisations to have to
communicate their specific culture to those who have come from a different context. This is different from the question of whether the social enterprise is operating in a business-like way, and it may be as much about translating the way the social enterprise does business into terms the commercial person can recognise. It can also be about ensuring there is an alignment of core values and philosophy between the key stakeholders.

Some identified additional strengths that they could see social enterprises have over for-profit businesses, in particular their expertise in the management of staff, and in having processes to determine strategy and mission from a values based perspective. Others noted that social enterprises often struggled more with issues such as complex management and cost accounting processes.

The capacity and motivation to build business skills was usually seen as linked to the growing complexity of an organisation. This often happened organically and without much conscious intention. Less common is the intentional choice to improve the level of business skills ahead of real or perceived need. Current government funding for capacity building of community organisations is addressing a combination of these situations - both those who need to improve their business skills to match their current activities, and those who want to improve their skills to future proof their organisations. While this funding has been well received, it is not a commonly available resource, and it is more common for social enterprises to have to piece together resources, often slowly, to build this capacity.

It is likely that, just as capacity and capability have grown in a social enterprise as its current activities have grown, so too the addition of a business acquisition has the potential to also improve the capacity of the social enterprise. This potential, or otherwise, would need to be carefully assessed before undertaking the acquisition, and would form part of the due diligence process on specific options. There would be little value in undertaking an acquisition which did not ultimately improve the overall position of the social enterprise. While the expressed goal may be income generation, there may also be additional benefits from growing aspects of the social enterprise’s work, like financial and monitoring expertise.

Scale was raised as an issue here, and also in relation to financial factors. From a business and systems angle, scale was seen as generally providing capacity and capability to manage the complexity of the social enterprise. In smaller organisations of any type, staff need to be more generalists and have a wide brief of responsibilities, which often leaves them feeling stretched and stressed. In larger organisations, there tends to be more specialisation, and the ability to be more thorough in the management of the work. While only one participant offered a potential turnover threshold of $3 million above which they thought the strategy of business acquisition might be workable, there is also the issue of how diverse and complex the activities of the social enterprise are. It seems possible that those organisations with a more narrow focus might have less management and staffing pressures, and so might have proportionately more capacity than a more complex organisation of a similar size. This might be as much of a factor in being able to undertake this strategy as the absolute size of an organisation. The relative access of the organisation to investment capital may also be more of a factor than scale on its own, and this will be discussed more in the next section.
5.2.4 Financial factors

As one participant has already been quoted as saying - “It’s money. It’s always money. They say it’s not everything, but try doing anything without it.” The issue of finances is somewhat of a Catch-22. The lack of money may well be the precipitating factor for considering this strategy, and the lack of money may stop the organisation being able to undertake the necessary preparation and due diligence. Several participants were aware of gaps in the area of their financial knowledge, particularly at the level they assumed they would need to undertake an acquisition. Given their sense of responsibility to guide Boards who often had fewer skills than they did, the pressure was even more acutely felt.

The issue of whose money would or could be used to purchase a business was an early one raised by participants. Only two came from organisations with enough cash reserves to purchase a business outright without needing any additional finance. Only one of those was likely to do that, due to already having a well thought out acquisition strategy that included using cash and loan finance. The other organisation with significant cash reserves, and also significant scale, was limited by their current governance capacity, despite their senior management team being in favour. They were likely to be some time away from being able to competently assess the usefulness of this strategy.

Despite the limitations some participants expressed in their own financial competency, or that of their Boards, they were comfortable with the concepts of ROI and opportunity cost. They were clear that, in order to take money from cash reserves or to borrow from a lender, the return had to be more than leaving it where it was. They were also clear that the end result had to leave the organisation better off from the investment of time and money. Where they were less confident was the complexity of weighing up the financial variables such as expectations, tax, level and timing of returns, scale, overheads etc. Some recognised that they would need expert assistance and, if this did not exist on their Board, then it needed to be found. They knew that this would more than likely incur a cost which also had to be figured into the overall calculations.

There were a range of calculations that participants saw would need to be done at every stage of the journey – before, during and after an acquisition. Again, another circular dynamic emerges here, where an organisation knows it needs additional income but has run out of current skills and strategies to generate this. In order to undertake a new strategy, they may need skills they do not currently have. It is possible that at this point they will find or buy in such expertise as mentioned, or that they may develop this expertise themselves as a by-product of exploring the strategy. The risk with the former option is that they may not find the right advice, or it may be very expensive. The risk with the latter option is that they may not know what their gaps are before it is too late. These are two of the many risks associated with this strategy, all of which have a potential solution, but any one of which could have serious implications for an organisation if not managed well. This reality may in turn require a new kind of organisational leadership.

Several issues to do with the scale of investment were mentioned. In many cases, participants felt they knew what the questions were but did not yet know the answers. The relationship between the level of investment and the level of return was raised. Participants logically knew that an investment of $10,000 was unlikely to match the return from an investment of $100,000. They also knew that there is generally a strong relationship between risk and return, and that a return higher than a bank deposit would require more risk and more work than a bank deposit. The timing of returns was identified by some, who
recognised that, in the early stages of investment, the returns might be lower while the business was stabilised after a change of ownership, and while loan capital was repaid. However, for those who saw this strategy as a potential solution to funding shortfalls, they then recognised that it was potentially a long term strategy that may not bring in any cashflow initially. The question was raised as to whether Boards would be willing and able to take a long term view, or would only want short term gains which were likely to be riskier.

Ironically, Boards and management often assume that taking something they already do well, and building a business around that targeted at a different market, will be less risky than an acquisition. In reality a business that is acquired has already been through and survived the start-up phases. This is to some extent what the purchaser pays for.

How prepared an organisation is to tolerate loss and failure, and the scale of that tolerance, is a key factor. Several participants noted that a social enterprise should only invest that which it could afford to lose and still continue to exist. The exception to this might be a final risk if the only other option was closure. The tolerance for failure was not closely linked to scale. It was more closely tied to both the level of crisis an organisation might be experiencing (again not the best context for undertaking a potentially risky strategy with which they may have little experience), and to the level of skill they could muster to undertake the strategy. Some participants thought the ideal position to be in was where an organisation could put aside an investment fund for new ideas; one they could afford to lose. While ideal, this is unlikely to be an option for all but the larger or most well-endowed organisations.

The influence of values on the process of acquisition was raised several times. While participants could see in theory the option this strategy afforded them for income generation, in some cases they were concerned as to the degree to which they or their Boards would be able to separate out their values from the operation of the acquisition. The issue of wage levels was raised as an example, particularly if the acquired business was one currently paying low wages. The social justice values of organisations would likely cause them to want or feel obligated to pay a fair or Living Wage. This is one obvious example of values, which ideally would be thought through before the strategy was undertaken and, in the case of any financial implications, included in the due diligence calculations. Further discussion on the role of values is provided in the next section.

The sources of loan finance, the eligibility criteria, and the ability to service any loan were well discussed by participants. As has already been noted, it is not common for social enterprises to have enough cash reserves to be able to buy a business outright, especially if the purchase needs to have some degree of scale to be economically viable. While there are a small number of philanthropic funders in New Zealand beginning to look at loans for new initiatives, the issue of lending to buy a business does not appear to have been tested. This leaves banks and non-bank lenders, who appear to have the same requirements for social enterprises as they do for for-profit purchasers, with the additional requirement of having governance suitable for the acquisition.

Lenders expect to secure their loan against something – generally an asset or a known, reliable source of income. Sometimes, in the case of a loan to purchase a business, this might be secured against the business itself. In other cases, the lender may want another form of security. This is where organisations that own assets, most commonly property, will have an advantage. Provided the stakeholders to the property are willing to allow their asset to be used as security, this could be the primary guarantor of the loan. The
process of getting this approval may take some time, and is best done ahead of an actual need. The criteria for, and the limits to, any such security need to be carefully agreed.

The level of loan needed also needs consideration. The actual purchase price of an acquisition may be only part of the capital required. The opportunity costs associated with using an organisation’s own capital may need to be taken into account – for example, in lost income from interest on investments. The running costs of the acquisition in the time of transition may be additional to its usual, ongoing costs; and the cost of paying management or advisors may also be a factor. A comprehensive business case, with associated budgets, will be an essential ingredient of an acquisition process.

5.2.5 Acquisition criteria

At some point in the consideration of how to generate income, and whether a business acquisition would be a viable option, a social enterprise will need to look at the broader range of income generation possibilities. A variety of these are outlined in Table 4. In order to narrow the focus down, some broad criteria such as risk, return, and time can be applied to the options. Once business acquisition is chosen as a preferred strategy, possibly as one amongst several, thought needs to be given as to what kind of business might be purchased. While specific examples are explored in 5.3.3, at this point the principles and processes for deciding what criteria they should use are explored. Participants recognised that they needed to be able to narrow down their search.

The issue of strategic alignment, between the owning social enterprise and the acquired business, was prompted by a specific question and then covered in depth by some participants. Some made the distinction between having aligned mission and values, and having related business types. There was no clear consensus on the need for strategic alignment, with some seeing it as irrelevant (especially if the acquisition was kept at arm’s length), and others saying it was essential, and expecting there would be opportunities to maximise the relationship between the two business types.

In this latter scenario, several participants reflected on the possibilities for leveraging off the respective brands of each entity. The social enterprise could promote the business to its customers and vice versa. Some risk with this was also identified in that the customers of the business might expect a lower price given it was owned by a charity, and the customers of the social enterprise might not agree with it owning a business. Careful branding and marketing was seen as the antidote to this. Cheng and Ludlow (2008) are of the view that having aligned values and a social outcome to the acquired business would provide a key strategic advantage, while Senker (2011) believes that social benefit needs to be added to the generation of a profit. While social enterprises are usually very aware of the importance of their reputation and brand, they are often more aware of protecting it in a more passive way by not doing anything to damage it, rather than actively seeking to expand and develop their brand. Informal feedback from external stakeholders would indicate they often have a conservative view about what NFPs should be engaged in, and this may have implications for pro-active marketing if an acquisition is undertaken.

The other scenario of keeping the two entities at arm’s length, and not choosing to leverage off either brand for combined synergies, was seen as more likely if the two business types were unrelated or if there was some reputational risk with the type of business acquired. While all participants were clear they would never consider an acquisition that had questionable values or business practices, they were less clear on
Table 4 - Template of filters for selection of income generation strategies for social enterprises

<table>
<thead>
<tr>
<th>Category</th>
<th>Sub-type</th>
<th>Options / Details</th>
<th>Risk (low–high)</th>
<th>Return (short – long term)</th>
<th>Consider for income growth</th>
<th>Consider for mission</th>
<th>Time frame (short – long term)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Philanthropy and fundraising</td>
<td>Philanthropic funders</td>
<td>Grants</td>
<td></td>
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<td></td>
<td></td>
<td>Loans</td>
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<td></td>
<td>Events</td>
<td>Small e.g. cake stalls, car boot sales etc.</td>
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<td></td>
<td></td>
<td>Large – e.g. gala dinners, sports tournaments etc.</td>
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<tr>
<td></td>
<td>Donations</td>
<td>Solicited and unsolicited</td>
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<td></td>
<td>Bequests</td>
<td>Solicited and unsolicited</td>
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<td></td>
<td>Social Media</td>
<td>e.g. crowd funding</td>
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<tr>
<td>Cash investment</td>
<td>Bank</td>
<td>Term deposits</td>
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<td></td>
<td>Bonds/stocks</td>
<td>Fixed interest investments</td>
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<td></td>
<td>Shares</td>
<td>Specific type or diversified</td>
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<tr>
<td></td>
<td>Managed funds</td>
<td>Specific type or diversified</td>
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<tr>
<td>Property</td>
<td>Existing or new build residential</td>
<td>Market rental</td>
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<td></td>
<td></td>
<td>Social housing</td>
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<td></td>
<td></td>
<td>Rent-to-buy</td>
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<tr>
<td></td>
<td>Existing or new build commercial, industrial, retail, community use or mixed use</td>
<td>Market rental</td>
<td></td>
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<td></td>
<td></td>
<td>Subsidised rental e.g. room rental for community groups</td>
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<tr>
<td></td>
<td></td>
<td>Rent-to-buy</td>
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<tr>
<td>Business</td>
<td>Current</td>
<td>e.g. café, clothing shop</td>
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<tr>
<td></td>
<td>Acquisition</td>
<td>Franchise</td>
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<tr>
<td></td>
<td></td>
<td>Existing commercial</td>
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<td></td>
<td></td>
<td>Existing NGO service or organisation</td>
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<tr>
<td></td>
<td>Start up</td>
<td>Existing expertise sold to new markets</td>
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<td></td>
<td></td>
<td>New product/service</td>
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<tr>
<td></td>
<td>Contract for service</td>
<td>Current</td>
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<td></td>
<td></td>
<td>Extension of existing work</td>
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<td></td>
<td>New area of work</td>
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<tr>
<td>Alternatives</td>
<td>Commodities</td>
<td>e.g. gold</td>
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<tr>
<td></td>
<td>Currency</td>
<td>Foreign exchange</td>
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<tr>
<td></td>
<td>Derivatives</td>
<td>Options and futures</td>
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<tr>
<td></td>
<td>Other products</td>
<td>e.g. wine, exotic cars, stamps</td>
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<tr>
<td></td>
<td>Domain names</td>
<td>Trade</td>
<td></td>
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<tr>
<td></td>
<td></td>
<td>Buy and hold</td>
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</table>

the limits to that. By way of illustration, a common ethical dilemma faced by many community organisations is whether to accept funding from the proceeds of gambling. While some choose not to, the majority do, and rationalise this as an unfortunate necessity to stay afloat and to be able to do the work they do. They also see this as recycling some of this money back to the community. It was interesting then
that several participants noted that buying a gambling outlet would not be an acceptable business acquisition. Does this mean that third hand receipt of gambling proceeds is acceptable but second hand is not? Perhaps it illustrates the complexity of the context and the lack of definitive answers. One also noted that they would consider purchasing a wine bar, as they thought it would be perceived to be a place where people came to dine, while they would not consider purchasing a sports pub where people came to drink beer, as their perception was that trouble ensued from that.

Aside from the choice of how aligned the acquisition needs to be to the Social Enterprise’s core business, which is a governance decision, there are a range of management and systems parameters which need to be identified prior to undertaking an acquisition. The issue of where to find a business to buy came up often. While participants knew that businesses are advertised, and that there are business brokers, few had ever been in the position of searching for a business to buy. Some noted there might be prior homework to do on identifying the qualities and skills they wanted in the professional advisors they would need, including any brokers. Then they would need to find relevant advisors. In addition to business brokers, and depending on the in-house skills they have access to, social enterprises might need assistance with aspects such as accounting, legal, lending, property, HR, and recruitment skills.

The location of an acquisition was identified as a potential purchase criterion by some participants, usually based on the expectation that someone would need to “keep an eye on things”. More on this issue of monitoring is explored in 5.4. While certainly there may be many advantages in having the acquired business close by, particularly if there were useful synergies between the two, on the other hand the nature of the business might mean it was impractical to be nearby. It is also possible the business could be online, in which case location would be irrelevant.

The nature, type and age of any assets that a business might have were seen as an important factor to consider when developing criteria for a purchase. Some assets like land appreciate over time, and are likely to be more expensive than equipment, which depreciates over time and has the added risk of becoming obsolete. The purchase of assets with a business had the potential to be positive or negative. Appreciating assets would still retain value even if the trading success of the business fluctuated. Depreciating assets would need replacing, and the costs of this would need to be calculated as part of the overall budgeting process.

While it might be self-evident that Social Enterprises looking for an acquisition would be wanting the most profitable option available, that was seen as needing to be balanced by factors such as whether the business was cash based or whether it had to wait for payment from, and potentially chase, creditors. Being able to ascertain how accurate the financial picture is of a possible acquisition was seen as critical in terms of assessing its value. Those participants who had some experience of this strategy commented that it is possible to purchase a business at a discount for a variety of reasons, such as an owner needing to sell quickly due to personal issues. Again, being able to assess the reason for the discount, and whether this represented value for money and could be improved, were relevant factors. It appears that buying a discounted business is a potentially riskier version of this strategy and probably best undertaken by groups with some experience in making acquisitions or who had exceptional advisors.

Financial factors were discussed in 5.2.4. What is relevant financially, in addition to the factors mentioned there, are the parameters that a social enterprise might establish for the size and type of lending they were willing to undertake, the type of lenders they would use, the ability to service a loan, and the impact of any security required on their ability to undertake their regular work. These issues are inevitably linked to the
earlier discussion on ROI and risk. When a social enterprise is working out its criteria for purchase, it ideally needs to work out its boundaries and be willing to stick by them. Venturing beyond those boundaries increases risk considerably; being willing to walk away from potential purchases because they do not meet agreed criteria is essential.

Businesses generally operate with staff, and the issues associated with the staffing for any acquisition, as well as the impact on the current staff of the social enterprise, were explored by participants. It was recognised that there were potential risks with staffing the acquisition, whether existing staff were retained or not. It was not a given that the existing staff were kept on after an acquisition; however, provided they were performing well, they often proved to be one of the key factors determining future success. Identifying if they were performing well would require some careful checking, especially as many sales are kept confidential from most if not all of the staff until completed. As one experienced participant said, sometimes simply watching how staff interact with each other and with management is the best measure of whether they enjoy their jobs and how they are doing. If existing staff are not going to be retained, then a plan to ensure recruitment of new staff is critical to ensure continuity of service. It is also possible that some staff might leave as a result of the sale, and a plan to address this also needs to be considered. Identifying which staffing scenarios are important is part of identifying the selection criteria for an acquisition.

The scenario of buying an owner operated business had some interesting potential for a few participants, particularly if the owner was willing to stay on for a while to train new management and to maintain continuity with customers. It also carried some risks in that it might not have enough scale to produce the return wanted, it might be over-valued, and it might be hard to determine the exact earnings from the business if the owner removed takings in the form of cash, (or said they did). There is likely to be a wave in the next few years of businesses owned by baby boomers whose families do not want to take over the business. Some of these owners may well be willing to stay on with the business in an advisory or even a management capacity for some time if it frees up some of their capital. They may also be willing to leave some finance in the business. The choice of whether an owner operated business is one of the search criteria may be more about whether it aligns with the size or type of business required. However, it might be seen to offer enough advantages as an option to become one of the non-negotiable criteria.

Franchises were discussed by a few participants as a possible type of business for selection. While they usually provide ready-made solutions, or at least promote that this is the case, it would be important to be confident that the level of income claimed is in fact possible. In addition, many franchise businesses are based around being run by an individual or couple who buy themselves a job. Once the cost of paying an operator is figured into the budget, they may not provide the level of return needed. On the other hand, they are likely to be somewhat lower risk than some other kinds of businesses, and a lower, steady return may be more appealing than a potentially higher but riskier return.

The other key factor participants spoke of when identifying what kind of business they would look at was whether there was opportunity for growth, or whether the business was of a type that would become obsolete. Each of these issues is a factor of how the wider market is behaving, and also how difficult it can be to predict that. Some business types which meet core human needs are more likely to have continuity, even if the form of those needs varies over time. Those businesses which are based on passing trends, or technology which is likely to change quickly, are more likely to have trouble staying viable unless they also have the ability to adapt just as quickly. Aiming for growth potential and avoiding obsolescence would be
useful selection criteria. It would be risky to assume that the purchase of a business, which is currently profitable, automatically guarantees that it will remain so without ongoing effort and investment on the part of the new owner.

5.3 Stage two - Due diligence – now we’re looking

In an ideal world, a social enterprise will have taken time to thoroughly work its way through the steps in stage one, in order to be in the best possible position to be considering a range of income generating strategies, and in particular a business acquisition. However, it is not always possible to do things in such a logical progression, and sometimes necessity or opportunities present themselves before this preparation can be done. Many of the components of stage one can potentially be done in conjunction with each other, and with this stage of due diligence. The more important issue is that all of the steps are accomplished before an acquisition is completed. This may involve having the courage to slow things down, or to walk away from potential acquisitions, if the necessary groundwork is not completed.

5.3.1 Due diligence on possible purchases

Countless books and articles have been written on the process of due diligence in general, and in particular on the process involved in acquiring a business. The participants were all well aware there was literature available, even if they had not needed to consult any of it up to this point. They were also aware of various professionals whose expertise they could draw on if they were to undertake due diligence on an acquisition. On the surface it might be logical to assume that the process is the same, regardless of who is doing the purchasing, and in many ways it is. However, what is different are the people undertaking the acquisition.

Regardless of how well prepared a social enterprise is, those from within the organisation involved in the due diligence will still represent an organisation which is driven by values. These values will influence the organisation’s strategy and even hold the potential to divert the organisation from its strategy. While this in no way suggests they should act in a way contrary to their values, if they have established their parameters for acquisition prior to this point, this will enable them to make objective choices rather than be swayed by subjective aspects. The issues raised in 5.2.5 in relation to the expectations for the outcomes from the acquisition, including financial and social, become critical at this point. It will be important for the social enterprise to stick to the acquisition criteria they have developed or, if they find they need to alter those, to have very sound reasons for doing so. Jennings (2012b) outlines a case study where the values clashes involved in the project were a contributing factor to its demise. The example given in 4.2.4 demonstrates a scenario where a Board initially thought that maximising ROI was their primary goal, whereas they instead ended up making an acquisition based primarily on aligned values. This left them with a lower ROI than they would have realised by leaving their money in the bank.

The other way a social enterprise can follow through with their acquisition criteria is to enlist the help of external resource people who they have fully briefed on what they are trying to achieve. They can explicitly invite those experts to let them know if or when they stray from their expressed objectives. Some acknowledged that because they were inexperienced with this strategy, and there wasn’t yet a body of knowledge to draw on, they were likely to need even more support and coaching from external advisors than might be usual. The tendency of social enterprise Boards to be risk averse and conservative by nature
was seen as an ongoing challenge to overcome. Some saw this conservatism as a natural brake to prevent them from taking overly risky decisions, and this needed to be balanced with being able to move at an appropriate pace and make timely decisions. Board members would need to have the necessary skills to hold these two factors in a creative tension, while also working productively with external advisors in ways which did not incur huge costs due to indecision.

Participants’ comments on the components of due diligence ranged from using “common sense” through to extensive detail on the steps required. One who was experienced at this strategy suggested that due diligence needed to happen in stages, with an initial quick screening to rule options in or out, and then a more detailed screening for only those options which might be serious contenders. The initial screening they saw as mainly covering financial factors, given that if the opportunity did not hold sufficient financial potential there was no point in checking out other factors. Only one participant identified the use of a confidentiality agreement to protect both parties. Presumably though, in order to get access to at least some financial data to undertake an initial screening, this would require a confidentiality agreement in most, if not all, circumstances. The literature on due diligence for acquisitions (Snow, 2011) generally recommends this.

The extent to which participants discussed financial factors was linked to their level of experience with the strategy, with those who were more experienced going into greater detail. During the due diligence phase, there were four main types of costs that needed to be understood:

- The purchase price of the potential acquisition
- The current ROI and all the components that went into that
- The projected ongoing running costs and ROI
- The internal and external costs of undertaking the acquisition

In addition to this, there were other financial factors mentioned, such as those associated with any loan finance required, the impact of external factors on the financial costs and returns, and any current or future liabilities which might be known or foreseen. The skill and sensitivity needed to undertake the price and contract negotiations was noted, which again linked in with being clear about who would do what, and that those people had sufficient skill for the tasks assigned. Keeping track of all of these factors would require skilled knowledge and probably significant time; this issue is covered further in 5.3.2. If any one of these factors was not estimated correctly, it would have the potential to undermine the success of the acquisition.

The role of the market and the type of business being considered were mentioned by some of the participants in relation to the due diligence stage. Those business types with high risk or low return were usually not seen as desirable, with the combination of the two being the worst scenario. The only exceptions to this could be if either factor was able to be mitigated. For example, the low return might be a short term factor ahead of investing in future growth of the business, while high risk might be tolerated if it did not put the owning organisation at any risk, or if the returns were likely to also be high. The volatility of the market was acknowledged by some participants as a factor they might have little control over, other than not choosing businesses which were likely to become obsolete in the short term.
In the due diligence stage, considerable thought and attention needs to be paid to the nature and quality of staff required to run the acquisition effectively. Those participants who had been through this process spoke of needing to understand the details of the staffing processes in the business. They saw staffing as one of those make or break factors, and the ability to retain or find appropriate staff as essential to ensuring the success of the acquisition. Some thought that the staff of the acquisition needed to have similar values to the owning entity, while others did not raise this as an issue. Again, this is another selection criteria issue to do with values and expectations that needs to be identified at the “getting ready” stage. If the decision was made not to retain some or all of the existing staff of the acquisition then, as well as having a plan to replace them, the owning entity will need to identify how it can handle this transition for people in a way that is congruent with its values.

5.3.2 Organisational issues

Governance raised its head again with the majority of participants, in relation to what would need to be established organisationally during the due diligence stage. Although this would no doubt be one of the issues discussed in the getting ready stage, it is in this stage that governance structures and composition need to be really clear. The issue of who will set the direction for the acquired business is critical to avoid any lack of clarity, confusion or conflict. This is tied closely to the legal structures that are settled on, both for the owning social enterprise and the acquired business. It is possible that the owning entity’s legal structure might need to be altered to provide the best framework going forward, and to protect its core business. The acquired business will likely need to have its own legal structure. In most cases, participants thought this needed to be separate from the owning entity, although the degree of cross-over of governance and management would need to be carefully worked out.

Legal advice on this is essential to ensure that both the structure and the governance composition do not compromise the potential for charitable tax status for the acquisition. Current New Zealand tax law (Department of Internal Affairs, 2013b) allows for a profit making entity that is wholly owned by a charity, and whose profits are fully returned to support the work of that charity, to itself qualify for charitable tax status and therefore pay no income tax. This additional benefit for an acquisition’s profit margin is likely to be a significant contributing factor to the ROI from an acquisition, and hence the decision as to whether to purchase. Legal assistance on this point is a cost not to be economised on.

The day to day management of the acquisition will be critical to its success, and was mentioned by three participants in detail. It is essential that, during the due diligence stage, a clear understanding of general staff issues is gained, together with a plan for management. Several factors might influence the form this will take. If the previous owner/operator or employed manager agrees to stay on as part of the settlement, either for the transition phase or for longer, then this decision might be straightforward, provided this person is deemed to be competent. If the business is being bought with a view to adding value, then retaining the existing management personnel may not be helpful.

The relationship between the management of the acquisition and the governance of the owning entity was seen as essential to clarify by several of the participants. Given their experience of the complexity of issues around the existing governance arrangements they dealt with, they were well motivated to ensure there was clarity in regards to what would be increasingly complex dynamics if an acquisition was made. There was discussion by some of the possible addition of a small committee, who would sit between the
management of the acquisition and the Board of the owning entity. The role of management staff on this committee would need to be clear, including the reporting and accountability mechanisms. Such a committee would need to be able to move quickly, and therefore clarification about the degree of delegated authority and autonomy it had would be essential.

Participants commented that it was unlikely to be realistic to add the management of the acquisition to the CEO’s existing responsibilities. However, it is also likely that the CEO of the social enterprise would be required to have some involvement with the acquisition, particularly if some of the back room functions of either organisation, such as payroll or accounts, were shared. This raises a different aspect of staffing to that raised in 5.3.1 - the extent to which the purchase of a business by a social enterprise might have an impact on the existing staff of the social enterprise. The staff involved in this are likely to need to develop additional skills and understanding of the nature of the acquisition in order to fulfil these functions. Again, the boundaries between these responsibilities need to be worked out during the due diligence stage, so that any financial or structural implications can be calculated.

The extent to which stakeholders might be involved in the due diligence stage needs to be taken into consideration. While they may have been consulted in the getting ready stage, including perhaps in choosing the criteria for an acquisition, it was suggested by some that this should be the extent of their involvement. The critical factors seem to be in agreeing who will choose the selection criteria for an acquisition, and then who will actually choose the acquisition. This might be internal to the organisation, or it might be contracted out to a broker or other expert. Unlike a regular purchase, particularly of a SME, which is likely to be undertaken by an individual or a family, the purchase of a business by a social enterprise has the potential to have multiple stakeholders who may have very different views. To avoid being tied up in endless meetings about process, attention needs to be given early on to deciding the boundaries of consultation and decision making.

Perhaps an analogy could be drawn with the selection of a CEO. Generally a variety of stakeholders might be canvassed about their selection criteria. Then a subcommittee is usually chosen to undertake the due diligence, and make a recommendation to the Board of either a short list or the final decision. Sometimes this is done by an external recruitment company. The Board ideally then receives the recommendation, asks for a summary rationale, and then endorses the appointment unless major errors have been made. Similarly with an acquisition, it is important to identify who needs to be consulted, which may be different from who wants to be consulted, and also who will be involved in the due diligence process and the final decision.

While the potential for branding synergies was touched on in 5.2.5, in relation to the getting ready stage, the issue of branding was not well covered by participants in the due diligence stage. While the extent of the possibilities for linked branding between the acquisition and the owning organisation might be one of the selection criteria the social enterprise chooses in stage one, its implementation in practice needs to considered in more detail in the due diligence stage. Any expectation of an ability to link the branding of the two organisations will potentially limit the options for selection, and will incur cost for both. In addition, the potential risks of linked branding need to be reviewed. Whether branding would be an initial up front expenditure, or one incurred at a later date once the social enterprise has confidence in the acquisition, needs to be decided as part of the cost forecasting. An equally valid option may be to keep the two entities entirely separate, in which case branding is unlikely to be a major issue.
5.3.3 Ideas, examples, possibilities

There was no shortage of ideas from participants on potential acquisitions, and some of those were linked to various types of contracts with government; not surprisingly, given that this is a model familiar to participants. What is of concern is that this was the default option for a few. Given their expressed desire to diversify income sources, and the current challenges with existing government contracts, the odds are not good that further contracts will deliver a magic solution. While additional contracts might achieve many outcomes, including helping to build the scale of the organisation, they are still unlikely to generate a significant enough surplus to create reserves which will support the sustainability and security of the organisation. Often contract scenarios involve subsidies of some sort, and provide opportunities to employ some of the existing service users of the social enterprise. Being sure about the possibility of these subsidies would be essential in the due diligence stage. If the financial modelling of the acquisition relies on government subsidies, then the social enterprise would do well to establish a guarantee of continuity and whether the business could still be viable without them.

Several of the participants initially assumed, or gravitated towards, an expectation that if they acquired a business they would want it to be able to employ people that the social enterprise already worked with, and who were generally finding it difficult to get employment. This model, commonly called a Social Firm, is the one most familiar to people in the community sector. It holds appeal because it explicitly helps the social enterprise meet its mission, plus it aligns with its values. However, experience from New Zealand and overseas (Social Enterprise UK, 2013b) indicates that having purely social goals, or blended social and financial goals, seldom creates a significant surplus. Evidence from the Scottish pilot study (Social Firms Scotland, 2012) indicated that community organisations undertaking a business acquisition were likely to drift towards trying to incorporate social goals. If maximising profit is the desired goal of an acquisition, then the degree to which the parent organisation’s values must be expressed or visible in the acquisition needs to be clarified in the getting ready stage, as discussed in 5.2.5, and then adhered to in the due diligence stage, in order to avoid this natural bias.

As stated in 2.4.2, while a social firm model is a completely valid model, if the primary goal is to create a healthy profit to support the parent organisation, then generating profit needs to be the clear focus. While there might be useful synergies with the owning social enterprise which occur as a by-product of owning a business, it is important to make sure that the pursuit of these does not detract from the purpose of the acquisition. However, the irony of the alternative model of Conscious Capitalism (Mackey & Sisodia, 2014) is that, by intentionally incorporating a multiple bottom line approach in a business, the evidence shows that the overall returns are better. The difference from a social firm approach is that financial outcomes are actively pursued in a combined approach with social and environmental outcomes. The social firm model tends to focus on the financial outcomes as a by-product of the social outcomes, and does not always reflect the level of financial rigour needed to establish if an acquisition will be fully profitable once all true costs are included. The other difference is that a business following conscious capitalism principles, while it still creates employment, may not focus on employing hard to place employees, which a social firm has as a priority, and which can be a more expensive model of employment.

Once the discussions with participants clarified the focus was on a straight for-profit acquisition, without a goal of transforming it into a social firm, then most had a range of ideas of what types of acquisitions might be suitable, and how the criteria for purchase would be applied. Although the scenario of using the acquisition to employ hard to place employees was ruled out, participants still commented on the potential
to utilise volunteers in the acquisition. Once again this reflects the inherent drift of social enterprises towards their familiar and preferred business model. While using volunteers may be an option, one of the best ways an organisation could meet its social outcomes would in fact be to be a good employer of well paid staff.

Other examples of drift were also raised when participants speculated on developing a business that utilised some of their existing intellectual property (IP). As Cox (2013) discussed, the use of IP to create marketable products or services is questioned by some, who believe that community organisations have a moral duty to share their IP free of charge. This is another kind of drift, this time to a start-up idea rather than an acquisition. It illustrates the default perspective social enterprises are prone to, of utilising the familiar even though these strategies do not often produce good financial returns. It takes imagination and effort to think beyond these perspectives, and to explore different models.

As noted in 5.3.2, the issue of who will choose an acquisition ideally needs to have been worked out before getting to the due diligence stage. This is likely to involve a combination of governance and management input, with a governance sign off. Some of the participants mentioned the role of more subjective factors in the due diligence process, such as intuition, common sense, and gut feelings. It is inevitable these will play a part, ideally though in a conscious and mindful way. If the objective criteria and expectations have been explicitly established as early on as possible, then the more subjective factors can be weighed up against those. Generally though, a subjective response relates to an unexpressed expectation or concern, which can be dealt with appropriately without derailing the due diligence process if there is a climate of transparency.

Participants tended to talk more in terms of types of businesses, such as franchises, rather than actual businesses such as a hardware store. There was a general recognition that each broad type of business had potentially unique attributes. However, as long as the chosen selection criteria were met, then the type was of lesser importance. As mentioned, franchises were raised several times as being a potentially safe option for social enterprises, as they provided more controlled systems and processes, and usually outside support. However, the trade-off for this security might be less profit, particularly if the franchise fees were high. At the other end of the risk scale were companies in receivership. These were seen as high risk, unless the factors behind the receivership were fully understood and could be addressed. The trade-off for this model was the potential for higher returns if the business could be brought back to profitability. Three participants discussed the idea of collective ownership of an acquisition, usually achieved by offering shares in the business as a way of funding some or all of the purchase.

The other option which was raised by several participants was anything to do with social housing. This was definitely a blended outcomes option, with the added advantage for a social enterprise of ticking its social outcomes box. Because the provision of social housing usually involves the purchase of property, then the common drop off in profit when social goals are added could potentially be offset by the appreciation of the assets over time. The adoption of this goal would need to be weighed up against the time frame required for returns, which in this scenario are likely to be long term. There is also an added risk with this scenario, as it may well rely on government subsidies, in this case for tenants’ rent, in order to pay its way or be profitable. A change in government policy on this could see the strategy become very costly, very quickly.

Successful social housing generally provides good wrap around support services for tenants, and the recent research by Woolley (2014) demonstrates that the social outcomes for well supported tenants far outweigh
those where this support is not provided. However, there is considerable cost in providing this support, not all of which is covered by rent or other funding contracts. The risk with choosing social housing provision as an investment strategy is that the social part of the equation, while necessary and valuable, is likely to mean that this is not an income generating mechanism in the short term. Woolley (2014) has found that it has taken many years to build the social housing stock to a point that is large enough to achieve some economies of scale. It is still not undertaken primarily as an income generating strategy, even though the asset base now enables leverage to purchase more housing stock. Therefore, it has over time been a useful investment strategy, but not one to choose if the goal is current cashflow. Overall, it has been a strategy with primarily social outcomes that has had an investment outcome as a by-product.

The other scenario mentioned by a few participants was for two or more organisations to combine resources to purchase an existing community service such as a supermarket or a petrol station. The advantage of having more than one organisation involved in the purchase was the potential to purchase a larger business. This was probably outweighed by the challenges associated with having the time and resources to get more than one organisation investment ready at the same time, and having jointly agreed acquisition criteria. It is also likely to rely on the quality of the relationships between the key stakeholders, in particular the respective CEOs and Board Chairpersons. The time, trust, and commitment needed to make this scenario work between organisations would be similar to that required if they considered a merger of organisations.

The one type of business not mentioned by participants was an internet business. In some ways, this was not surprising, in that while most had experience with websites as an information portal for their organisations, very few had experience trading from a website. However, in some ways it is surprising that participants did not at least reflect on the possibility of an internet business. This may be a function of having no experience with running this type of business, which in turn may be a function of the sector they work in, and it may also be a function of the generation of the participants. While age was not a criterion of choosing participants, seniority and experience were, and these in turn meant that participants ranged in age from their late 30s to their 60s. Internet businesses offer interesting potential though, in that they often have a lower purchase price, and come with a greater possibility to earn income from a global market, depending of course on the product or service they offer.

5.4 Stage three - Now we’ve bought – what do we do now?

The success or failure of many business acquisitions is linked to the quality and thoroughness of the preparation and due diligence done in stages one and two. In discussing the operating conditions which would need to be in place to successfully run an acquisition, participants continually referred back to the ground work which needed to be done in those stages. In particular, they referred to competent governance, and quality management and systems, including in particular excellent financial systems.

The same aspects of governance covered in earlier stages were described, with explicit expectations around reporting and outcomes. The boundaries with management were seen to be important, with everyone knowing what their roles were, and who reported to whom, about what, and by when. The usual cycle of monthly meetings that community organisations have was noted as inadequate for the immediate day to day decision making that was needed in a business. Although CEOs of social enterprises usually have parameters about the authority they have for spending, and with contracts, between Board meetings, this
is usually conservative. The limits for the management of the business acquisition might need to be significantly larger, to enable the effective running of the business in a timely manner. However, along with greater freedom to spend needed to come clear expectations and reporting mechanisms.

Whether or not the management of the business is the same as prior to the acquisition, participants agreed that thorough management systems needed to be in place and monitored to ensure the acquisition runs successfully. Some businesses, especially those which are owner/operated or have been running for a long time, tend to have relaxed systems. This would not create confidence in those responsible for monitoring progress. However, attempts to impose or introduce additional monitoring may be met with resistance. Clear communication and negotiation with staff about expectations, and realistic measures, would go a long way to reducing this resistance, especially when staff could see how useful they were.

Participants recognised that the handover processes from one owner to another would need to be very carefully handled, particularly if it was hoped that most or all of the existing staff would remain with the business. While the due diligence stage usually necessitated keeping the sale of the business confidential from many stakeholders, at some point this information needed to be shared. Staff and customers were seen as a business’ greatest assets, so investing in both over the transition time was essential. It would be important to provide reassurance to both, as well as to other key stakeholders, while also building new relationships.

A challenge not mentioned by participants is the possibility that oversight for the business may end up being provided by people who are not experts in the field, either at the management or the governance level. This is a common dilemma, and there are a variety of views, from those who believe that only an expert in the field can competently manage people who work in that field, to those who believe that a competent manager can manage any situation. There is no guarantee that a competent practitioner will make an effective manager, and there is also no guarantee that a competent manager can be effective in a field they know nothing about. Whichever level of experience the management, and for that matter the governance, have in the type of business represented in the acquisition, it is critical that the people involved in the oversight have a good understanding of all aspects of the work. This may be gained from a combination of experience, observation, involvement, or training.

Having an excellent grasp of the financial factors of the business is crucial in ensuring its success. The current and potential ROI is always going to be a significant factor in the acquisition criteria. Participants also recognised that the current and future ROI should continue to be a main focus in the running of the business. Knowing how to measure and evaluate the ROI was central to this. Not all participants felt confident to do this; this was one of the components which they expected they would need expert assistance with. Linked closely to financial issues were all the day to day functions of the business which would need to be well managed too, including customer service, sales, marketing, invoicing, and stock management.

The branding issues were raised again in stage three, and in particular how the brands of the acquisition and the owning entity might be linked over time. The reputational issues of both organisations needed to be taken into consideration so that any synergies were constructive ones. Again this connected back to the selection criteria worked out in the first two stages, and the expectations that stakeholders might have. If the acquisition was purely for financial return, with no expectation of social outcomes, and/or if the
acquisition was radically different from the owning organisation, then there might be less value in cross-branding the two organisations. However, even if they had nothing in common at all, there could still be value in cross-branding to tap into the feel-good factor of supporting a social enterprise by doing business with the acquisition. On the other hand there may also be risks with cross-branding, particularly if the acquisition does not perform well, and this also needs to be considered.

Several participants noted that all businesses face change, and the attitudes and mechanisms to deal with this needed to be developed and fostered. The acquisition of an already established business should in no way lull the social enterprise into believing it has a ready-made solution for all time. The business would require careful managing and constant fine tuning in order to maximise its returns. Opportunities for development and growth of the business would need to be identified and pursued to keep the business relevant and profitable.

A factor that was not raised by participants directly was what to do if the acquisition failed to achieve its purpose of income generation, for whatever reason. Indirectly, participants had earlier commented that they thought it was important that social enterprises identify their risk tolerance, and what they could afford to lose. Because community organisations typically work on very tight margins and very little profit, it is possible they might not initially have the expertise to identify and monitor what the management and financial targets needed to be, and at what point action would need to be taken if these targets were not met.

It would be important to develop as early in the process as possible, in conjunction with discussions on risk, what the tolerance of the owning organisation would be to factors such as a drop in profits, a change in core markets, or the loss of key staff. Along with this is the need to have an exit strategy, and clarity about when this would be enacted. While the tolerance to risk might shift over time, and the measures of success might be refined, it would still be important to have the tools and the processes readily available to evaluate progress and know when it was time to walk away. And, as one participant noted, it would be unlikely for the social enterprise to lose 100% of its investment should the business fail.

If the exit strategy is worked out at the same time as the discussions on risk, and what the owning organisation can afford to lose, then this may well influence the selection criteria. For example, if the business comes with assets that can be re-sold, then there is always likely to be some recovery of investment. If the business has no stock or assets, such as an internet business, then it may be more likely there would be no recovery of investment if the business failed. There are other reasons when an exit strategy might be relevant, such as when the business has served its purpose and the owning entity wants to re-invest in another venture; when the owning entity is wound up; when it is anticipated that the business may struggle in the future; or when the business has become so successful that a very good return can be achieved by selling it. While it may not be possible to plan for some of these scenarios, again having the tools and processes to make good decisions in a timely manner would be essential to the successful operation of an acquisition.

5.5 Conclusion

This chapter has discussed the findings of the research in light of the three research questions, and in relation to the three stages of business acquisition that the research identified a social enterprise would
need to go through in order to undertake this strategy. This discussion and subsequent analysis has identified the complexity involved in the strategy, and the components which would need to be in place in order for it to be both considered and implemented. The strategy carries significant risks, especially if not done well. It also holds significant potential to provide much needed additional income to support a social enterprise. The final chapter draws conclusions from the research, summarises the recommendations outlined in this chapter, looks at the implications for practitioners, and identifies some potential areas of research that would logically build on this work.
Chapter six – Conclusions and recommendations

6.1 Introduction

This research investigated whether the strategy of business acquisition was a valid option for the community sector in New Zealand, and in particular for social enterprises. Through exploration of relevant literature, and interviews with eleven experienced practitioners, information was sought in order to reflect on the following questions:

1. What conditions need to be in place for a social enterprise to acquire an existing for-profit business?
2. To what extent is it necessary for an acquired business to have aligned purposes, values or outcomes to those of the social enterprise?
3. What conditions need to be in place for a social enterprise to successfully run an acquired business long term, and to ensure its on-going profitability and sustainability?

Through the analysis of the interview transcripts, three key stages were identified for the process of acquisition to be effective:

1. Stage one – Due diligence – getting ready
2. Stage two – Due diligence – now we’re looking
3. Stage three – Now we’ve bought – what do we do now?

By looking at the interaction between the questions and the stages, a thorough picture was built up of the multi-faceted nature of this strategy, and the complexity of conditions that would need to be in place for the strategy to be successful. This chapter summarises the conclusions and recommendations from the research, and then offers some thoughts on what this research means for current practitioners, and also for future research.

6.2 Summary of conclusions

In deciding how to present the conclusions to this research, the author has chosen to use the common questions which have been raised over the course of the research. Inevitably when the topic was named, either in the formal interviews or in informal conversation, one or more of the following questions were asked, often in the exact words of the sub headings. By collecting the final conclusions together under these headings, the author believes the research will be of most practical use to those who might be in a position to consider the strategy of business acquisition.

6.2.1 How do we get started?

Possibly the pre-eminent finding in this research related to how essential the preparatory work is for any community organisation when considering and then undertaking a business acquisition. While three key stages were identified in the research – before, during and after an acquisition – the first stage could potentially take the longest, sometimes several years. This kind of time frame is likely to deter any organisation which might be tempted to see this as a quick fix strategy. If this first stage is done well, it
would create a solid framework for the other stages and potentially shorten the amount of time they would take.

Stage one is essentially about getting investment ready, with all that entails. While investment readiness is certainly about money, it is much more complex than this. Getting investment ready is to some extent a generic process which would also enable an organisation to pursue a range of strategies, and to make informed decisions about how to use and maximise their resources. There would then need to be some specific factors considered when one strategy is chosen over another. These factors must include clarity about sources of capital, legal structures, specific governance or advisory skills required, and the criteria for purchase. Some of these criteria will need to be met before a search for a potential acquisition is even undertaken, and some of these are covered in 6.2.3. Many aspects of the functioning of the social enterprise, which is seeking to undertake an acquisition, are likely to need to be reviewed and possibly refined in order to be in a position to do this well.

Getting started involves a decision taken at some point by someone to do something new or different. Knowing that the strategy is potentially complex and requires a lot of preparation may also hold some security for those who choose it. If they accept in advance that there are multiple steps to undertake, probably over a considerable period of time, then they can work their way through them in a measured fashion, particularly if this strategy is chosen as part of a proactive plan. This allows time for it to be undertaken with care and intention. The key questions that people raise when the strategy is considered are “who is going to do this?” and “how do we pay for it?”, and these are discussed below.

6.2.2 Who is going to do this?

The first stage of getting ready includes clarifying all the key roles, and ensuring there are sufficient people with sufficient skills to undertake an acquisition strategy. Often in a social enterprise, the staff are overworked and the Board members are voluntary. The thought of adding a complex strategy such as this into the mix is likely to feel overwhelming. When people ask who is going to do this, they are usually hoping it doesn’t involve them, or wondering how they could possibly do this on top of everything else. In order to get investment ready, and then choose one or more strategies for income generation, work may first need to be done to find the appropriate people who can both guide the organisation and then manage whatever strategy is chosen.

As discussed in the research findings, the precipitating factor causing an organisation to think laterally about alternative sources of income is often a current shortage of income or resources. Unfortunately, because community organisations do not always have a comprehensive picture of their financial position, nor sometimes the skills to review that and plan accordingly, by the time the financial situation is critical enough to prompt some creative thinking, there may be insufficient resources left to undertake a strategy such as this. The staff and Board will need time and courage to look at every aspect of the organisation in order to identify how it can be sustained, or indeed if it should be. One outcome of this kind of rigorous process is that an entirely different kind of Board, and indeed staff, may be required to sustain the organisation going forward. It is no small challenge for people to consider doing themselves out of a job for the good of the organisation.
While having sufficient capacity is an ideal pre-requisite to this strategy, it is also probable that the social enterprise will build capacity as a result of undertaking an acquisition. At some point a judgment call will need to be made as to whether there is sufficient capacity to proceed, or whether the potential benefits, if capacity is developed as the acquisition process proceeds, outweigh the risks of not developing enough capacity as time goes on. It is certainly preferable to have that capacity in hand before beginning, as the alternative is likely to result in over-stretching the social enterprise to the point of no return.

The preferable approach, as raised several times, is for organisations to regularly plan and review, and to maintain a state of investment readiness. This will enable them to be both proactive and reactive as circumstances require. It will also mean they have staff and Board with the ability to make good strategic decisions, and be able to maximise their financial resources at any one time. (McMorland & Erakovic, 2013) outline the stages of development that common good organisations, as they’ve termed them, typically go through. As groups progress through the stages, their capacity and capability also need to increase. It is unlikely that an organisation at an early stage of development would have the people and financial resources to undertake this particular income generating strategy. The choice of business acquisition over a range of other possible factors involves having access to the necessary skills, time and knowledge. The results were clear that it should not be attempted without these.

The skills, preferences, and biases of the key people involved in a social enterprise are also likely to have an influence on which income generating strategy they choose, and if they choose business acquisition, then which kind of business they choose. It is therefore important that as much as possible an organisation stays mindful of these factors, in order to maintain as much objectivity as they can. If, for example, a business was chosen because one key Board member had some experience in that field, and then that Board member leaves, will the organisation have sufficient skills to continue with that business in their absence? On the other hand, it can be useful to call on the additional resources that key people bring, provided they can be replaced if needed.

Another factor that may emerge is whether the Board has sufficient skills to effectively manage the CEO. Often in a community organisation, particularly in the early stages, the CEO is the most skilled person on the team, and needs to support and coach the Board. As time goes on, ideally the Board members develop capacity, and are able to undertake the level of strategic planning required to ensure the sustainability of the organisation. With this goes the capacity to manage, support and monitor the CEO. While Boards don’t need to be omni-competent, at the stage at which business acquisition might be considered they do need to have maturity, good people skills, objectivity, analysis, the ability to recognise when they don’t know something or don’t have the information they need, and the ability to ask questions. Without this balance of skills, as well as clarity about boundaries between governance and management, the strategy is best not undertaken.

The use of external resource people is critical to the success of this strategy. The type of people needed will depend on the extent of the resources available internally to the organisation, and the nature of the acquisition. Community organisations are often used to accessing expert help as pro-bono contributions, at least as the first option. While this can save considerable cost, it also carries risk. Every group will have a story to tell about how the task got bigger and relationships with the resource person got frayed due to it taking more of their time than expected, and longer than the organisation wanted. The advantage of paying for external help when needed is that it comes with more likelihood of accountability for both parties. Paying for potentially expensive services helps focus people, so that costs don’t grow unnecessarily. It also
allows the organisation to negotiate and enforce time frames which can be critical when negotiating an acquisition.

The responsibilities of governance and management don’t stop once an acquisition is made. They may remain the same; or some different skills, and therefore some different people, may be needed. This links again to being clear on the expectations of all involved, as well as knowing what the lines of communication, monitoring and accountability are. If there is a need for different people at different stages of the process, then appropriate transition plans will need to be developed.

6.2.3 How important are core values?

Inevitably, if social enterprises begin to think about getting investment ready as a precursor to building the financial sustainability of the organisation, the issue of values comes up. So even before the strategy of business acquisition is explored, it is likely that there will be discussion on what is motivating the organisation, and what they are comfortable doing. While participants accepted the premise of the research was looking at purchasing a business primarily for income generation, several found it difficult to focus on doing this without also attempting to create some degree of social outcome. This was even though they could see this might reduce the financial return. It was almost as though they couldn’t help themselves, and this raises the question as to whether they would be able to pursue a purely income generating strategy without trying to achieve blended aims. Is it even possible for a values driven organisation to put their focus on social outcomes aside, in order to objectively pursue income generation? Or to own a business which was not aligned at least in some way with its primary work?

All the participants were clear that they would be unable and unwilling to acquire a business which was unethical or reflected badly on the owning entity. However, that left countless options, and they were continually thinking about how they could achieve multiple outcomes from owning a business. This may be because the nature of the community sector is such that people are used to working with limited resources and trying to get the most out of those. It may also be because meeting social outcomes is their default setting, and they may be unable or unwilling to step aside from that.

This dynamic means it is imperative that a social enterprise considering an acquisition is clear what it is trying to achieve, why, and what the parameters to that are. They also need to understand the implications of their choices on the financial outcomes, if that was their initial motivation. If achieving the best financial return possible is the primary goal, and if they know they will continue to try and add multiple outcomes to the expectations, they may need to consider having some different people involved who will help them focus on that aim.

There are a range of potential options which come from combining the following factors in different ways – financial outcomes, social outcomes, similarity of business type with the owning entity, and the ability to link branding between the two entities. These form part of the acquisition criteria which are best worked out in the getting ready stage. In order to do this, organisations might find it easier to rule out what they would not consider, and then approach everything else as a possibility. They would still need to narrow the search down at some point, and again, this is where their acquisition criteria are essential. If the decision is to aim for linked branding, or a business with synergy with the owning entity, then this will narrow down
the types of possible acquisitions. If once a search is underway, it proves difficult to make a choice, it may be that the criteria need to be re-visited and refined. This may entail another conversation about values.

Faith based organisations potentially have the most challenge in this area, given their values are coupled with religious beliefs, as well as often being organisations with longer histories and traditions, and sometimes significant assets. Any other organisation with substantial assets and some longevity may also have more deeply developed or entrenched values to address. Where there are substantial assets, there will be an organisational story as to how those came about. Within that story there may be clues as to what the organisation could do again to utilise those resources in a new way. Organisations that do have a strong asset base can become conservative in the management of those resources in order to preserve what has been built up. This can divert them from focussing on their core mission. They are usually in a stronger position than an organisation without assets, as they are more likely to be able to take time to pro-actively develop a long term strategic plan. One question which might enable an in depth and courageous conversation is “What risks did our organisation take in its past, why, and what can we learn from that to meet our mission today?” This could lead them to a plan for new income generation strategies to further increase their mission outcomes.

6.2.4 How do we pay for it?

Although, as mentioned above, investment readiness involves many factors, it clearly includes a number of financial components. It takes time to develop the capacity and skills to manage and monitor financial issues at the level required to undertake any investment beyond putting money in the bank. It will inevitably continue to develop and be fine-tuned if an acquisition is undertaken; however, the research demonstrated that some pre-requisite competency is essential. This is both in terms of the current business of the social enterprise, and also the ability to assess any potential purchase from a financial perspective. If a social enterprise is considering business acquisition as a strategy, and does not have these skills, then they will need to proactively develop them as early in the process as possible.

Many newer or smaller community organisations approach their finances from a budgeting perspective, seeking to balance the books to meet their current expenses. In order to increase their income, an organisation has to move to a growth and investment approach, and be able to firstly imagine, and then secondly formulate other ways of generating income. When considering strategies for increasing income, it is important to identify if the primary goal is cashflow, or capital growth over time, or both. Usually these two factors sit in inverse proportion, especially in the early stage of investment, until any capital growth takes hold.

The financial skills required, accessible internally or externally, will enable an organisation to evaluate possible acquisitions and undertake all the necessary calculations to ensure they know what is a viable option and what is not. These calculations need to include all the costs before, during and after the acquisition. It is also important to establish what percentage and scale of return is needed, and to understand how this would influence the size of the acquisition. Even if a smaller acquisition was more profitable than a larger one, the relative size of the profit may mean that the larger organisation is what would be needed in order to achieve the overall profit required. A smaller acquisition might also not provide enough overall return to pay for a manager and other overheads which were not part of the current costs of the acquisition.
Unless an organisation has access to capital from whatever source, this strategy would not be possible. Only a few larger and probably older organisations are likely to have sufficient reserves to be able to purchase a for-profit business outright. This would be a much easier proposition than seeking grants or loan finance. The main factors that would need to be weighed up, if a purchase was made from existing funds, would be the opportunity cost of using the money for that purpose rather than where it was currently invested, and whether there would still be enough money left in reserves to meet whatever the organisation’s commitments were. For many organisations who might undertake this strategy, they would need to seek loan finance, and more about the lenders’ criteria is covered in the next section. There are no known sources of grant capital in New Zealand at present to fund such a strategy, although one participant did say “with the amounts of money we throw at programmes you could provide seed capital for a not-for-profit to buy a business and let them grow their impact over time”.

6.2.5 Who else do we have to convince?

While the key leadership of a social enterprise might be clear that the strategy of business acquisition will be the best option for them, there will be a number of other stakeholders who might need to be considered or consulted, or who may have the power of veto. If the organisation plans to leverage off the equity in their current assets to acquire a business, then there may be a parent organisation that has to be convinced in order to do this. If the organisation has a membership based structure where some or all of the members have to be consulted, then this step has to be undertaken. And even if other stakeholders do not have a direct power of veto, their disapproval of the strategy might have a detrimental effect on the existing work of the social enterprise.

In each of these situations, a careful case may need to be made to explain to or convince stakeholders why this course of action has been chosen. It will be important to remember that the leadership of the social enterprise may have been engaged in a planning and information gathering process which has taken considerable time, and it may also take stakeholders some time to understand and accept the strategy. It will be useful to bear this in mind from the beginning and to have a parallel plan of stakeholder engagement, and possibly marketing, in order to avoid delaying the process once the social enterprise is ready to undertake an acquisition strategy. There may be conflicting perceptions of what a social enterprise or community organisation should be involved in, and this in turn may influence the extent of shared branding the two organisations are able to develop.

Unless an organisation is very large or well resourced, at some point they will need to access external advice. Firstly there will need to be some criteria developed in order to choose the advisors and, even if the criteria includes that the advisor is willing to do the work pro-bono, there will then need to be criteria developed as to the extent to which the advisors’ advice will be adhered to, particularly if they don’t like the advice.

If loan finance is required to undertake an acquisition, then the lenders’ criteria will need to be met. It will be useful to explore early on who the potential funders might be, and what their parameters for lending will be, as this may affect the preparation and due diligence, as well as potentially affect the selection criteria. If a particular business type or attribute will render the social enterprise ineligible for loan finance,
then it is best to know that as soon as possible. It may be that this option is then removed from the drawing board, or it may be the organisation develops a plan to meet the loan criteria.

Whether the finance comes from bank or non-bank lenders, there are some common lending criteria that can form a starting point for the social enterprise’s preparation. The lender will want to know that the organisation has the capacity and competency to manage an acquisition well. They may require information about the skills and experience of key advisors, Board and staff. They may require a guarantor for a loan if it is not secured against an asset. They will certainly set a limit on the lending, which will involve an interaction between the key financial indicators of the acquisition such as the equity level the owning entity has in its assets, and the loan to value ratio that it deems acceptable. Having this information in advance in the getting ready stage, at least in general terms, will enable realistic selection criteria to be developed.

If the type of business to be acquired will be connected to or funded by external contracts, then the procurement policies of those funders may well influence the acquisition process. There may be external compliance or certification requirements which, while they may already exist in the business to be acquired, may also be expected in the owning entity. Again it is important to know this in advance, particularly as it may influence both the choice and cost of an acquisition.

6.2.6 What choices have we got?

The process of getting investment ready will inevitably involve an organisation weighing up a range of scenarios for growing their income. These are summarised in Table 4. By considering a reasonably complex matrix of criteria that will be particular to each organisation, they will narrow the options down to some which will meet their goals. Traditionally, when community organisations have had surpluses, they have deposited those in a bank. If the surpluses grew significantly, then they would look at other cash investment options, often via a broker or third party. If they grew further, then property has been the common investment tool. Buying a business, especially directly rather than via a managed investment scheme, has not been a commonly used strategy in the community sector.

There may well be space in the community sector for customised investment advice for organisations seeking to make best use of their funds and resources. While there are multiple resources available for this via the commercial sector, and while the tools are the same, the values, skills and attitudes may well be different. Decision making in the community sector can often be slower, especially until the capacity to make quick decisions is developed, and external advisors may not be accustomed to this. It could be helpful to have the tools and knowledge commonly used in the commercial sector packaged up in ways that meet the unique needs and perspective of the community sector.

There are options to invest in businesses via an intermediary, and some participants wondered whether this was a safer and less time consuming strategy than undertaking it directly. A decision on this would involve weighing up factors such as time, expertise, cost, available businesses, level of return, and availability and accessibility of capital if needed. The other key factors which might influence the decision to invest in a business directly would be the potential for synergies from direct ownership. These might include the ability for cross-branding and enhancement of reputation, as well as the likelihood that the
capacity of the owning entity would grow through the experience of working through this process directly, including the possibility of providing some back room services for the acquisition.

6.2.7 Is it an option for us or not?

Why this strategy rather than any other? The literature review provided few clues on this and even fewer examples. It is clear from this research that business acquisition is a potentially risky and complex strategy, and the circumstances in which it can or should be attempted are outlined below. The perceived or actual degree of risk involved is likely to be a key factor in explaining why so few groups have tried this, as is the need for capital up front to invest. What is surprising is that there is so much in the social enterprise literature suggesting start-ups as a viable initiative for mission, growth, or income generation, despite the fact that start-ups have a high failure rate. Possibly the reason they are considered first is because start-ups may not be thought to require significant capital initially, and also because they usually involve an already familiar aspect of the business. However, they do often require capital to grow to an economically viable point, and that takes many groups by surprise. That may be a contributing factor to their lack of success as an income generation tool. While they don’t all fail in the sense that they go out of business, they often struggle to do more than break even. What start-ups can offer is the ability to develop skills and capacity as they proceed. However, this tends to be a by-product of the strategy, rather than part of the original plan.

By contrast, in order to successfully undertake a business acquisition, a social enterprise needs to be in a relatively strong position already, and to have undertaken a significant amount of preparatory work to be investment ready. They also need to have accepted that this strategy is likely to be a long term initiative, and so they will have understood that it is not an emergency short term fix. The only exception, when a social enterprise might consider this strategy in the short term, would be if they were fully investment ready, and could quickly purchase a business that was likely to remain fully profitable through a transition.

The scale of the owning organisation and its stage of development, combined with the same factors for a potential acquisition, are important dynamics in determining whether this strategy is a viable option for a social enterprise. Stages of development are not always predictable or linear; however, in the early stages, organisations usually do not have the capacity of a more mature organisation, and are therefore unlikely to be able to muster the resources required.

As a result of distilling all the available data from the research, the following two scenarios are those in which the strategy of business acquisition is most applicable, and most likely to succeed:

1. Large organisations that will inevitably have capacity in systems and staffing, regardless of whether they have large reserves and assets, although these make it easier. They have the luxury of taking their time to be pro-active about planning and developing strategy, and have chosen to move past the natural inertia and conservatism that can often happen in maturity. They will have found a bold, courageous mission goal which requires and motivates them to be creative about maximising their income over time. They are also likely to have a reasonably well developed capacity to survive a poor investment decision.

2. Other organisations with a degree of maturity that are going through a renewal stage, or are evaluating their long term strategy in order to stay relevant and viable. They may not
necessarily be large, although they may have been in the past. They have access to some reserves or assets which they can leverage from. They have developed enough capacity to find a way to consider and develop a new strategy. While there may be some concerns about their long term relevance or survival, they are unlikely to be able to undertake this strategy if they are faced with imminent closure. Having a bold mission goal is an important motivation for seeking additional income, although keeping a valuable community organisation viable may also be a strong enough motivator.

The final factor for an organisation to consider is whether they have fully weighed up all the risks and have a plan to manage those. Risks can take many forms and, while there are common ones such as financial and branding risks, there will be others particular to each organisation. The risk of failure needs to be considered with each potential scenario, and the possible impact on the owning organisation if this happened. In most cases, the organisation should be able to sustain the risk of failure without it putting the owning organisation at risk of closure. The threshold for this, and the tolerance for this possibility, needs to be clear. Along with this is the necessity of an exit strategy. Making an acquisition, or any other investment decision, should not be done without knowing how the owning organisation can walk away if needed.

6.3 Recommendations

The following recommendations fall under the same headings and stages used in chapter 5.

Stage one - Due diligence – getting ready

Current context and environmental conditions

1. If business acquisition is chosen as a strategy for growth or income, and the social enterprise is not already investment ready, then sufficient time needs to be allowed for the various stages of change and due diligence required to undertake this strategy.

2. National and local governments commit to procurement policies with local benefit clauses that allow smaller local organisations to participate in contracting for service provision, and ensure positive outcomes of contracts are experienced locally.

3. Faith based and other organisations with substantial assets review their investment and asset management history and policies in order to:
   - Identify strategies and strengths that were used to build those assets and which offer insights for the future; and
   - Evaluate if they can creatively and courageously leverage off their assets and resources for further developing their mission and social outcomes.

Governance

1. Boards ensure their recruitment processes enable them to have membership fit for purpose.

2. Boards regularly undertake strategic long term planning, including a review of their means of income generation to achieve their mission.

3. Boards seek to maximise their current income and to maintain a state of investment readiness, including having appropriate legal structures, and the ability to move quickly if needed.
Business approach

1. Social enterprises identify if they have the capacity and capability to undertake a business acquisition before embarking on the strategy and, if not, whether they have the resources to build this capacity first, or whether it could come as a result of the acquisition.

Financial factors

1. As part of becoming investment ready, social enterprises identify likely sources of capital for any purchases undertaken, and ensure they can meet the lending criteria ahead of any need. This may involve having robust financial systems, and arranging pre-approved finance.
2. The business case for an acquisition includes detailed projections of all possible costs to ensure these can be covered.

Acquisition criteria

1. Social enterprises seek to identify which income generation strategies meet their requirements.
2. If business acquisition is the chosen strategy, then a matrix of selection criteria needs to be developed to assist their decision making, including identifying which criteria are non-negotiable for them, and what reasons would cause them to review their criteria.

Stage two - Due diligence – now we’re looking

Due diligence on possible purchases

1. Social enterprises identify what people and resources they will need, ideally in advance, in order to comprehensively undertake due diligence on any particular acquisition.
2. Social enterprises identify which criteria need to be fully satisfied prior to selecting an acquisition.

Organisational issues

1. Skilled legal advice is sought to ensure the appropriate legal and governance structures are put in place to enable the successful running of the acquisition, and to avoid tainting of the owning entity.
2. There is clarity in the lines between, and the respective responsibilities of, governance and management.

Ideas, examples, possibilities

1. Social enterprises establish the types of businesses they are willing to consider as part of identifying their selection criteria.
2. Social enterprises remain aware of their bias to drift to primarily social outcomes, and make conscious choices to apply their selection criteria consistently to possible purchases as agreed.
Stage three - Now we’ve bought – what do we do now?

1. A thorough handover and transition strategy is developed for the change of ownership.
2. Excellent governance, management, and financial processes and people are involved in the running of the acquisition to ensure its success.
3. An exit strategy is prepared, including the indicators and threshold beyond which action is required.

For each of the two likely scenarios outlined in 6.2.7 where business acquisition may be a potential strategy, each of the recommendations above applies in order to ensure the best possible outcome.

6.4 Future research ideas

In the course of this research, a number of questions and issues arose which were outside the scope of the work. Some were more closely aligned to this particular topic than others. Further investigation of any of these may prove useful for a range of stakeholders. The following questions may be worth exploring further.

Governance and legal structures

1. How do traditional Boards make the transition to being able to achieve investment readiness and to undertake income generation strategies such as business acquisition?
2. What type of legal structure would be most appropriate for an acquisition by a social enterprise?
3. Can a regular business be transformed by the addition of multiple outcomes, and still remain profitable and sustainable?

Faith based organisations

1. What values, practices, and risks allowed faith based organisations to develop significant assets in the past, and are those same qualities, behaviours and circumstances in evidence today?
2. What investment and asset management principles do faith based organisations use, and how do they link these to the missions of their organisations?

Start ups

1. What are the comparative outcomes for social enterprises from start-ups versus business acquisitions?

The role of the chief executive and senior management

1. How does the length of tenure of a CEO in a community organisation affect the development and choice of long term strategy?
2. What are the implications for the community sector for the high levels of stress experienced by, and the limited resources available to, CEOs?

**Scale and capacity**

1. To what extent are the scale of an organisation and its stage of development correlated with its ability to undertake various income generation strategies?

2. Is it possible to undertake community development at a medium to large scale?

### 6.5 Closing remarks

This research began with three questions to explore the strategy of business acquisition for community organisations in New Zealand. It identified three stages to progress through in order to ensure the necessary groundwork was done to make the strategy successful. Finally, it highlighted two organisational scenarios for which the strategy was most suited and had the best chance of succeeding.

It is now clear that this is a challenging, time-consuming and potentially risky strategy. Doing nothing is also potentially risky, and is a strategy in itself. However, doing nothing may be a conscious or an unconscious choice. Whether business acquisition is the right or best strategy for any particular organisation comes down to having a number of key factors in place. It should only be attempted if this is the case. Provided it is done well, and given a bit of luck with conditions outside of the organisation’s control, it has the potential to improve the financial outcomes for the owning organisation as well as to add value in other ways – e.g. scale, reputation, brand, and infrastructure. Done poorly, it has the potential to distract the owning organisation from its core business, or at worst to put the owning organisation out of business. This is particularly so if the legal structures do not enable the parent organisation to be protected, or the maximum tax benefit to be realised.

The first organisational scenario where the strategy would be most suitable is where there is reasonable scale and healthy reserves, and this enables a long-term view of income generation. They are likely to have used the power of compounding interest and other investments to grow their reserves over time, and have then decided to leverage off their assets and reserves in order to leapfrog their development. By way of illustration, one of the two larger organisations represented in the research had until recently taken a conservative approach to investment management, and were now experiencing resistance from key stakeholders to taking a different approach that might be higher risk but could bring in higher returns. The other larger organisation had set ambitious mission goals and needed significant capital to carry those out. This led them to taking an intentionally entrepreneurial approach and leveraging off their current assets. Both had scale and reserves; only one was investment ready and active.

The second organisational scenario where the strategy would be most suitable is in small to medium organisations that are well established and have some access to lending or investment capital. They are motivated by mission or a necessity to think laterally to generate additional income, and they have sufficient stability to remain viable for the time it will take to implement an acquisition strategy. Unfortunately, many organisations of this size are so focused on managing their current pressures, or with survival, that they struggle to have the capacity, capability and thinking space to explore major new strategies. They are caught in the trap of feeling so overloaded and so focused on the survival of the
organisation that they cannot or will not step out of their comfort zone. However, it is worth asking if the strategy of business acquisition is potentially any more complex and stressful for them than the task of managing subsistence survival?

Perhaps it is the presence of bold plans, for both survival and growth, that will galvanise otherwise typically slow and conservative organisations to undertake strategies outside of their experience or comfort zone. Those organisations which are willing and able to be adventurous and courageous, and to utilise their extensive skills to create long term, proactive strategies, will not only help ensure the survival of their organisations, they will also be able to abundantly thrive and continue to achieve their mission. The strategy of business acquisition is one tool which can assist some organisations on their journey of survival, growth and mission effectiveness.
References


Appendix 1 - Participant questionnaire

From section 2 of the proposal:

“The research questions I will explore are designed to identify the skills and factors involved for a Social Enterprise in acquiring a for-profit business:

1. What conditions need to be in place for a social enterprise to acquire an existing for-profit business?
2. To what extent is it necessary for an acquired business to have aligned purposes, values or outcomes to those of the social enterprise?
3. What conditions need to be in place for a social enterprise to successfully run an acquired business long term, and to ensure its on-going profitability and sustainability?

Expanding these broad areas for the interviews:

The format of these questions will apply most directly to CEO’s/Senior Managers/Board Chairs of social enterprises (or those who support and advise the sector). If the questions are posed to an individual who is not speaking on behalf of an organisation then the questions will be adapted as below in brackets.

1. I’ve read (know) a little of your organisation’s background from the web/your constitution/annual report etc. You know from the topic of my research that I’m looking at the value of business acquisition in the community sector (which for the purposes of this research includes church organisations). I’d like to start by asking if you can you tell me something of how you think business skills and tools (strategies) apply currently in your organisation (are relevant in the community sector)?
2. Can you tell me what’s happening in your organisation to make sure it will still be here in the long term (what you see happening in the sector by various groups to ensure they will be sustainable long term)?
3. Has your organisation considered (Have you give any thought to/what do you think about) the strategy of business acquisition? If yes, where are you (where is your thinking) up to in that process? If not, what might cause you to consider it?
4. If you are (or were to) considering or are involved in business acquisition, what factors do you think need to be in place for the acquisition to proceed effectively?
5. Are there any specific investment or acquisition criteria which you think need to be met before a business acquisition should proceed, or factors which should be avoided? (Prompts – ROI, cash flow vs. debt, goodwill, staff, governance, management plan, etc.)
6. What, if any, limits might your (do you think an) organisation (needs to) put on the type of business it would consider acquiring?
7. To what extent do you think it is necessary or important for the owning charity/organisation and the acquired business to have aligned aims or activities?
8. Once a business acquisition has occurred, what do you think needs to be in place in order for the acquisition to develop sustainably?
9. Is there anything else you’d like to add?
Appendix 2 - Participant information and agreement forms

Information for participants

Research Project Title: Business acquisition in the community sector in New Zealand.

Synopsis of project:
In this research I plan to explore the strategy of business acquisition as a means to diversify income sources in the Community Sector, focusing particularly on Social Enterprises. The goal of this strategy is to assist Social Enterprises to better meet their social objectives. In broad terms, Social Enterprises are organisations in the community sector which blend business skills with achieving social good. They usually have charitable tax status and often hold public sector contracts to deliver services. Typically they have a limited range of income sources such as contracts, grants and donations, all of which can be vulnerable to sudden changes outside of their control.

What I am doing:
In this project I will focus specifically on business acquisition as a strategy to generate income, and I will explore the following questions which are designed to identify the skills and factors involved for a Social Enterprise/community organisation in acquiring a for-profit business:

1. What factors or criteria may need to be in place for a Social Enterprise/community organisation to acquire an existing for-profit business?
2. To what extent is it useful for an acquired business to have aligned purposes, values or outcomes to the Social Enterprise/community organisation?
3. What factors or criteria may need to be in place for a Social Enterprise/community organisation to successfully run an acquired business long term and ensure its ongoing profitability and sustainability?

What it will mean for you:
I would like to conduct a 60-90 minute face to face interview with you to explore your experience and views on this topic. I would also like to audio tape the interview so that I can later transcribe it and further analyse the material we cover in the interview. You have the option of reading the transcription of the interview if you wish.

If you agree to participate, you will be asked to sign a consent form. This does not stop you from changing your mind if you wish to withdraw from the project. However, because of my schedule, any withdrawals need to be done within 2 weeks after I have interviewed you, or 1 week after reading the transcription should you choose to do so. It is expected the transcription will be completed within one month of the interview. Please indicate on the consent form if you wish to see this.
Your name and any other information that may identify you will be kept completely confidential. All information collected from you will be stored on a password protected file and only you, my two supervisors, and myself will have access to this information.

Please contact me if you need more information about the project. At any time if you have any concerns about the research project you can contact my principal supervisor:

Gavin Rennie, phone 815 4321 ext. 5070 or email gennie@unitec.ac.nz

UREC REGISTRATION NUMBER: 2013-1018
This study has been approved by the UNITEC Research Ethics Committee from 27.6.13 to 27.6.14. If you have any complaints or reservations about the ethical conduct of this research, you may contact the Committee through the UREC Secretary (ph: 09 815-4321 ext 6162.) Any issues you raise will be treated in confidence and investigated fully, and you will be informed of the outcome.
Organisational Consent

I _____________________________ (name) _____________________________(position)
of _____________________________________________ (organisation)
give consent for Vicki Sykes to undertake research in this organisation as discussed with her.

This study has been approved by the UNITEC Research Ethics Committee from 27.6.13 to 27.6.14 and is subject to the approval of research ethics application no 2013-1018.

Signature: ________________________________

Date: ________________________________
Participant Consent Form

Research Project Title: Business acquisition in the community sector in New Zealand.

I have had the research project explained to me and I have read and understand the information sheet given to me.
I understand that my discussion with the researcher will be taped and transcribed.
I understand that I can see the transcription and the finished research document.
I understand that I don't have to be part of this if I don't want to and I may also withdraw within two weeks of the completion of the interview, or within one week of reading the transcription if I request to do this.
I would like to see the interview transcript YES / NO

I understand that everything I say is confidential and none of the information I give will identify me and that the only persons who will know what I have said will be the researcher and her supervisors. I also understand that all the information that I give will be stored securely on a passworded computer by the researcher for a period of 5 years.

I have had time to consider everything and I give my consent to be a part of this project.

Participant name (please print) ______________________________

Signature: _____________________________

Date: ____________________________

Project Researcher: _____________________________

Date: _____________________

UREC REGISTRATION NUMBER: 2013-1018
This study has been approved by the UNITEC Research Ethics Committee from 27.6.13 to 27.6.14. If you have any complaints or reservations about the ethical conduct of this research, you may contact the Committee through the UREC Secretary (ph: 09 815-4321 ext 6162). Any issues you raise will be treated in confidence and investigated fully, and you will be informed of the outcome.
Appendix 3 – Ethics approval

Vicki Sykes
8 Waterbury Place
Mangere
Auckland, 2022

24.7.13

Dear Vicki,

Your file number for this application: 2013-1018
Title: Business acquisition in the community sector in New Zealand.

Your application for ethics approval has been reviewed by the Unitec Research Ethics Committee (UREC) and has been approved for the following period:

Start date: 27.6.13
Finish date: 27.6.14

Please note that:

1. The above dates must be referred to on the information AND consent forms given to all participants.
2. You must inform UREC, in advance, of any ethically-relevant deviation in the project. This may require additional approval.
3. Organisational consent/s must be cited and approved by your primary reader prior to any organisations or corporations participating in your research. You may only conduct research with organisations for which you have consent.

You may now commence your research according to the protocols approved by UREC. We wish you every success with your project.

Gillian Whalley
Deputy Chair, UREC

cc: Ken Simpson
Cynthia Almeida