

# Interpreting social enterprises

Carlo Borzaga  
Sara Depedri  
Giulia Galera

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## RESUMO

### Compreendendo negócios sociais

A variedade de instituições e organizações existentes crescentemente caracteriza os sistemas econômicos avançados. Ao passo que as teorias econômicas tradicionais enfocavam quase que exclusivamente organizações maximizadoras de lucros (ou seja, empresas geradoras de lucro) e organizações governamentais, a crescente relevância das organizações sem fins lucrativos e particularmente das organizações sociais exige dos pesquisadores reflexões sobre uma nova abordagem econômica ampla, capaz de explicar tal variedade organizacional. Neste artigo, examinam-se as principais limitações das teorias ortodoxas e institucionais e reafirma-se a necessidade de criar e testar um novo arcabouço teórico, que leve em conta as formas variadas empregadas por organizações diversas na perseguição de seus objetivos, as variadas motivações que impelem os atores e as organizações, e os diferentes padrões de aprendizagem e rotinas dentro das organizações. O novo arcabouço analítico aqui proposto baseia-se em desenvolvimentos recentes, principalmente evolutivos e comportamentais, das teorias da empresa. Esta passa a ser interpretada como um mecanismo de coordenação da atividade econômica cujos objetivos não coincidem forçosamente com a maximização de lucros. Ao contrário, os agentes econômicos são hoje movidos por uma complexidade de motivações e uma vontade intrínseca e não monetária de manter um papel crucial na formação das atividades da firma, acima e além de objetivos puramente monetários ou financeiros. Acredita-se que o novo arcabouço seja particularmente apropriado para a correta interpretação da emergência e do papel de formas organizacionais e de propriedade não tradicionais, as quais não são movidas pela busca de lucros (organizações sem fins lucrativos), sendo reconhecidas principalmente nos formatos legais das cooperativas, Organizações Não Governamentais (ONGs) e empresas sociais. Uma gama contínua de formas organizacionais, que vão desde atividades geradoras de lucro até atividades voltadas ao bem público, e que englobam organizações de benefício mútuo como seu principal constituinte, são aqui consideradas e discutidas.

**Palavras-chave:** variedade organizacional, economia evolucionária, economia comportamental, motivações não pecuniárias, benefício privado, benefício mútuo, benefício público.

*Carlo Borzaga* is Full Professor in the Department of Economics at the University of Trento, Italy, where he teaches Political Economics and Labour Economics. He is also President of the European Research Institute on Cooperative and Social Enterprises (EURICSE) in Trento (38122 – Trento – Italy).

E-mail: [carlo.borzaga@euricse.eu](mailto:carlo.borzaga@euricse.eu)

Endereço:

EURICSE

Via San Giovanni, 36

38122 – Trento – Italy

*Sara Depedri* is Research Fellow in the Department of Economics at the University of Trento, Italy and at European Research Institute on Cooperative and Social Enterprises (EURICSE) in Trento (38122 – Trento – Italy). She teaches Economics of Employment Choices and Workers' Motivations and Economics of Nonprofit Organizations.

E-mail: [sara.depedri@unitn.it](mailto:sara.depedri@unitn.it)

*Giulia Galera*, received her PhD in 2009 at the School of International Studies at the University of Trento (Italy). The doctoral work was devoted to analyze the impact of social enterprises in transition economies, with special regard to Poland and Ukraine. She is currently research coordinator at the European Research Institute on Cooperative and Social Enterprises (EURICSE) in Trento (38122 – Trento – Italy) where she is in charge of carrying out research and coordinating research projects; developing and promoting training programmes; and disseminating research findings to relevant stakeholders. EURICSE is a research centre devoted to study cooperative and social enterprises according to a multi-disciplinary and international perspective.

E-mail: [giulia.galera@euricse.eu](mailto:giulia.galera@euricse.eu)

## 1. INTRODUCTION

Since the 1990s, the concept of **social enterprise** has been increasingly used to qualify entrepreneurial initiatives in a number of different sectors of general interest (DEES, 1996; BORZAGA and DEFOURNY, 2001). Social enterprises have acquired steady prominence as a global dynamic, thanks to their capacity to deal innovatively with some of the problems and challenges of contemporary societies (GALERA and BORZAGA, 2009), cutting across countries characterized by dissimilar levels of economic development, welfare systems and degrees of democratization.

The defining features of social enterprises are the goals pursued and the production modalities adopted, rather than simply the goods and services produced. Consequently, a varied and increasing number of initiatives are currently defined as social enterprises, including those supplying social services, those promoting ethical financing, micro-credit and fair trade, and generally those producing goods and services with goals other than profit, such as the organizations that aim to combat poverty and undernourishment (YUNUS and WEBER, 2008). The spread of these initiatives has helped to broaden the definition of social enterprise and has also played a part in generating some conceptual confusion. This evolution underscores the need to both develop a general and shared definition of **social enterprise** that goes beyond specific and diverse cultural and legal contexts, and to explain the development of these institutions.

This article provides support for an interpretation of social enterprises as institutions that bridge the gap between the demand for and the supply of those goods and services of general interest that are undersupplied or not supplied at all by public agencies and for-profit enterprises. Following a brief analysis of the concept of social enterprise, its main features, evolution and dissemination, this article proposes an interpretation of the social enterprise as a specific institution in which a group of people can manage production activities benefiting the entire community or people in need. The analysis proposed, while challenging the conventional interpretation of social enterprises, provides insights into the specific conditions under which they can develop.

## 2. ANALYZING THE HISTORY OF THE CONCEPT SOCIAL ENTERPRISE

The term **social enterprise** was first used in the 1980s to identify the innovative private initiatives established voluntarily in Italy by groups of citizens that had formed to deliver social services or to manage economic activities designed to help to integrate disadvantaged people. At about the same time, organizations sharing similar goals were developing in several other European countries. These initiatives were initially set up using the non-profit legal forms provided by national legal systems (associations, foundations or cooperatives), which

were in some cases modified to allow them to combine entrepreneurial activities with the pursuit of social aims. As a result, in some countries, such as France and Belgium, most of these organizations adopted associative forms, while in other countries, such as Italy, they adopted cooperative forms, giving rise to **social cooperatives**.

Concurrently, the social enterprise concept also started to be used in the United States (DEES, 1996) with a strong emphasis on the market and business world (DEFOURNY, 2010, p.44). The term social enterprise was used to refer to initiatives that were substantially different from those found in Europe. In the United States, the term referred mainly to profit-generating activities carried out by non-profit organizations to fund the pursuit of social goals. In this approach, the search for commercial ways to raise funds was spurred by a number of problems faced by non-profit organizations in the late 1980s, including rising costs, more competition for fewer donations and grants, and increased rivalry from for-profit companies entering the social service sector.

Over the last decade, as indicated in the growing international literature on this theme, the concept of social enterprise has made amazing breakthroughs not only in Europe countries and in the United States, but also in other regions of the world such as East Asia, Latin America, and the countries of the former Soviet Union (DEFOURNY and NYSSSENS, 2010).

In East Asia, social enterprise-like initiatives have started to emerge within civil society organizations in response to structural changes, including the dislocation of the manufacturing industry and deindustrialization in the process of accelerated globalization, high unemployment, and growing social inequality problems. The concept first appeared around 2000, but had no generally accepted definition (DEFOURNY, 2010). Nevertheless, the South-Korean parliament passed a law in 2006 for the promotion of social enterprises dedicated to providing social services or work integration for hard-to-place jobseekers. These organizations had a role in clarifying the concept (BIDET, 2008). When considering Mainland China, Taiwan and Hong Kong as well, the most specific feature of social enterprises in East Asia certainly continues to be the state's strong involvement and control (DEFOURNY, 2010).

In Latin America, the array of socio-economic institutions other than public agencies and conventional enterprises has been growing since the 1980s as a response of civil society to inequality, unemployment and social marginalization. The solidarity economy in Latin America encompasses a multitude of social segments, agents and institutions. It is aligned with a global movement that is critical of capitalism, although its focus is usually on starting concrete enterprises aiming at individual, social and ecological development (GAIGER, 2010). Latin America's social and solidarity economies are increasingly rooted in locally focused, community-led, democratically driven, and self-managed economic activity (VIETA, 2012). Social enterprises, such as previously defined, can be seen as

part of this locally led reaction, which is taking place in all Latin American countries.

In post-communist countries, in spite of the dramatic rise in the number of civil society organizations at the start of the transition, social enterprises are generally not visible (BORZAGA, GALERA, and NOGALES, 2008). The roles of social enterprises in Central Eastern and Southeast Europe are still widely underestimated. Several factors help to explain their insufficient development relative to the demand for general-interest services and the adoption of entrepreneurial behaviors by groups of people, including lack of supporting environments and infrastructures, restricted access to resources, unsuitable institutional framework and inconsistent legal environment. This results in a lack of legal regulations and unsuitable legal frameworks that fail to consider social commitment and the degree of disadvantage of social enterprises. Overall, in the social systems and economies of post-communist countries, social enterprises are still seen as **gap filling** agents, rather than as long-term welfare and economic players (LES and JELIAZKOVA, 2007).

Given the spread of social enterprises in various geographical and cultural contexts, the concept of social enterprise covers several meanings that seem to diverge according to the different approaches. This differentiation evidently concerns not simply the concept *per se*, but also the processes and embedded dynamics that lead to the different understandings of the term, the activities conducted, and their types of action.

On the one hand, the combination of the notion of **enterprise** with the adjective **social** has generated new definitions characterized by different meanings; on the other hand, a number of new concepts have been developed to define the same types of initiatives. Given the absence of an internationally shared definition, the lack of statistical data, and the poor theoretical and empirical research, it is still difficult to provide an accurate picture of the social enterprise from an international perspective, which leads to a multiplicity of partially overlapping definitions. The terms most often used are **social entrepreneurship**, **social business** and **social enterprise**. Furthermore, other concepts combining entrepreneurial activities with the pursuit of social aims have emerged. Many terms are used to refer to these types of enterprises, sometimes interchangeably and often creating confusion. The term social entrepreneurship (or social enterprise, where enterprise is not used as a noun but as a verb) and social business overlap to some extent and tend to be blurred with social enterprise. Although the literature in this field is not yet consolidated, the time is ripe for a tentative clarification.

The terms social enterprise, social entrepreneurship, social business and social entrepreneur all refer to initiatives that explicitly aim to generate social value through the private use and management of human and financial resources that are partially generated by market and quasi-market exchanges. As such, these initiatives are not designed to pursue the maximization

of profits, but rather to use market mechanisms to underwrite the provision of goods and services that have a social impact. These four terms have been widely employed to refer to initiatives in a variety of spheres.

One can better understand the main differences between the terms by contrasting social enterprise (when enterprise is used as a noun) and social entrepreneurship. Social enterprise refers to a production unit fully belonging to the universe of enterprises and producing general-interest goods or services in a continuous and stable way. Social entrepreneurship, on the other hand, encompasses a broad range of activities and initiatives that fall along a *continuum*, including a range of entrepreneurial initiatives, from institutionalized entities pursuing a social goal, relations and practices that yield social benefits, and entrepreneurial trends in non-profit organizations, to ventures developed within the public sector (JOHNSON, 2000; ROPER and CHENEY, 2005; MAIR and MARTÌ, 2006). Another crucial difference between these two terms is the emphasis of social enterprise on the collective dimension and of social entrepreneurship on the individual dimension. In Europe, the social enterprise is normally a collective enterprise whose background is rooted in a long-lasting tradition of associations and cooperative enterprises. By contrast, the concept of social entrepreneurship tends to highlight the crucial role of **extraordinary individuals**, who are driven by philanthropic aims.

The term social business (and social business enterprise) falls somewhere between the other two concepts, though it is closer to the definition of social enterprise. It was proposed by Yunus (YUNUS and WEBER, 2008) to distinguish his initiatives from the broader spectrum of social entrepreneurship activities. Similar to the concept of social enterprise, social business refers to production units that are formally established and organized to ensure continuous production, especially in fields of activity of general interest other than welfare. However, like social entrepreneurship, social business disregards the collective dimension, emphasizing the entrepreneurial qualities of the founders of the enterprise with a clear preference for the shareholder legal form.

Another definition, partially connected with the described concepts, is social innovation. This term is a recent construct that is meant to grasp lasting social change, both in terms of process adopted and outcomes achieved. Social innovation is indeed defined as

“a novel solution to a social problem that is more effective, efficient, sustainable, or fair than existing solutions and for which the value created accrues primarily to society as a whole rather than to private individuals” (PHILLS, DEIGLMEIER and MILLER, 2008, p.36).

The concept dismantles the barriers between sectors and entrepreneurial forms and refers to a wide set of novel solutions.

As such, a social innovation can be a product or a production process, but also an idea, a social movement or a combination of several elements; hence the alleged heightened appropriateness of this concept to understand and produce, in principle, lasting social change, when compared to social enterprise and social entrepreneurship (which specifically refer to specific organizational typologies or practices), but also its intrinsic vagueness.

The conceptual explosion of economic terms along with the adjective **social** signals an important change in the debate about the role of enterprises. It witnesses the emergence of a new sense of responsibility on the part of single individuals, groups, and enterprises that are increasingly concerned about the impact of their actions upon society and the environment. Nevertheless, although all these concepts can be seen as parallel trends that strengthen each other, their reach and revolutionary character varies considerably. Social enterprise appears to be the most innovative concept because it is strongly connected with a process of institutionalization. While it has a narrower focus than the other terms, it identifies more precisely the key features of the diverse, voluntary, bottom-up organizations established over the last three decades to produce general-interest services. Given their consolidation, wide dissemination and key contribution to socio-economic development, these new organizations can be regarded as a model of social innovation ahead of one's time.

### 3. THE MAIN FEATURES OF SOCIAL ENTERPRISES

The first and so far most comprehensive definition of social enterprise was put forth by the EMES European Research Network (BORZAGA and DEFOURNY, 2001; DEFOURNY and NYSENS, 2010). This definition is broadly accepted by academics and has inspired several pieces of legislation designed to regulate these forms of enterprise, as well as the recent initiative of the EU Commission on Social Business. This definition was initially devised along two dimensions, one economic-entrepreneurial and the other, social. Following an intense scientific debate and the introduction of specific laws on social enterprises, this definition can now be more precisely structured along three axes: the economic-entrepreneurial, the social and the ownership-governance ones (DEFOURNY and NYSENS, 2010).

The economic-entrepreneurial axis assumes that social enterprises show the typical features of any kind of enterprise. Accordingly, social enterprises must be engaged in the stable and continuous production of goods or services and rely at least in part on the use of costly production factors (e.g. paid work and costly credits). Finally, owners are expected to take a significant level of economic risk.

The social axis presupposes that social enterprises pursue an explicit social aim of serving the community or a specific group of people through the production of general-interest or merit goods and services. Given the context specificity of the concept of **merit goods**, which depends on the judgment of a

given society, the typology of services supplied can vary substantially. According to the diversity of unmet needs that may arise at local levels in different countries and contexts, the set of services delivered can range from welfare, health, educational and cultural services to economic and general interest services (e.g. water supply, gas, electricity). All of these can be provided free of charge or at low prices to those who are unable to pay for them.

The ownership-governance axis presupposes that social enterprises are characterized by collective dynamics involving people from a community or a group that shares a certain need or aim; the adoption of decision-making processes not based on capital ownership and ensuring the participation of all relevant stakeholders; and compliance with a total or a partial non-distribution constraint, meaning that the organization distributes profits only to a limited extent and has an asset lock, thus avoiding profit-maximizing behavior. The participatory and inclusive governance system aims to strengthen the social orientation of the enterprise, on the one hand, and to support a fair distribution of results, on the other. The said criteria are meant to allow for an effective identification of new needs emerging at a community level and to help to create and strengthen trust among the stakeholders concerned.

This definition does not refer to a specific national legal system or to specific legal forms. It envisions the social enterprise as a new private-sector and autonomous legal entity, which differs from traditional non-profit organizations, because it engages in productive activities according to entrepreneurial criteria. Unlike conventional enterprises, social enterprises pursue an explicit social goal. This implies producing goods and services that generate direct benefits for the entire community or specific groups of disadvantaged people. Social enterprises pursue a balance between the fair remuneration of labor and capital and the by-products generated, to the advantage of users, and they usually rely on several sources of income, including governments, when the services delivered are recognized as merit goods, plus monetary and work donations, as well as market and private demand.

### 4. EVOLUTION AND DISSEMINATION OF SOCIAL ENTERPRISES

The development of social enterprises has been heterogeneous. In some countries, they have expanded widely and rapidly, whereas in others they emerged later or are yet to take root. The analysis of the socio-economic factors favoring or preventing their emergence provides a useful basis for understanding social enterprises (BORZAGA and IANES, 2006).

When looking at the context of the emergence of social enterprises, particularly at the beginning of their development, several initiatives responded to the new needs that were ignored by for-profit enterprises and were inadequately addressed by public policies. Social enterprises have often been started as

self-help groups of local communities. Rather than advocating more effective local government interventions, these new initiatives organized concrete responses themselves, by instigating entrepreneurial initiatives and mobilizing a mix of resources. They have responded to new and unmet needs, often relying on voluntary work as well, especially in the start-up phases. Other initiatives established during the 1980s sought to combat rising unemployment by creating enterprises that produced goods and services fulfilling unmet demand, to facilitate the integration of people who were difficult to employ (BORZAGA and BECCHETTI, 2011). So far, social enterprises have mainly developed in the production of welfare services and work integration. Nevertheless, they are also expanding into other fields of interest to local communities.

Social enterprises have followed various evolutionary trends, according to their ability to interact with government players. The dissemination of social enterprises has been especially dynamic in countries that have implemented decentralization policies in the sphere of social services, in contexts of growing pressure on public finances. Responding to fiscal crises and the declining legitimacy of welfare systems, social enterprises offer an appealing alternative to public agencies in terms of providing services. The resulting decentralization generated a new field for intervention by social enterprises and for public resources to flow to. These developments helped to consolidate the organizational models of social enterprises under construction and stimulated a progressive concentration of social enterprises in public markets, particularly welfare markets.

The increasingly high percentage of income generated from public contracting can accelerate the dissemination and consolidation of social enterprises, but simultaneously it may have the unintended consequence of increasing the dependence of social enterprises on public resources and policies, thereby reducing the propensity of social enterprises to innovate.

However, this trend is not the predominant one (BORZAGA and FAZZI, 2011). The search for new and diversified types of relationships among social enterprises, public institutions, and private-sector enterprises is widening and deepening. One important issue is whether contracting mechanisms can better exploit the general-interest goals that characterize the mission of social enterprises and the nature of the goods and services that they produce. At the same time, social enterprises are increasingly engaged in those structures in which socio-economic development policies are discussed and defined, especially at the local level.

When looking at the activities conducted, one can identify new trends when it comes to investing in product and process innovation. Social enterprises appear to be especially eager to identify new products and fields of activity. These new fields may border on the traditional core activities of social enterprises, such as health and education, but may also involve completely new spheres, including culture, environment, so-

cial tourism, and social housing. Process innovation has also occurred as social enterprises resort increasingly to networking through company groups and agreements. These include consortia, groups, product societies, project partnership, and temporary enterprise associations that aim to clarify and coordinate the roles and interdependency among the various players of the production chains. These initiatives have involved social inclusion initiatives targeting disadvantaged people by means of agreements between social and for-profit enterprises.

## 5. LEGAL RECOGNITION OF SOCIAL ENTERPRISES

Since the 1990s, the dissemination of social enterprises has been linked to the introduction of a set of regulations that have resulted in institutionalization. Regulations have played a part in defining the social enterprise sector. From an international perspective, despite similar identity connotations, social enterprises are extremely diverse as far as both their fields of activity and legal-organizational forms are concerned.

National legislatures have generally followed one of two paths in regulating this sector (GALERA and BORZAGA, 2009). The first involves the creation of legal forms designed specifically for social enterprises; these have generally been created by adjusting existing legal forms, usually those of co-operatives. The new regulations have specified goals, activities, constraints, governance assets and incentives. Italy's Law 381 on social cooperatives, passed in 1991, was the first such law to be instated and it was subsequently regarded as a benchmark reference by other countries that followed a similar route, such as France, Korea, Portugal, Spain, Poland and Greece.

The main features of the Italian Law are that it defines a general-interest goal that social cooperatives are expected to pursue, focusing on the types of services<sup>(1)</sup>, the possibility of engaging a plurality of stakeholders (including remunerated workers, beneficiaries and volunteers), and the imposition of severe constraints on the distribution of profits, in addition to the typical features characterizing cooperative enterprises, namely, the assignment of both collective ownership and democratic governance according to open-door and one-person, one-vote cooperative principles.

The second path does not link social enterprises with a specific legal form, pinpointing instead a number of structural and mission characteristics that could, in principle, be satisfied by any type of private-sector legal form. Belgium was one of the countries that resorted to this approach, with its *entreprise à finalité sociale*, as well as the United Kingdom with its Community Interest Company, and Italy with its Law 118/2005 (and subsequent decrees) on the Social Enterprise. These three laws are quite similar and follow the definition provided in this paper. All three identify the main goal of the enterprise as the pursuit of general interest. All three establish precise and severe profit distribution constraints.

There are, however, two main differences among the three laws: the fields of activity that social enterprises are entitled to engage in and the collective and participatory dimension. In terms of activities, the Italian law identifies the sectors in which social enterprises can operate, while in other cases (United Kingdom, Belgium and France) the law leaves it up to the enterprise to choose which general-interest activities to carry out. In terms of participation, the Italian and French laws admit only collective social enterprises and governing bodies in which workers and clients participate.

In the United States, where the definition of social enterprise generally focuses on generating income for organizations that provide services typically thought of as belonging to the non-profit sector, social enterprises were, until recently, stuck between the choice of being set up as for-profit entities with some social objectives or as non-profit entities with some commercial objectives. However, several states are now passing laws enabling the registration of low-profit limited liability companies (L3Cs), which are meant to bridge the gap between non-profit and for-profit organizations. L3Cs could in principle revitalize the provision of social services in the United States, provided that appropriate supporting policies stimulating capital flows to these organizations and building public awareness are adopted (DOERINGER, 2010).

## 6. INTERPRETING SOCIAL ENTERPRISES

The emergence and dissemination of social enterprises challenge both the dominant model of welfare systems, which is based on the action of the State and Market, and conventional economic theory, which assumes that enterprises promote only the interests of their owners and minimize production costs. From this point of view, there are two main concerns worth mentioning: on the one hand, some authors are concerned about the commercialization of social enterprises, claiming that their productive ends could endanger their original social missions (DIAZ, 2002); on the other hand, other authors contest the sustainability of social enterprises and question their existence independently from substantial public interventions.

In order to address these concerns, one must acknowledge the limits of the traditional definition of **enterprise** and revise it accordingly. Conventional enterprises created and managed for profit maximization have a narrower scope. They can contribute to general well-being only if the markets in which they operate are perfect or almost perfect; in other words, markets must be sufficiently developed to avoid high transaction costs, provided that all agents have the resources needed to purchase the goods and services that can meet their needs. As can easily be ascertained, situations of perfect or at least sufficiently high competition are not as common as is usually stated. Most importantly, they rarely occur for several goods and services, including welfare and, more broadly, general-interest services. Depending on the specific case,

these services cannot be provided by for-profit enterprises for at least three reasons.

- First, the existence of non-paying demand, i.e., people who typically have fundamental needs but are unable to earn the money required to purchase the goods and services that they require at market prices.
- Second, there are situations of market power due to monopoly or quasi-monopoly in which competition is limited and one or a few enterprises can influence price levels, to the disadvantage of users or to their difficulty in assessing the true quality of the services supplied. Given the lack of appropriate information, it is impossible to agree and verify, ahead of time, important characteristics of the service *ex post*; hence, it is unfeasible to assess the correspondence between the price of the service and its utility or value.
- Third, difficulties or the impossibility of preventing part of the value produced by the enterprise from turning into positive externalities, namely benefits for non-paying users. This undermines the possibility of achieving profit margins attractive to for-profit entrepreneurs.

When goods and services are influenced by one or more of these limitations, the production and exchanges carried out by conventional enterprises turn out to be insufficient, with respect to either the quantity or the quality of needs. As a result, part of the population will unavoidably be left unsatisfied. According to mainstream economic theory, public authorities can solve these problems by regulating markets and enterprises; redistributing resources to the advantage of those who would not otherwise be able to satisfy their needs; or arranging for the direct production of services by public agencies.

These strategies, however, have proved to be increasingly ineffective. Over the last three decades, public interventions have been increasingly unable to confront all these problems. Over the same period, social enterprises have autonomously emerged as an alternative player. Their development *per se* confirms the shortcomings of the dominant interpretation.

Consequently, a different interpretation of the enterprise and its functioning is required to understand the rationale of social enterprises. This new interpretation must be based on a more in-depth analysis of both human behavior and the role of enterprises. In contrast to the claims of conventional economic theory, individuals make their own decisions — including those related to production, work, and consumption — not simply to obtain maximum individual advantage, but with a plurality of motivations, including intrinsic ones (the interest in the action *per se*) and social ones (the interest in other people's well-being). Concerning the role of enterprises, their scope ought to be enlarged and they should be conceptualized as institutional mechanisms coordinating the activity of a plurality of

stakeholders, whose aim is to solve a specific problem, usually of a collective nature, through the continuous production of goods or services.

Bridging both interpretations, a successful enterprise does not necessarily have to maximize profit; generally, it aims to coordinate individuals driven by different motivations. As a result, the enterprise will tend to structure itself as an incentive mix that can succeed in attracting various human and financial resources. The resources attracted contribute to achieving the goal set, although they do not exclusively benefit the owners.

By looking into the definition in greater depth, one finds that any enterprise must fulfill two conditions: it has to produce goods or services that satisfy human needs and it has to breakeven, thereby ensuring a *minimum* of financial autonomy and guaranteeing its long-term survival. While it is true that all enterprises must fulfill both social needs and economic and financial sustainability constraints, the two conditions can be combined and met to varying extents by different types of enterprises. Thus, one can define a *continuum* of organizational behaviors and objectives, as shown in Figure below (BORZAGA, DEPEDRI, and TORTIA, 2010). At one end of this *continuum*, economic and financial objectives predominate and the social aim is simply a constraint. At the other end, general-interest objectives predominate, and financial and economic aims represent constraints.

The left-hand end of the *continuum* identifies the classic model of the for-profit firm, exclusively devoted to profit maximization (i.e., maximizing its long-term guarantee of survival) and limited in its activity and management by the constraint of satisfying local demand. Yet it represents only one possible rationale for the creation of entrepreneurial ventures and it does not necessarily apply to all enterprises.

The opposite end of the *continuum*<sup>(2)</sup> identifies pure social enterprises. Their activity is entirely devoted to public-benefit objectives, while financial and economic equilibrium is merely a means to this end. The financial and economic equilibrium is ensured by attracting resources from a variety

of sources, including public agencies, the market, donors and volunteers. These constraints help to ensure the long-term efficiency of the enterprise and do not conflict with the non-profit nature of the firm. Profits are in fact accumulated to lock in assets for future members and users, with an intergenerational social benefit.

A variety of types of enterprise falls between the two extremes, such as the cooperative enterprises, which promote the interests of specific categories of stakeholders.

The positioning of social enterprises and the individuation of heterogeneous aims of organizations explain the diverse governance and management structures of these organizations. Specifically, the prevalence of social over self-interested aims explains why social enterprises have distinctive control and governance mechanisms, characterized by democracy and fair treatment. Furthermore, social goals also include the well-being of employees and require all stakeholders to share the organizational mission. This inter-relation with stakeholders explains the endeavor to involve people and emphasize their non-monetary motivations. Inclusion and the sharing of common procedures may be juxtaposed with hierarchy, control, and the use of powerful monetary incentives as coordination mechanisms.

One can therefore conclude that, for all the types of organization considered, especially social enterprises, organizational objectives and control rights condition the features of the production process. For example, they may influence how information circulates, how knowledge is created and used, and how competences and human capital are accrued and retained (HODGSON, 1998). In social enterprises, reduced hierarchy and control favor the circulation of information that sustains the creation and spread of non-coded and tacit knowledge. This system of knowledge production is supported by the development of more informal and horizontal models of governance in which trust and personal interaction play a more fundamental role than they do in other organizational forms (FREY and OSTERLOH, 1999).



**Organizational Objectives and the Satisfaction of Needs**

Against this backdrop, one can propose a more compelling interpretation of the social enterprise. It can be regarded as an incentive structure that is consistent with the goal of producing goods or services to the advantage of the community (a **common good**) or of a group of citizens. Through the consistent coordination of goals, ownership structure and constraints, this incentive structure helps to overcome problems generated by monopolistic action and the insufficient or asymmetric distribution of information. Indeed, given the impossibility of distributing profits to the owners and the fact that social enterprises are often managed by users, social enterprises are not interested in exploiting market power or information advantages to achieve a higher profit. At the same time, they stimulate the involvement of stakeholders with social or preferences that concern others. These include workers that commit to the enterprises goal and accept lower remuneration relative to that of conventional enterprises, and funders that are happy to get remuneration of capital below the market cost of capital. Consequently, social enterprises can also distribute part of the product to users who do lack the funds to purchase goods and services at market prices, but who are not acknowledged as needy people by the public administration. In these cases, social enterprises, as compared to for-profit enterprises, stand out for their **distributive** natures (BACCHIEGA and BORZAGA, 2003), because they manage to combine the production function with that of voluntary and systematic distribution of part of the value produced to people who would not otherwise be able to satisfy their needs. Although they are private-sector entities, social enterprises fulfill functions traditionally ascribed to public authorities. At the same time, they are also more flexible in activating responses and addressing the new needs of small groups of citizens.

This approach to interpreting social enterprises challenges conventional assumptions that are mainly centered on the action of private-sector enterprises and the State. These assumptions regard private-sector enterprises as being responsible only for the production and allocation of private goods (because they promote the interests of producers) and the State, and only marginally nonprofit organizations, as responsible for redistributing the income generated. However, production and distribution that benefit marginal groups can both be managed by social enterprises. Acknowledging the existence of social enterprises implies that private citizens should not simply be regarded as philanthropists that can use part of their income to the advantage of third parties; they can also organize enterprises that perform totally or partially in the market, and that consequently operate according to allocation rationales other than equivalence.

## 7. POSITIONING SOCIAL ENTERPRISES

Realizing that social enterprises are a new form of enterprise driven by different motivations also helps one to understand their positioning in societies and in economies.

First, one can say that social enterprises are categorically different from other types of enterprises and organizations. They differ from public enterprises because they are managed by private-sector entities according to an entrepreneurial logic. They differ from conventional for-profit enterprises because they are characterized by goals, ownership assets, constraints, and types of governance that exclude the maximization of owners' monetary advantages. They also differ from traditional cooperatives, which are owned by non-investors and which aim primarily to promote the interests of their owners. Nevertheless, social enterprises are close to cooperatives in terms of assets ownership, democratic governance structure, and common origins. This explains why social enterprises often decide to adopt cooperative forms.

Social enterprises are not expected to replace existing institutions such as conventional enterprises, traditional nonprofit organizations and public agencies. Instead, they should be seen as additional players that strongly contribute to innovation from at least two standpoints. First, the development of social enterprise initiatives calls into question conventional economic paradigms, including the traditional interpretation of the enterprise, and paves the way for new theoretical explanations of economic behavior. Second, the experience of social enterprises corroborates that activities traditionally characterized by redistributive goals can be managed according to entrepreneurial modalities.

## 8. ADVANTAGES AND LIMITS OF SOCIAL ENTERPRISES

Social enterprises pay particular attention to social and interactional dynamics. When relating to their different stakeholders, they tend to base their exchanges on relationships rather than on market dynamics. While for-profit firms typically relate to their stakeholders through market transactions, based on price exchanges, social enterprises rely on personal transactions with all their stakeholders. Trust, relationships, knowledge, information and involvement are the keywords of these transactions. Moreover, social enterprises are by definition more closely embedded in the local community; they enhance cooperative behaviors among stakeholders, and enjoy a higher reputation in the community. These traits are particularly important for three elements at least: the achievement of the organizational goal, the economic efficiency of the organization, and the production of externalities and the increased well-being of the society.

Concerning the organizational mission, one can demonstrate that the governance structure of social enterprises allows for the achievement of higher social goals. These organizations usually involve in their membership heterogeneous local stakeholders, mainly volunteers and users other than workers. This governance structure facilitates the provision of community services, since the members of social enterprises aim to satisfy



localized needs, which have idiosyncratic features linked to a specific community and may not be satisfied in the same way in other contexts. Furthermore, by enhancing the well-being of marginal classes of citizens, social enterprises reduce negative spillovers. Negative social effects linked to poverty and marginality can be mitigated by the ability of social enterprises to solve social dilemmas within their boundaries without resorting to imperfect and often unusable contractual relations, which would inflate transaction costs, limit the circulation of information, and exacerbate contrasting interests. Inclusive and multi-stakeholder governance serves the purpose of coordinating the various participants in solving social dilemmas. This is possible when the motivations of the players involved interact proactively with public-benefit objectives (BORZAGA and TORTIA, 2009). Furthermore, governance structure and social aim guarantee better alignment of services and clients' needs, besides preventing the inefficiencies of other types of organization, especially public agencies, because they are less bureaucratic and more flexible.

A second advantage typical of social enterprises is their ability to reduce inefficiencies and transaction costs with internal agents, from users to donors, from volunteers to workers (DEPEDRI, 2010). In general, these enterprises increase non-self-interested behaviors and cooperation among peer members, as well as the sharing of rules and sanctions, which are fundamental elements for the management of common resources in a self-organized manner (OSTROM, 1994). Specifically, the strength of the relationships among the various stakeholders provides social enterprises with several direct advantages in the management of exchanges with their constituent parties. Self-regarding preferences and opportunistic behavior that usually hinder organizational performance and the achievement of the organization's goals are drastically reduced in social enterprises, through the implementation of self-managed organizational processes.

Reducing opportunistic behavior and sharing the organization's goals are particularly important, especially in exchanges with clients. Social enterprises tend to build their reputations through fair communication and stakeholder participation. Therefore, clients' sense of trust and reputation vis-a-vis social enterprises are enhanced, with advantages for both the organization, which gets complete and symmetric information on users' preferences, and the said users, who are better satisfied with the organizational services. This positive outcome is further improved in social enterprises by their higher degree of innovation and the elasticity of supply.

Similar dynamics also concern relations with donors and volunteers: the reduction of self-interested behaviors in social enterprises, due to the organizational mission, the multi-stakeholder governance and the embedding of the organization in the territory, functions as a guarantee for people willing to donate time or funds. This allows social enterprises to gather new resources from the local society to a greater extent than other organizations.

However, the main advantage of the non-opportunistic behavior of social enterprises concerns the management of its employees. Several studies have shown that three features characterize social enterprises: the ability to select altruistic and intrinsically motivated employees; the use of incentives other than standard economic rewards; and the presence of managers who internalize the social aim of the organization (LEETE, 2000; BENZ, 2005; BORZAGA and DEPEDRI, 2005). To attract people that are intrinsically motivated and interested in the social dimension of the job, social enterprises first tend to offer wages lower than the market level, which therefore exclude applications from indifferent employees and managers, drawing only dedicated people (HANDY and KATZ, 1998). Moreover, social enterprises tend to offer their workers a mix of incentives, the monetary remuneration working only as a threshold that can induce workers to accept or refuse employment, whereas their interest in the activity, the sharing of values and the psychological ownership of the organization determine the job satisfaction, employees' effort and workers' creativity (MIRVIS and HACKETT, 1983; MICHIE and SHEEHAN, 1999; BORZAGA and DEPEDRI, 2005). Finally, the work environment (relations with colleagues and internal social norms), the other employees (mainly intrinsically motivated people) and managers (especially attentive to employee involvement, fairness, democracy and communication) improve the **group sense** linked to the social dimension of the activity, causing people to internalize the organization's mission in a process of integrated regulation (GAGNÉ and DECI, 2005). As already stated, these behaviors and dynamics generate advantages both for the employees, in the form of high job satisfaction (e.g. BORZAGA and DEPEDRI, 2009), and for the social enterprises, in the form of lower control costs and staff turnover (e.g., ALMOND and KENDALL 2001; BORZAGA and TORTIA, 2006), while leading to better performance (e.g. PRESTON, 1989).

Thanks to all of these improved relations with their stakeholders, social enterprises seem to be managed and designed to encourage innovation in the organizational and production domains, when it comes to new services and new organizational solutions. Differences in the inputs used and in the outcomes achieved support the efficiency of these organizations and hence their ability to respect financial constraints and to pursue their long-term existence. Three main factors specifically improve output. First, the services produced by social enterprises tend to be more flexible and innovative, and can satisfy a greater number of users and a larger share of local needs. Second, the employees of social enterprises strive harder and ensure production stability, despite their often lower wages. Third, the mobilization of local resources and the transmission of social standards to the community (specifically to agents belonging to the community) create a virtuous circle: they enhance relationships, increase cooperation and trust, disseminate knowledge and ideals, and reduce the opportunism of the people involved. Specifically regarding inputs, social enterprises seem to have four main advantages in achiev-

ing cost savings. First, they benefit from free resources and enjoy advantages in obtaining funding in the market. Second, they benefit from lower transaction costs (e.g. in the collection and transmission of information) and waste fewer resources (e.g. thanks to less bureaucracy and greater flexibility). Third, they incur lower costs in controlling the performance of managers and employees by using control and penalty mechanisms that differ from those employed by other types of organization. Fourth, when compared to other types of organization, the mix of incentives provided to employees by social enterprises is less expensive. Thus, in theory, efficiency seems to be sustainable for social enterprises in terms of an input-saving and or output-increasing analysis.

Finally, it one should mention that social enterprises not only enable better relations with their stakeholders, but also leverage the effects of welfare by their productive activity. The allocation and distribution mechanisms of social enterprises are unique and well adapted to increasing the production of socially beneficial goods and to reducing poverty (TORTIA, 2010). Moreover, they seem to produce higher levels of positive externalities: they raise local well-being, enhance the production of social capital, and solve marginalization issues. Concerning local economic development, they help to improve the employment level by also offering work to those who are disadvantaged in the job market. As for social capital, social enterprises promote voluntary work, enhance the dissemination of knowledge and social norms within the community, spread trust and cooperation, and strengthen relations and social cohesion. Finally, relations with the local community strengthen

fairness principles, collective actions, and altruistic behavior, which also have an impact on the social marginalization of users and of the disadvantaged workers of social enterprises.

## 9. CONCLUSIONS

Social enterprises constitute a new, complex and multi-sided phenomenon that is still difficult to interpret. However, one can understand their characteristics, specificities and behavior better when they are regarded as mechanisms through which a group of people can autonomously manage production activities that benefit the entire community or groups of disadvantaged people. This approach can explain why these enterprises have developed so quickly and will continue to spread. Moreover, it provides insights into the specific conditions under which social enterprises develop, especially in a historical stage when it is increasingly evident that for-profit enterprises that focus primarily on short-term profit maximization and public authorities are unable to keep pace with the escalating needs.

This brief interpretation of social enterprises is not comprehensive and does not consider the broad range of products and services that they can provide. However, the identification of salient issues can help to determine strategies, contractual relations, membership, and policies for recruiting and incentivizing investors and employees. It can also help to define appropriate public policies and legislative frameworks, since social enterprises can only thrive if their distinctive ownership and governance mechanisms are suitably acknowledged and exploited. ♦

## NOTES

- (1) With a distinction between social cooperatives providing social assistance, health and educational services and those that aim to integrate disadvantaged people into the work environment.
- (2) A wide variety of intermediate firm types exists be-

tween the two extremes of the *continuum*. The most common of these are cooperatives, which are explicitly mutual-benefit organizations, since their primary objective is to satisfy the needs of a group of members that control the organization by virtue of individual rights, not ownership of capital shares.

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## ABSTRACT

**Interpreting social enterprises**

Institutional and organizational variety is increasingly characterizing advanced economic systems. While traditional economic theories have focused almost exclusively on profit-maximizing (i.e., for-profit) enterprises and on publicly-owned organizations, the increasing relevance of non-profit organizations, and especially of social enterprises, requires scientists to reflect on a new comprehensive economic approach for explaining this organizational variety. This paper examines the main limitations of the orthodox and institutional theories and asserts the need for creating and testing a new theoretical framework, which considers the way in which diverse enterprises pursue their goals, the diverse motivations driving actors and organizations, and the different learning patterns and routines within organizations. The new analytical framework proposed in the paper draws upon recent developments in the theories of the firm, mainly of an evolutionary and behavioral kind. The firm is interpreted as a coordination mechanism of economic activity, and one whose objectives need not coincide with profit maximization. On the other hand, economic agents driven by motivational complexity and intrinsic, non-monetary motivation play a crucial role in forming firm activity over and above purely monetary and financial objectives. The new framework is thought to be particularly suitable to correctly interpret the emergence and role of nontraditional organizational and ownership forms that are not driven by the profit motive (non-profit organizations), mainly recognized in the legal forms of cooperative firms, non-profit organizations and social enterprises. A continuum of organizational forms ranging from profit making activities to public benefit activities, and encompassing mutual benefit organizations as its core constituent, is envisaged and discussed.

**Keywords:** organizational variety, evolutionary economics, behavioral economics, non-pecuniary motivations, private benefit, mutual benefit, public benefit.

## RESUMEN

**La comprensión de los negocios sociales**

La variedad de instituciones y organizaciones caracteriza, cada vez más, sistemas económicos avanzados. Al paso que las teorías económicas tradicionales enfocaban casi exclusivamente organizaciones maximizadoras de lucros (o sea, empresas generadoras de lucro) y organizaciones gubernamentales, la creciente relevancia de las organizaciones sin fines lucrativos y particularmente de las organizaciones sociales exige de los científicos reflexiones sobre un nuevo abordaje económico amplio, capaz de explicar tal variedad organizacional. Este artículo examina las principales limitaciones de las teorías ortodoxas e institucionales y reafirma la necesidad de crear y probar un nuevo marco teórico, que tome en cuenta las formas variadas empleadas por las diversas organizaciones en la persecución de sus objetivos, las variadas motivaciones que impelen a los actores y a las organizaciones, y los diferentes estándares de aprendizaje y rutinas dentro de las organizaciones. El nuevo marco analítico aquí propuesto se basa en desarrollos recientes, principalmente evolutivos y comportamentales, en la teorías de la empresa, que pasa a ser interpretada como un mecanismo de coordinación de la actividad económica cuyos objetivos no coinciden forzosamente con la maximización de lucros. Al contrario, los agentes económicos son movidos por una complejidad de motivaciones y una voluntad intrínseca y no monetaria de desempeñar un papel crucial en la formación de las actividades de la empresa que trascienden los objetivos puramente monetarios o financieros. Se considera que el nuevo marco sea particularmente apropiado para la correcta interpretación del surgimiento y del papel de formas organizacionales y de propiedad no tradicionales, que no son movidas por la busca de lucros (organizaciones sin fines lucrativos) y que son reconocidas principalmente en los formatos legales de las cooperativas, ONG y empresas sociales. Este artículo considera y discute una gama de formas organizacionales que van desde actividades generadoras de lucro hasta actividades dirigidas al bien público y que engloban organizaciones de beneficio mutuo como su principal constituyente.

**Palabras clave:** variedad organizacional, economía evolucionaria, economía comportamental, motivaciones no-pecuniarias, beneficio privado, beneficio mutuo, beneficio público.