

## **SOCIAL BUSINESS MODELS AS GROWTH STRATEGY FOR NON-PROFIT ORGANIZATIONS**

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### **Abstract**

The purpose of the article is to examine the current definitions of social enterprises (SEs) in Europe and in Israel in particular. This article lists some of the industry's top definitions, presents four models for SE implemented currently in Israel and investigates, in depth, a model in which a non-profit organization (NPO) establishes a SE. In the chosen model, we interviewed eight key stakeholders who manage and work for the NPO and the SE. The findings of the study reveal several important parameters for managing the success of the SE. Among the identified parameters the authors discuss the one regarding the management of the tension between the economic goals and the social goals, and the ability to manage a three-sector partnership successfully.

### **Keywords**

Israel, social enterprises, nonprofit organization, social business, cooperative, hybrid organization

### **JEL Classification**

L31, M20, O10

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### **Introduction**

In the last decade, social enterprise models and their ecosystems have been developing fast all over the world. Several tentative definitions and typologies were offered by researchers, to explain this phenomenon of social enterprises. Today, there is still no complete agreement on one definition of the concept, but there are key guidelines for analysing the phenomenon. The first purpose of this article is to present current definitions of the SE field from Israel and other countries. The additional aim is to present a case study of an Israeli NPO which develops a SE. We expect to learn more about the characteristics of this unique model.

### **Review of scientific literature**

Doyle et al. (2010) suggest that SEs reflect two key concepts: social goals and entrepreneurial creativity. Fernando and Mario (2017) suggest that SEs are hybrid organizations, which may follow one of these 3 main models:

A. **WISE** (work integration social enterprise) bring back to earning employment people at risk which were out from the labour market.

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B. **BOP** (Base-of-the-pyramid) provides vital products/services at a reasonable price to poor customers which would otherwise not have access to them.

C. **Hybrid trade** (creating a new balance for trade) enterprises focus mainly on controlling trade relations. In order to achieve this, they generate revenue for marginalized producers by charging extra conscious consumers.

In addition, they suggest looking at the relationship of the organization with its environmental issues, suppliers, market, competition (Table no.1).

**Table no. 1 Key distinguishing factors between traditional and hybrid organizations**

<b>Type of organization</b>	Relationship of social/environmental issues to organizational objectives	Relationships with suppliers, employees and customers	Interaction with market, competitors and industry institutions
<b>Traditional organizations</b>	Social/environmental issues are addressed only if the organization has the organizational slack (e.g. resources and profit) and a strong business case	Relationships with suppliers, employees, customers and suppliers are primarily functional and transactional in nature. Cost factors are primary	Industry activity is premised on creating markets for traditional goods and services, appropriating and protecting competitive benefits and altering industry standards for self-serving benefit
<b>Hybrid organizations</b>	The business model is configured to address explicit social/environmental issues; organizational slack and the business case are secondary	Relationships with suppliers, employees and customers are based on mutual benefit and sustainability outcomes.  Costs are considered but only after social and environmental outcomes are met	Industry activity is premised on creating markets for hybrid goods and services, competing successfully with traditional companies and altering industry standards to serve both the company and the condition of the social and environmental contexts in which they operate

Source: Haigh and Hoffman (2012) as cited in Fernando and Mario (2017)

Defourny and Nyssense (2016) suggest identifying 6 main paths/trajectories, resulting in 4 major SE models. They form a triangle which is set by 3 axes of interest: **mutual interest (MI)**, **general interest (GI)** and **capital interest (CI)**. These axes are completed, then, with a multi-dimensional analysis comprising the financing source of the SE: **dominant market income**, **dominant non-market resources** (public funding), and **hybrid resources** (mixed resources). According to their analysis, the field forces create supported by the six criteria,

the 4 main models of social businesses: **ENP** (entrepreneurial non-profit), **SC** (social cooperatives), **SB** (social business), **PSE** (public-sector social enterprise). Each model is characterized by combinations of its native interest in the field and its sources of income (Fig no. 1).

This figure is based on EMES Network's research, a group (launched in 2013 to build up international knowledge around SE) of 200 researchers from 50 countries, Israel included. It suggested 3 major dimensions to identify SE models: their **social goals**, **types of income** (their business model from non-profit, hybrid or for profit organizations) and **governance structure**. There can be a diversity of social goals from addressing a social problem to marginalized groups or foster economy democracy. Governance structure can be explained in different models from the point of view of profit distribution (from "some to non" distribution of profit, depending on the form of SE from non-profit or for-profit and also on the local law). Fici (2015) mentions another perspective on governance which pays attention to the types of stakeholders and their innovation to be involved in decision making in the SE.

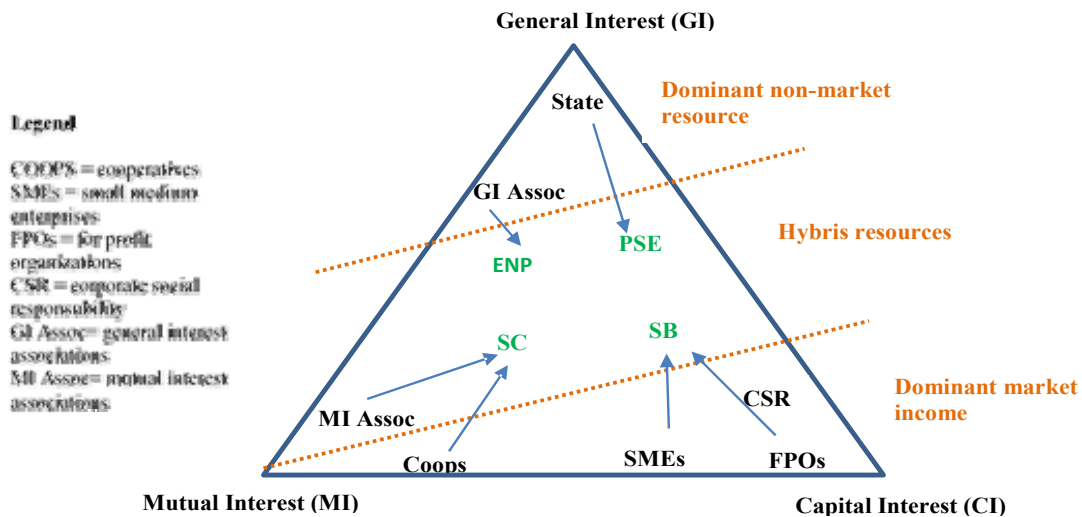


Fig. no. 1 Institutional trajectories and resulting SE models

Source: Defourmy and Nyssense (2016)

## SEs in Israel

### 1. Background facts on Israel

According to GEM (Global Entrepreneurship Monitor Report on 54 countries) Israel is a young, 70 years old country with a population of 8.4 million people, GDP \$296.1 billion (2015), SME contribution to GDP: 45% (2012), economic development Phase as innovation-Driven, has the highest score from 54 countries on Cultural and social norms for innovation (scored 7.2 in a scale from 1-9=highly sufficient).

### 2. Models of SEs

In Israel the academic research on social enterprises started in 2009. It has been focusing on NPO's development of SEs by selling services from its expertise or establishing a new income-generating venture (Benziman, 2009; Abrutski & Askenazi, 2011). Solel (2011) included cooperatives as SE models. Gidron and Abbou (2012) included business entities. From a survey of SEs from 2012, Gidron and Abbou (2017) found that the phenomenon is relatively small, under 200 organizations were established since the year 2000 (employing

15-20 people). An SE encompasses marginalized populations, coping with disability, or youth at risk.

Abbou et al. (2017) defined 4 specific SEs models in Israel today: commercial **SBs**, **cooperatives**, **NPOs** and **public sector**. Each model has different characteristics in relations to ownership, economic projects, social aims, governance structure and specific challenges (Table no.2).

**Table no. 2 Distinct characteristics of Israeli SE models**

Characteristics	Business	NPO	Cooperative	Public sector
<b>Governance</b>	One or two entrepreneurs	Participatory governance	Democratic governance involving stakeholders	Operate within the public Sector and abide by its rules
<b>Ownership</b>	Independent	Established by an organization; led by voluntary board	Established by a group; collective ownership	Established by a public organization
<b>Economic project</b>	Initial funding: private equity, loans and investors; Ongoing: 100% sales; Profits: belong to the owner (s) or shareholders; Risk: high risk tendency	Initial funding: philanthropy; Ongoing: sales and donations; Profits: invested in social cause; Risk: low risk tendency	Membership fees and share purchase; Sales; Profits: belong to group members; Risk: Medium risk tendency	Initial funding: public organization’s budget (POB) Ongoing: Sales, POB Profit: Invested in the products and/or welfare of workers in WISEs Risk: low-to-medium risk tendency
<b>Social mission</b>	Emphasis on a social mission that can provide a competitive advantage, such as environment or employment; Target population: stronger individuals within marginalized populations	Broad variety of social missions, including: culture, education, employment, rehabilitation; Target population: can accommodate a larger spectrum of marginalized populations	Social mission priority to social mission such as social activities and consumption; Target population: socially conscious individuals	Broad variety of social missions that provide a competitive advantage such as environment or rehabilitation Target population: general public and marginalized populations
<b>Specific challenges</b>	Business side taking over the social side; Costs required to cope with social issues	Relating financial activity to social core; Professional economic management	Effective decision-making and management; Require membership fees that might exclude marginalized or poorer populations	Refraining or limiting Replacement of government services; lack of participatory governance

Source: Abbou et al. (2017)

**2.1 Legal definition of SEs**

Israel doesn't provide legal forms for SEs (unlike USA – with L3C or the UK – with CIC, (Brakman, Reiser, 2014). In June 2017 a proposed amendment to the Israeli Companies Law, was meant to set SEs in the law as companies that would be able to earn and distribute dividends. The recommendation is to limit the dividend distribution to 50% of the profit, so that at least half the profits will remain in the company in order to develop the social activity. It will also be committed to adopting a social goal.

**2.2 Support and guidance of SEs**

Although the market is relatively small, a variety of consultants, investment funds (some in cooperation with government funds) for SEs can be found in Israel. Among them are IVN, Dualis, Social Impact Bond, Shatil, Minga, the Forum of SE in Israel.

**3. This article presents a case study on NPOs which develop SEs in Israel**

Gotesman et al. (2017) show that in the last decade government policy of privatization social services led to the strengthening of non-government organizations (NPOs, Business, SE) as a provider of services to civilians instead of the government. Looking at the third sector in Israel, Gotesman et al. (2017) found that out of the entire job employment in Israel, NPOs provide jobs to 448,000 people (13.6%). The services these organizations provide cover a large and diversified domain, including education, culture, religion, health, welfare. NPOs source of income is self-generated (35%), public (50%), coming from donations (15%). By 2015, 36,000 NPOs were active (Almog-Bar, M., 2016).

Following the conclusion in Table no. 2, in the context of the characteristics of NPOs developing an SE, we conducted research hoping to reach a deeper understanding of this model.

**Research Methodology - Case study**

We chose an Israeli NPO, which had already established a successful SE and conducted in-depth interviews with eight key stakeholders. In Table no. 3 we present main facts about the NPO and its SE.

**Table no. 3 Main details about the NPO and its SE**

<b>NPO</b>	<ul style="list-style-type: none"> <li>- Main goal is to narrow socioeconomic gaps through the activities of large businesses (for profit) in Israel;</li> <li>- Founded 22 years ago;</li> <li>- 27 employees;</li> <li>- Budget 2,298,000 EUR;</li> </ul>
<b>SE</b>	<ul style="list-style-type: none"> <li>- Main goal is taking care of youth at risk by establishing small business (like carpentry shops, outdoor advertising, gardening, food and so on);</li> <li>- Founded 4 years ago;</li> <li>- 25 employee;</li> <li>- 100 youth at risk benefit from its establishment;</li> </ul>
	<ul style="list-style-type: none"> <li>- Key partners in financing the establishment: 15% NPO, 85% government;</li> <li>- 100% independent revenues from the sale of products by the youth at risk;</li> </ul>
	<ul style="list-style-type: none"> <li>- The organization reached an economic balance and fully covered its expenses only in the fourth year.</li> </ul>

We interviewed eight key stakeholders: one member of the NPO board of directors, the CEOs and two employees; the CEO and 3 employees of the SE. In Table no. 4 we present an index of characteristics and factors indicated by managers as being important when managing an organization within this model type.

**Results and discussion**

**Table no. 4 Characteristics of NPO which develops SE**

<b>Characteristics</b>	<b>Factors results</b>
<b>Reasons for establishing the SE</b>	- finding a modern and effective solution for the target population in providing them employment;
<b>Success indicators of the SE</b>	- significant continuous employment for the target population; - strong and sustainable tri-sector partnership between sectors (NPO, government and business); - achieving economic balance after a reasonable period of time since establishment;
<b>Deliberations that should be taken into account in managing the balance between economic and social goals</b>	In the first period of the SE, deepening the achievement of social goals for the target population even at the expense of economic balance (such as: producing during weak periods in order to maintain employment all year round, opening work shifts with few participants, accepting every youth at risk who applies, regardless of their qualifications). Later on, deepening the achievement of financial goals even at the expense of some social goals.
<b>External factors that can influence the SE success</b>	- changes in the Youth Employment Law; - new decisions by the government/local authority regarding the use of its buildings for the operations; - excessive requirements on the part of insurance companies for the operations; - local economy – customer purchasing power;
<b>Advantages of establishing the SE under an NPO</b>	- source of income diversity to the NPO (from spare profits); - it is easier to introduce additional partners from the philanthropic / business world to the SE; - NPOs previous experience with youth at risk, can contribute to the success of the SE; - NPO can help ensure the preservation of its social goals alongside with the business goals;
<b>Disadvantages in the development of the SE under the NPO</b>	- uncertainty regarding the NPOs sources of financing of the SE; - NPOs managers, board of directors lacking experience in managing business; - difficulty in obtaining credit from the banks for the development of the SE;
<b>Benefits of working with the SE main partner (this case, the government)</b>	- access to more significant financial resources. - access and ongoing use of the partner's infrastructure for building the business. - division of responsibility with the state on taking care of the target population (youth at risk);
<b>Difficulties of working with the SE main partner (this case the government)</b>	- differential gaps between partners point of view on managing the SE (such as: implementing innovative changes, what is considered large /small in activity, cheap/expensive, fast/slow, clean/dirty); - requires bureaucracy skills in managing the partnership with the government; - different points of view of partners regarding how to grow and develop (such as: in which channels, by what costs, and at what social goals);
<b>Skills required of the SE employees</b>	- good understanding of the three-sector partnership management; - inclusion of the social and economic challenge side by side; - strong belief in the model itself as a tool for influencing the target population;
<b>Circumstances for closing the SE</b>	- SE will not prove sustainable economic ability; - the target population will no longer want to be part of it; - it has no significant impact on the target population.

Analyzing the above-mentioned answers, we can pinpoint to

- a. the managers' reason for establishing such a model of SE under NPO: to come up with better solutions in providing employment to the target population;
- b. the benefits of such a model: providing significant continuous employment for the target population, establishing a strong and sustainable tri-sector partnership between sectors (NPO, government and business) and achieving economic balance after a reasonable period of time since establishment;
- c. the limits: the uncertainty regarding financing, lack of experience in managing a SE, difficulty in obtaining credit from the banks, bureaucracy, possible difficulty created by the partnership with the government, sustainability.

What we see as the most prominent characteristics are: maintaining a balance between achieving financial goals and their social goals and the requirement for a high level of management skills of a three-sector partnership.

### **Conclusions**

Our research is one step towards further elaboration of the definitions in the SE growing field. In this article we have presented a number of definitions of the SE field. Fernando and Mario (2017) suggest that social enterprises are hybrid organizations (in forms of WISW, BOP, Hybrid trade). Defourny and Nyssense (2016) identify 6 main paths/trajectories, resulting in 4 major SE models (ENP, SC, SB, PSE). In Israel, Abbou et al. (2017) present 4 main models: SBs, cooperatives, NPOs and public sector. Each model has different characteristics in relations of ownership, economic projects, social aims, governance structure and specific challenges. Our case study, conducted in Israel, focuses on the model of an NPO which founded a social enterprise. The interviews of the eight stakeholders revealed the fact that the two main factors important for managers were:

- a. maintaining a balance between the achievement of economic and social goals;
- b. this model requires a high level of management of a three-sector partnership.

Additional parameters were also stressed, such as the one which indicates that the organization's employees should prove managements' skills allowing them to cope with the tension between economic and social goals.

We consider that the significance of this research is the finding indicating the importance employees see in the target population point of view in terms of the effectiveness of the SE. Since there are only a few models like this in Israel, the study was limited to one organization. Therefore, we interviewed a relatively small number of people. For a better understanding of the model we recommend further in-depth research which will continue to explore other similar organizations both in Israel and worldwide in order to contribute to defining the field and characterizing successful models of work in the area.

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