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Part 1: Overview of Social Enterprises
Overview of Social Enterprises

There is no special legal definition of ‘social enterprise’, although there are some working definitions used in Australia. Social enterprises can be ‘for-profit’ or ‘not-for-profit’. The key feature they share is the running of an enterprise to achieve an economic, social, cultural or environmental mission that benefits the public or a particular community.

The key defining characteristic of a social enterprise, is a trading enterprise that uses its revenue or business model to further a community or public purpose. Some social enterprises look like normal businesses, offering products or services, and directing profits to a cause. Others operate with their mission embedded throughout their business model, such as by employing underemployed populations, or taking special environmental approaches to producing products, and then using profits to further support their mission. The definition of social enterprise is discussed further below.

Social enterprises can be large or small. Although the term social enterprise is being used more in the public lately, there are lots of Australian organisations that have been running social enterprises for years, like op shops and indigenous community enterprises.

Social enterprises worldwide are becoming increasingly sophisticated and social entrepreneurs now have more options than ever before for setting up and structuring a social enterprise, or adding a trading element to an existing not-for-profit organisation.

An example of a social enterprise

A social enterprise operates to achieve an economic, social, cultural or environmental mission

A social enterprise trades, or operates some sort of business

Social enterprises in Australia can be for-profit or not-for-profit, or even a hybrid of both. There may be benefits and downsides to both for-profit and not-for-profit structures, which can mean organisations create a hybrid structure to access certain advantages whilst avoiding certain downsides. Structuring options are discussed in more depth in part 3 of this guide.
What is the definition of social enterprise?

The social enterprise sector is wide and complex, and the meaning of social enterprise is contested, both in Australia and overseas.

While there is no legal definition of social enterprise, there are non-legal definitions of ‘social enterprise’ that have been created for particular purposes. One that is often referred to in Australia is the definition used by Social Traders and in the Finding Australia’s Social Enterprises Sector (FASES) project work (run by Social Traders, Swinburne University and the Centre for Social Impact).

The Social Traders definition is helpful, and may be used or required by some funders. There is some debate that any business reinvesting profits towards a purpose should be able to be considered a social enterprise, regardless of the proportion of that reinvestment. There is also some debate about whether the business activities of a social enterprise should in and of themselves, create impact (for example, by employing underemployed communities, or contributing to environmental sustainability).

The Social Traders definition of social enterprise

Social enterprises are organisations that:

• are led by an economic, social, cultural, or environmental mission consistent with a public or community benefit
• trade to fulfil their mission
• derive a substantial portion of their income from trade, and
• reinvest the majority of their profit or surplus in the fulfilment of their mission

Read more about Social Trader’s discussion of this definition on their website.

Some other jurisdictions, including the United Kingdom and the United States of America, have created special corporate structures that can be used by social enterprises. They are called ‘Community Interest Companies’ in the UK, and ‘Benefit Corporations’ as well as ‘Low-profit Limited Liability Corporation’ in the USA. In these jurisdictions, social enterprises don’t have to use these structures to be considered a social enterprise. The structures are discussed further at the end of part 3 of this guide. There is no special structure in Australia.

There are also a range of social enterprise certifications available around the world. These are private certifications earned when an organisation meets the criteria of the certifying body (similar to ‘organic’ or ‘fair trade’ certifications).

There are certifications that can be awarded to Australian businesses, such as the B Corp certification awarded by B Lab, which is available to for-profit businesses including social enterprises. To be certified as B Corp, an organisation must meet B Lab’s standards of social and environmental performance, transparency and accountability, and meet certain legal criteria. To be clear, a certification as a B Corp is not the same thing as being a benefit corporation, which refers to a special legal structure, rather than certification.
Part 2: Important factors to consider when starting a social enterprise
Important factors to consider when starting a social enterprise

This section covers key considerations when setting up including:

► preliminary questions to consider
► whether a social enterprise should incorporate
► deciding between not-for-profit and for-profit, and
► whether a social enterprise should consider becoming a charity

Many groups and entrepreneurs are considering setting up social enterprises or adding a social enterprise to an existing organisation. When getting started, there are some very important legal decisions that groups need to make. Getting them right from the start will save you time, effort and fees down the track. This part of the guide will direct you towards the key issues you need to consider at the initial stages of starting up a social enterprise.

Preliminary questions

Before you start setting up your social enterprise, it’s a good idea to think carefully about what you want your social enterprise to look like, what issue you are trying to address, and what approach you should take to address that issue.

Some questions to consider are:

• Can you clearly describe the particular social, community or environmental mission of your enterprise? Could your mission be considered charitable (it doesn’t have to be, but this may impact your access to tax concessions)?
• What issue are you trying to address? How will your social enterprise contribute to resolving that issue?
• Who will you need to work with? Who should you engage in designing your social enterprises? The people you are trying to help? The people who might help fund your enterprise?
• Is anyone else working to resolve the issue? If yes:
  – What can we learn from them?
  – Should we join them?
  – Where is the issue? Is it within one state, or is it across multiple states or territories? Where will the enterprise operate?
• Is anyone else already doing something similar? It there room or need for another social enterprise in the space?
• Where will your funding come from? Will you seek to access philanthropic grants? Do you want to attract investors? Will you be community-owned?
• Who will oversee the enterprise and its operations? Will your enterprise have staff? Will your enterprise have ‘owners’ or ‘members’?
• If you will have shareholders, will they be a small group of people connected to you, or will you run public campaigns to find lots of shareholders?
We recommend that you consider these questions now and then again after reading this guide. Understanding the implications of the law on the operations of a social enterprise may change your views about how you will set up, operate, and fund your social enterprise.

If the details and practicalities of your idea are still unclear in your mind, you may find it beneficial to talk to someone about your idea, or join a program that helps social enterprises get started, such as the CRUNCH program, which is run by Social Traders, or the coaching provided by Social Enterprises Sydney to groups in Western Sydney.

### Business Plan

A business plan is essential for setting up a successful social enterprise, and is often a critical tool when convincing funders or investors to support your project. If you already have a business plan, you might want to revisit it after you have finished reading this guide, once you have considered all the legal issues involved.

Your business plan should be settled before you incorporate, because it will help you to make an informed decision about your legal structure. It’s time-consuming and expensive to change legal structures down the track and (and in some cases, it can be very difficult to change at all, for example it is very hard to change from being a charity to being a for-profit), so it is worth putting thought and effort in at the start to set yourself up for success.

Business plans can be difficult to draft, however they are very helpful for making decisions, getting funding and staying on track as you progress setting up your social enterprise.
Measuring your impact

As well as having a business plan, your enterprise will need to be able to demonstrate the impact that it is making through its work towards its mission or purpose. Increasingly, investors and funders want to see clear articulation of how you are planning to measure and evaluate your impact, and may require you to report to them on your impact.

Measuring impact is not an easy undertaking, but again, having a plan from the start can be critical to success. For example, will you measure baselines when your operation starts so that you can measure the change that you have made down the track? Will you have the right data monitoring practices in place from the start? Have you considered privacy law implications of data tracking and reporting?

There are an increasing range of resources on impact measurement that are publicly available, as well as a growing number of professional groups working in the area, including:

- Social Impact Measurement Network Australia
- Centre for Social Impact – see the Compass Guide to Impact Measurement
- Emma Tomkinson’s (a social impact analyst) resources

Measuring impact is especially important for some kinds of impact investing (discussed further below) such as social impact bonds.

Funding your organisation

Identifying sources of funding for your organisation is crucial when creating your business model, and deciding whether your organisation will be for-profit or not-for-profit will directly affect the sources of funding available to your organisation. For example, only for-profit organisations can be funded by equity purchased by investors; and only not-for-profit organisations that are endorsed as deductible gift recipients can seek tax deductible gifts. Most philanthropic grants are only available to not-for-profit organisations (and more specifically many philanthropic grants are only available to charities or even more narrowly only to...
deductible gift recipients – there is a discussion of the difference between not-for-profit, charity and deductible gift recipient below).

The complexity of the funding sources your organisation chooses to utilise will often depend on your organisation’s specific arrangements or circumstances. The table on the next page is intended to be a brief, generic summary of the funding sources (or sources of capital) available to social enterprises. As you will see, some funding sources are only available to for-profits or not-for-profits, and this can have a significant influence on your choice of legal structure.

**Impact Investment**

Impact investment is a growing field in Australia. It refers to methods for funding social or environmental projects that will provide the investor with both an impact and a financial return. It is an alternative to grant funding in many cases, and for funders, it is attractive as the same money can be used over and over to fund social projects. Of course, not all social or environment projects can generate a financial return, however social enterprises are likely to be engaged in activities that both contribute an impact and generate income. You can read more about impact investing at Impact Investing Australia, an organisation advocating for increased impact investing activities in Australia.

Different types of impact investing approaches are illustrated in the middle of the funding spectrum below (although there are other more complex funding arrangements, such as bonds and notes, beyond this spectrum).

### Different types of impact investing approaches

- **Grants and donations**
  - Purpose first – social or environment outcome sought, no financial return to provider of funds

- **Low interest loans**
  - Social or environmental outcome as well as financial return

- **Impact investment through share purchase**
  - Finance first (or only), no concern for social or environmental outcomes, although increasing number of investment funds applying ethical screening to investments

- **Commercial loans**

- **Commercial investment through share purchase**

There are many forms that impact investing can take, from low-interest loans through to the purchase of shares (equity) in a for-profit social enterprise. Many impact investors are interested in investing in social enterprises, as they see potential for the delivery of both financial return through trading activities, and the achievement of social or environmental impact through the work of the enterprise.

Some examples of social enterprises that have received impact investments include STREAT (see case study below), Hepburn Community Wind, Women’s Property Initiative, Goodcycles, Goodstart Early Learning, Who Gives A Crap, and the Yackandandah Community Development Company. The availability of the different types of impact investing approaches to your social enterprise will depend on its legal structure.
Table of funding sources and structures

<table>
<thead>
<tr>
<th>Funding sources</th>
<th>Eligible or suitable entities</th>
<th>Level of Complexity</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>For profit</td>
<td>Not-for-profit</td>
</tr>
<tr>
<td>Equity (ordinary, or impact investment or crowd sourced investors)</td>
<td>✓</td>
<td>×</td>
</tr>
<tr>
<td>Debt (commercial, through impact investing, owner loans or philanthropists)</td>
<td>✓</td>
<td>✓ (owner-loans not possible)</td>
</tr>
<tr>
<td>Donations (deductible by the donor)</td>
<td>× (with some exceptions)</td>
<td>✓</td>
</tr>
<tr>
<td>Grants (from charitable trusts, philanthropic foundations, corporate foundations, individual granting programs or giving circles)</td>
<td>× (with some exceptions, for example small business grants, or social enterprise grants from corporate foundations or philanthropists)</td>
<td>✓ (note that many philanthropic foundations can only provide grants to not-for-profits that are also endorsed as a deductible gift recipient, Item 1)</td>
</tr>
<tr>
<td>Social Investment Bonds (usually government-led)</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Crowd Funding (can be through donations or through pre-purchases)</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Micro donations (with some exceptions)</td>
<td>× (with some exceptions)</td>
<td>✓</td>
</tr>
<tr>
<td>Membership (as distinct from shareholders) fees</td>
<td>× (with some exceptions)</td>
<td>✓</td>
</tr>
</tbody>
</table>
Should you incorporate?

Is it necessary to incorporate a new entity for our social enterprise?

Before you decide to incorporate a new structure for your enterprise, it’s a good idea to test the assumption that you need to set up and operate an incorporated entity to achieve your goals. Some options that don’t require setting up a whole new organisation are discussed below.

- **Run the enterprise out of your existing organisation**: if you are an existing organisation that wants to set up a new social enterprise as part of your organisation, you may not need to set up a new structure. Some organisations operate a business from within their existing structure. Whether you set up a new structure will depend on whether your current structure can accommodate the type of funding arrangements you are interested in, and also on whether your new business might expose your existing organisation to risks, in which case it would be more appropriate to put the business in a new and separate structure (which can be wholly owned by the existing organisation).

- **Continue unincorporated**: If you are a start-up, it may be possible to conduct your activities without incorporating. However, there are some particular and important benefits that flow from incorporating, for example: limited liability for members and shareholders, the ability for the incorporated body to enter into agreements in its own name, and the preference of many funders for organisations to be incorporated, and tricky issues raised by shared unincorporated ownership of businesses such as partnership laws.
• **Join another organisation:** Is there an existing organisation whose purposes and aims are consistent with yours? If there is, it might be a good idea to investigate joining that organisation, presenting your idea to the organisation, or teaming up in some other way to work together. Some organisations will consider proposals for new projects, or may be willing to employ you to run a new project within their organisation. Rather than starting an organisation from scratch, it can be more efficient to run your idea within an existing organisation, as you can benefit from their existing infrastructure (such as premises, payroll, insurance, financial staff).

• **Auspicing:** Some not-for-profit organisations are willing to auspice projects, such as social enterprises that are in the pilot, or incubation stage. This normally involves an auspicing agreement between your group and the auspicing body. An auspice agreement is basically an agreement to work in, or under the auspices of, another organisation, and a way for an organisation to access funding without being incorporated or without satisfying grant criteria (such as holding certain insurance). Under an auspicing agreement, one organisation (the principal organisation) agrees to apply for funding for another person or group (the auspicee), and if the funding is received, the principal organisation receives, holds, and disperses the funding to the auspicee for their project. Before approaching another organisation to auspice your project, you should carefully consider a number of important issues, including checking that the principal organisation’s purposes are consistent with yours, and that the funding options that you think best suit your project can be accessed and administered by that organisation (for example, do they have the right tax endorsements).

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**Related Not-for-profit Law resource**

For more information, go to the Not-for-profit Law webpage which discusses the incorporation decision.

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**Related Not-for-profit Law resource**

For more information about auspicing or joining another organisation, read the part of our website which discusses working with other organisations.

For a detailed list of issues you should consider before considering an auspice arrangement, see Not-for-profit Law’s resources on agreements.

---

**Note**

Only some organisations are willing to auspice projects.

Many philanthropic organisations won’t allow auspice arrangements, and organisations that are willing to auspice often charge an administrative fee.
If incorporating, should we choose to be for-profit or not-for-profit?

In this section we have summarised the key legal issues you should consider when choosing between incorporating as a for-profit or not-for-profit entity. Choosing which legal structure to adopt for your social enterprise is the most important decision you will make when getting started, and whether you are not-for-profit, for-profit, or a hybrid of the two, will significantly impact the way you can run and fund your enterprise.

Importantly, the legal structure you choose will affect:

• the sources of funding available to your social enterprise, and whether or not your enterprise can attract ‘investors’ for funding. For this reason, your business model will strongly impact your choice of structure

• the tax concessions your social enterprise is eligible for

• ongoing reporting and governance requirements you must meet, and

• whether or not your social enterprise can be registered as a charity

Factors influencing the not-for-profit vs for-profit decision

When thinking about what structure is appropriate for your organisation, we recommend that you consider the following questions, which will help you to apply the information in this guide.

<table>
<thead>
<tr>
<th>Question</th>
<th>Relevance</th>
</tr>
</thead>
<tbody>
<tr>
<td>Where will your funding come from?</td>
<td>Donations and philanthropic funding can generally only be directed to not-for-profits. For-profit entities can seek investors to raise funds. Similarly, not-for-profits can also seek investors to raise funds through impact investment but this can be more complex, and often results in debt.</td>
</tr>
<tr>
<td>Where do you want profits to go?</td>
<td>A fundamental characteristic of not-for-profit organisations is that profits are not distributed outside of the organisation – which means no dividends or distributions can be made, and all profits are directed to achieving the organisation’s mission. In a for-profit organisation, profits are often distributed to shareholders or investors. In a for-profit social enterprise, profits are normally partially distributed to investors and partially reinvested into the organisation.</td>
</tr>
<tr>
<td>Is it important for your enterprise to be perceived as not-for-profit?</td>
<td>Public perception may inform your choice of structure.</td>
</tr>
<tr>
<td>Do you want investors or owners or members?</td>
<td>Some structures have investors and/or owners, some have members; these are not the same.</td>
</tr>
<tr>
<td>Does your organisation hope to access charitable and other tax concessions?</td>
<td>Some structures have investors and/or owners, some have members; these are not the same.</td>
</tr>
</tbody>
</table>

Hybrid Structures

Hybrid structures are a use of two (sometimes more) entities to form one social enterprise. Quite often, none of the legal structures discussed in this guide are a perfect fit for a social enterprise. For example, you may want to choose a private company structure so you can have access to equity funding from socially minded investors, but will be undertaking certain activities that are charitable and you would like to access income tax exemptions for your charitable activities. Or, you may want a not-for-profit structure, but have a particular project that could attract investors.

Hybrid structures can be useful to harness the benefits of both for-profit and not-for-profit structures by:

• expanding funding avenues that might not be available to a singular corporate structure (for example, equity is not available to a not-for-profit structure such as an incorporated association)
• limiting the exposure of a charity to liabilities of trading activity by creating a for-profit subsidiary that trades and owns property, or
• enabling an enterprise to separate its activities, to obtain charity, or even DGR status for parts of its activities, which may not have been possible if the enterprise was a singular corporate structure (this benefit is achieved if each element of the hybrid has separate governing documents)

Hybrid structures are discussed in more detail in part 3 of this guide.

Case study

STREAT Ltd is a Melbourne-based not-for-profit social enterprise that operates café businesses and employs young homeless Australians. In 2012, STREAT bought two cafes and a coffee roasting business from another social enterprise. In doing so, it changed its legal structure to form a hybrid model, which involved both a private company and a not-for-profit entity.

In preparation for buying the cafes and coffee roasting business, STREAT formed STREAT Enterprises Pty Ltd, a private company. STREAT Enterprises would directly own the cafes and coffee roasting business, and all the enterprise’s trading would be done through STREAT Enterprises. The purchase would be financed by selling 50% of the shares in STREAT Enterprises to investors to raise funds. STREAT Ltd would own the other 50%.

STREAT initially operated as a not-for-profit social enterprise entity. However potential to receive equity investment led to the need to add a for-profit arm to the organisation:

This hybrid structure was beneficial for STREAT for three main reasons:
• it enabled STREAT Ltd to remain a public benevolent institution and keep its DGR status
• it gave STREAT access to significant amounts of funding and more funding opportunities in the future, through the sale of equity in STREAT Enterprises, and
• it transferred liability for trading and ownership of the cafes and coffee roasting business to STREAT Enterprises
Tax concessions and their impact on the 'for-profit vs not-for-profit' decision

Social enterprises need to carefully consider whether the benefits of tax concessions outweigh the restrictions that concessions place on an organisation. The table below sets out which types of organisation are eligible to apply for tax concessions. Most tax concessions are only available to not-for-profit organisations.

Tax concessions can provide a range of benefits, such as allowing donors to claim their donations as a tax deduction, allowing staff to claim certain salary benefits, and reducing income tax for the organisation (discussed further below).

Caution

Tax concessions can place additional administrative and reporting burdens on organisations.

It’s worth noting that many social enterprises are able to operate using a for-profit structure, without accessing tax concessions, and can take advantage of the benefits of being a for-profit, such as attracting investors. A for-profit social enterprise can still receive gifts and donations even if it does not have Deductible Gift Recipient (DGR) endorsement, but cannot undertake charitable fundraising activities unless it is not-for-profit. DGR endorsement can be a requirement for larger donors and grants from trusts and other philanthropic funders because under law they can only give to Item 1 DGR endorsed organisations. Corporations and simple charitable trusts do not have the same restrictions and may be able to grant to for-profit social enterprises. The different tax exemptions are briefly explained below (there are some exceptions to the general positions in the table below).

If you decide to use a not-for-profit structure for your social enterprise, tax exemptions and concessions are an important benefit you should consider. Not all tax exemptions and concessions are available to all not-for-profit organisations - some are only available to charitable organisations registered with the ACNC. DGR endorsement is also only available to certain kinds of organisations (there are particular categories that an organisation needs to fit into to be endorsed as a DGR).

<table>
<thead>
<tr>
<th>Tax Exemption</th>
<th>Eligible organisation</th>
<th>Not-for-profit</th>
<th>For-profit</th>
<th>Charity</th>
</tr>
</thead>
</table>
| (a) Income tax exemptions | • Charities registered with the ACNC and endorsed by the ATO as exempt from income tax  
• Certain community service organisations, cultural, educational, employment, scientific, sporting and health organisations (as specified in the Income Tax Assessment Act)  
• Other categories specified in the Income Tax Assessment Act such as a fund established (by will or trust) in order to contribute to another charitable fund, employee or employer associations, trade unions, promotion of tourism, public health organisations etc. | ✓              | ✓ (very limited) | ✓       |
### (b) GST concessions
- Charities who are registered with the ACNC and endorsed by the ATO as ‘tax concession charities’
- Not-for-profit organisations who have DGR endorsement from the ATO
- Certain other organisations and funds, such as school charitable funds

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<tbody>
<tr>
<td>✓</td>
<td>×</td>
<td>✓</td>
</tr>
</tbody>
</table>

### (c) Fringe benefits tax concessions
- FBT exemptions are available to some NFPs (provided the fringe benefits provided to employees are not more than the relevant cap) eg:
  - Public benevolent institutions
  - Health promotion charities; and
  - Public and non-profit hospitals
- Charities registered with the ACNC and endorsed by the ATO as a charitable institution
- Certain other not-for-profit organisations (subject to the caps):
  - religious, educational, charitable, scientific or public educational institutions
  - that encourage music, art, literature or science
  - that encourage or promote a game, sport or animal race
  - for community service purposes
  - to promote the development of Australian information or resources, or
  - to promote the development of agricultural, pastoral, horticultural, fishing, manufacturing or industrial resources of Australia

<p>| | | |</p>
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<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>✓</td>
<td>×</td>
<td>✓</td>
</tr>
</tbody>
</table>

### (d) DGR endorsement
- Organisations which fall within one of the categories of organisations specified in the *Income Tax Assessment Act* and are endorsed
- Organisations who are specifically listed in the *Income Tax Assessment Act*

<table>
<thead>
<tr>
<th></th>
<th>(only limited types)</th>
<th></th>
<th>(only limited types)</th>
</tr>
</thead>
<tbody>
<tr>
<td>✓</td>
<td>×</td>
<td>✓</td>
<td></td>
</tr>
</tbody>
</table>

The benefits associated with the tax concessions outlined below are summarised as:

- **Income tax exemption**: If your organisation qualifies for income tax exemption, then it will not have to pay any income tax on its taxable income, lodge tax returns, or keep certain complicated financial information, which would usually be necessary to lodge a tax return. Under the *Income Tax Assessment Act 1997* (Cth), for-profit organisations are not exempt from income tax unless their dominant or primary purpose is to promote the advancement of one of the recognised categories of charity or not-for-profit categories

- **GST concessions**: Not-for-profit organisations are required to be registered for GST if the organisation has an annual turnover of more than $150,000. An organisation that is required to be registered for GST is required to pay GST to the ATO if it sells something, and can claim an 'input tax credit' from the ATO
for the amount of GST included in the price of goods and services it purchases. There are various, specific types of GST concessions for the not-for-profit sector

• **Fringe benefits tax concessions:** Generally, fringe benefits tax is payable by an employer on the value of non-salary benefits which are provided to its employees. This tax is usually passed on to the employee by the employer. A rebate is available to eligible not-for-profit organisations

• **Deductible Gift Recipient endorsement:** DGR endorsement is a special kind of tax status allowing people who donate to the organisation to ‘deduct’ those donations from their own income for tax purposes. DGR endorsement also makes an organisation eligible to receive funds from certain grant makers and philanthropic bodies that can only fund DGRs. If your business plan is relying on a significant proportion of your funding coming from philanthropic grants and larger donations from trusts or funders, your organisation should carefully examine whether it is eligible for DGR endorsement

**Note**

Getting DGR endorsement is a complicated and lengthy process. You will probably need a lawyer to assist you.

• **State based tax concessions:** In addition to the federal taxes described above, states also collect separate taxes through the various state revenue offices, such as stamp duty. Your organisation may be eligible for state tax concessions. Eligibility for tax concessions will be based on whether the organization retains profit for its members or not (there are some additional very specific activities which can attract state tax exemptions that are unlikely to be related to a social enterprise such as activities of trade unions)

**Related Not-for-profit Law resources**

Not-for-profit Law has many resources on tax concessions that cover their implications in more detail as well as eligibility requirements and processes for applying. See the part of our Information Hub that discusses tax at www.nfplaw.org.au/tax.

**Should our organisation register as a charity?**

Only not-for-profit organisations can register to become charities (in some very limited circumstances, organisations with traditionally for-profit structures have been able to establish themselves as not-for-profit, for example Pty Ltd structures). Eligible organisations can register as charities with the ACNC. The benefits
of registering as a charity are summarised in the table on the next page. There are some limitations to becoming a charity that are also noted.

According to the ACNC, to register as a charity an eligible organisation must:

- meet the definition of ‘charity’ (an organisation is likely to meet the definition of ‘charity’ if it is not-for-profit, has a charitable purpose, and provides a public benefit)
- have an Australian Business Number
- meet the ACNC governance standards, and
- not be a type of organization that cannot be registered (this include political party, government entity, or an entity engaged in, or supporting terrorist or other criminal activities)

Charitable purpose has a special legal meaning, and a new definition of what is ‘charitable’ came into effect on 1 January 2014. Charitable purposes recognised by the law include:

- advancing health
- advancing education
- advancing social or public welfare
- advancing religion
- advancing culture
- promoting reconciliation, mutual respect and tolerance between groups of individuals in Australia,
- promoting or protecting human rights
- preventing or relieving the suffering of animals
- advancing the security or safety of Australia or the Australian public
- advancing the natural environment
- other purposes for the public benefit (a general category), and
- promoting or opposing a change to any matter established by law, policy or practice in the Commonwealth, a State or Territory (if promoting a change the change is in aid or furtherance of one or more of the above purposes, or if opposing a change that change is in opposition or hindrance of one or more of the above purposes)

Caution

According to the definition of charity in the Charities Act 2013 (Cth), an entity that is not-for-profit and has charitable purposes or purposes incidental or ancillary to, and in furtherance of, charitable purposes, and operates for the public benefit may be registered as a charity. The new legislation clearly sets out the various ‘charitable purposes’.

The requirement that a charity operates for the ‘public benefit’ means that to be a charity, organisations must be assisting a broad enough purpose or category of people to be said to be providing a public benefit through its work.

There are certain benefits and limitations to becoming a charity that you should consider.
Benefits | Limitations
---|---
Charities can apply for (but may not necessarily qualify for) DGR endorsement, which gives charities greater access to donations and grant funding. | Members of charities cannot receive any benefit (ie. charities cannot return dividends to investors).

Charities can access federal tax concessions – income tax concessions in particular are very helpful for charities who generate income. | A charity’s activities are limited by their charitable purposes – all of a charity’s activities should be in furtherance of its mission.

Being registered as a charity means your organisation will be searchable on the register of charities (maintained by the ACNC) – this can help the public have trust and confidence in your organisation. | Details of directors are publicly available on the register of charities.

If your group incorporates as a CLG, its reporting requirements are lower if it is registered as a charity (because certain obligations under the Corporations Act do not apply to charities). | If your organisation is incorporated as a state-based structure such as an incorporated association, it will need to report to both its state-based regulator, and the ACNC (some states, such as South Australia, have made changes to reduce double reporting for incorporated associations – watch this space).

**Related resources**

For more information about charities, and whether your social enterprise could be eligible to be registered as a charity, see the ACNC’s factsheet which discusses who can register to be a charity with the ACNC.

Also see the part Not-for-profit Law’s webpage on charities.

If you are not sure, you may want to get legal advice about your organisation’s eligibility for charitable status before you start the process of applying to the ACNC.
Part 3: What legal structure should we choose?

Once you have considered the issues discussed in Part 2, and have decided whether your social enterprise will be for-profit, not-for-profit, or a hybrid form of both, you will need to decide the legal structure you will use.
Once you have considered the issues discussed in part 2 of this guide, and have decided whether your social enterprise will be for-profit, not-for-profit, or a hybrid of both, you need to decide the legal structure you will use. This is a very important decision, which will affect other issues like the different types of funding your social enterprise can receive, eligibility for tax concessions and the ongoing reporting requirements you must meet and other regulatory issues. Even within the for-profit and not-for-profit categories there are several options and each structure has relative pros and cons. It is always a good idea to seek legal advice about the particular benefits and downsides of each structure in relation to your particular plans.

The following table provides an overview of structures available to social enterprises of different types.

<table>
<thead>
<tr>
<th>Structure</th>
<th>Can be used in for-profit?</th>
<th>Can be used in not-for-profit? in general</th>
<th>Can be used in a hybrid?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Public Company (Ltd)</td>
<td>✓</td>
<td>✗ in general</td>
<td>✓</td>
</tr>
<tr>
<td>Note, can be listed or unlisted</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Private company (Pty Ltd)</td>
<td>✓</td>
<td>✗ in general</td>
<td>✓</td>
</tr>
<tr>
<td>Unit trust (note, these do not necessarily provide limited liability protection)</td>
<td>✓</td>
<td>✗ in general</td>
<td>✓</td>
</tr>
<tr>
<td>Incorporated association (Inc.)</td>
<td>✗</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Company Limited by Guarantee (Ltd)</td>
<td>✗</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td>Distributing Co-operative</td>
<td>✓</td>
<td>✗</td>
<td>✓</td>
</tr>
</tbody>
</table>
For-profit

All for-profit companies have shareholders, who ultimately own ‘equity’ in the company through holding shares in it. There are both ‘private’ and ‘public’ companies. Public companies can be unlisted (most common for social enterprises) or listed on the Australian Securities Exchange. Private companies have shares that can only be privately held and traded (ie. they can’t be widely advertised, although some exceptions apply).

Most for-profit social enterprises use a private or unlisted public company structure. Note that private companies (Pty Ltd) can have a maximum of 50 non-employee shareholders. If your organisation would like more shareholders than this, it should consider being a public company (it’s unlikely to be necessary to be listed on a security exchange), or a co-operative. Distributing co-operatives can also be used to structure a for-profit enterprise.

Shareholders are also sometimes called ‘investors’, but holding shares in a company is only one way of investing in a company, and there are other types of investment that can be made such as bonds and debentures.

Start-up funding for private and public companies and for-profit co-operatives generally comes from its shareholders buying initial shares in the company and also from taking out loans. For-profit companies provide protection to directors and shareholders, as personal liability is limited to the unpaid amount on shares owned in the company. There are often disclosure requirements associated with offering shares to investors (although exceptions apply, especially where offerings are smaller or investors are sophisticated or from your personal networks).

Caution

The legal requirement to act in the best interests of the company and its shareholders can be a tricky area for for-profit social enterprises, as sometimes there can be a tension between the best interests of the shareholders, and the best interests of the social enterprise and its social mission.

For-profit companies have constitutions that set out rules of the company, and will have at least one director. Depending on the size of the company, a for-profit will also have a board of directors who are responsible for overseeing the company.

The key difference between a for-profit company and a not-for-profit company is the way that profits are used. In a for-profit company, profits can be distributed to the shareholders (normally in accordance with rules). This is called ‘making distributions’ or ‘paying dividends’. In a social enterprise setting, a for-profit company needs to augment how it deals with profits so that it can meet definitions of social enterprise, such as the FASES definition. For-profit social enterprises normally distribute some profits to investors, and retain some profits to be re-directed back in to the social enterprise and achieving the mission of the organisation.

There is some debate about whether this causes tensions in the obligations of directors. There has not been any case law in Australia on the question of how much profit in a for-profit organisation can be directed toward mission rather than to shareholders. Some for-profit social enterprises put clauses in their constitutions to explicitly acknowledge that they have a social mission, and to allow directors to consider that mission when making decisions in the running of the company. There are some arguments that this tension is lessened in the co-operative structure. Care should be taken when choosing between a company structure (private or public) and co-operative structure as there are significant differences (for example, start-up co-operatives need to satisfy the regulator of co-operatives in the relevant state that they are designed to function under the seven co-operative principles).
ASIC regulates for-profit companies and the compliance and reporting requirements imposed by ASIC are quite onerous. The Corporations Act also imposes strict legal duties on board members, or ‘directors’ of private and public companies, including the duty to act in good faith in the best interests of the company. Regulatory requirements for Pty Ltds are generally lower than for public companies or co-operatives.

**Note**

Not-for-profit organisations can hold shares in for-profit companies. This is sometimes the case for organisations with ‘hybrid’ legal structures, which combine for-profit and not-for-profit structures.

**Common structure choices for for-profit social enterprises**

In many circumstances, a for-profit social enterprise will fall into one of two categories:

- an entity with a small pool of owners, which will often use a Pty Ltd structure, or
- an entity with a larger pool of owners, which will typically choose between a public company structure and a co-operative structure. Organisations in this category should seek advice about the relative merits of each of these structures before deciding on a structure.

There are other, more complex structures, such as trusts and partnerships, that can be used in for-profit social enterprises.

As Justice Connect doesn’t advise for-profits, we are only able to provide limited information about starting up for-profit social enterprises. You should seek advice on the best structure for your organisation.

**Real-world examples of for-profit social enterprises**

- The Yackandandah Community Development Company uses an unlisted public company structure, with community members as shareholders. Its constitution is available on its website and can be viewed as an example of a for-profit constitution that includes permissive clauses around pursuing a community purpose.
- Thankyou Water uses a Pty Ltd structure, that is owned by a charitable trust.
- The Hepburn Community Wind project uses a combination of a for-profit co-operative structure (a distributing co-operative) that owns a Pty Ltd structure.
Example

A private company runs an ethical clothing social enterprise, set up to employ intellectually disabled young people. The shop received its start-up funding from shareholders (also called investors), who each invested money to buy 25% of the equity in the company. Shareholders can be individuals, other companies, not-for-profit entities or even trusts. They invest by buying shares in the company.

The structure of a social enterprise set up as a private company might look like this:

<table>
<thead>
<tr>
<th>Shareholder 1</th>
<th>Shareholder 2</th>
<th>Shareholder 3</th>
<th>Shareholder 4</th>
</tr>
</thead>
<tbody>
<tr>
<td>25%</td>
<td>25%</td>
<td>25%</td>
<td>25%</td>
</tr>
</tbody>
</table>

Some profits are reinvested into the enterprise to fulfil its growth strategy and further its social mission.

In this example, let’s assume that the shop now makes a profit. Because the shop is operated by a private company, it returns money to its shareholders by paying dividends. But because the private company is also a social enterprise, the business directs are least 50% of the profits into the social enterprise to further its social purposes, or uses these profits to further the mission of the organisation in other ways, such as by providing education scholarships to employees.

A private company owes duties to its shareholders under the Corporations Act, and a social enterprise is a business that uses its profits to further its social or environmental purposes. A social enterprise with a private company structure must balance these obligations. It can be helpful to add clauses to the company constitution that clearly state that the business has a social mission, and that directors may consider that social mission when making decisions, so long as to do so is within the law.
Not-for-profit structures

There are a few different legal structures which are commonly used by not-for-profit social enterprises, and they are summarised in this section. There are benefits and limitations to each structure.

<table>
<thead>
<tr>
<th>Structure</th>
<th>Benefits</th>
<th>Downsides</th>
</tr>
</thead>
<tbody>
<tr>
<td>Incorporated associations</td>
<td>• Less onerous reporting obligations</td>
<td>• Groups with less than 5 members cannot use this structure</td>
</tr>
<tr>
<td></td>
<td>• Regulator takes ‘educative’ approach to enforcement</td>
<td>• State-based structure makes it difficult to operate across different states</td>
</tr>
<tr>
<td>Companies limited by guarantee</td>
<td>• National regulator</td>
<td>• Can be expensive to set up</td>
</tr>
<tr>
<td></td>
<td>• In the case of charities, simpler reporting requirements as reporting is to the ACNC not ASIC</td>
<td>• If not a charity, complex reporting requirements to a strict regulator (ASIC)</td>
</tr>
<tr>
<td>Non-distributing co-operatives</td>
<td>• For organisations passionate about co-operative principles, the structure enshrines co-operative principles</td>
<td>• Fewer co-operatives in Australia and fewer professionals with co-operatives expertise</td>
</tr>
<tr>
<td></td>
<td></td>
<td>• Co-operative principles and associated obligations will not suit all social enterprises</td>
</tr>
<tr>
<td>Indigenous corporations</td>
<td>• Takes into account Aboriginal and Torres Strait Islander customs and traditions</td>
<td>• Excludes non-Indigenous groups</td>
</tr>
</tbody>
</table>

Tip
For more detailed information, read our fact sheets that discuss the main incorporated legal structures that are used by not-for-profit organisations. Summaries are provided below.

Many not-for-profits can be run purely for the benefit of their members (for example, a tennis club). However, to be considered a social enterprise under definitions like the FASES definition, not-for-profits need to have a purpose to benefit the community, environment or a public purpose. Many not-for-profit social enterprises are also charities.

Often the group of people or cause to be helped through a not-for-profit social enterprise is separate from its membership. Members are often involved because they have an interest in the cause or purpose of the not-for-profit social enterprise. However, sometimes it is the members of a social enterprise that the organisation is trying to assist. This is acceptable, so long as membership is open and targeted enough to be consistent with the meaning of social enterprise (for example, a group may operate to benefit its members who are all unemployed refugee women).

If a group is set up to only benefit its members, this will also be relevant when seeking to register as a charity. Again, the conditions of membership and types of members, as well as the group’s purpose, must be consistent with charitable purposes, and satisfy the ‘public benefit’ test. This is possible, but your group may need to seek some advice about how to ensure that the requirements for charitable registration are being met.

Incorporated associations

An incorporated association is similar to a company in that there is a legal structure with a group of members and a governing body. The entity has a separate legal identity to its members. While members have certain rights (such as voting rights) they do not have a right to receive profits of the association. This is why incorporated associations are ‘not-for-profit’.

Incorporated associations must have a set of ‘purposes’, as well as rules of the association (also known as a constitution), which are to be lodged with Consumer Affairs Victoria (CAV), upon applying to become an
incorporated association. The activities of the association must be directed to those purposes and comply with the rules. Incorporated associations can make a profit, but that profit must be re-invested into activities directed to achieving the purposes of the association.

Incorporated associations can charge a joining fee or subscription fee to members, and can provide members benefits consistent with their purposes (for example, a tennis club charges members a yearly fee and in return members can hire tennis courts and access discounted tennis lessons, although note that such a club would be unlikely to be considered a social enterprise). Incorporated associations can also provide benefits to other groups, such as by running programs, services, or emergency relief, so long as this is consistent with the purpose of the organisation.

An incorporated association is run by an elected management committee and secretary, and must have rules that govern how the incorporated association functions.

**Note**
Incorporated associations are state-based, and have a different regulator in each state.

For more information on the regulator in your state, go to the Getting Started section of our website.

**Company limited by guarantee**

A company limited by guarantee (CLG) is a not-for-profit company, and works differently to other companies formed under the Corporations Act. The members of CLGs agree to provide a ‘guarantee’ up to a certain amount (usually a small amount like $10). This is similar to paying an annual subscription fee, but operates differently under law. A CLG doesn’t have shareholders, so it can’t raise money by issuing shares, and it cannot pay dividends to its members.

CLGs are regulated under the same strict legislation as Australian companies (the Corporations Act), however some requirements for CLGs are different (and more simple) than those that apply to for-profit companies.

If a CLG is registered as a charity, the majority of requirements under the Corporations Act no longer apply to it, and a CLG that is a charity is no longer liable for many common fees and penalties under the Corporations Act. Instead, the CLG reports to the ACNC instead, in line with the ACNC Governance Standards and financial reporting requirements which are less onerous.

**Remember**

CLGs are regulated by ASIC, unless they are a charity, where most of the regulation is the responsibility of the ACNC instead.

**Co-operatives**

Co-operatives are organisations based on voluntary, democratic participation from the members that form the organisation. One of their distinguishing features is that they are part of a movement of co-operatives, and in jurisdictions that have adopted the harmonised Cooperative National Law, the ‘cooperative principles’ are included in the laws. These principles are expressed throughout the law, for example through limitations on having different classes of membership, and through ‘active membership’ requirements, and when registering a co-operative, the relevant Registrar must be satisfied that the organisation follows the co-operative principles.

Many of the ‘original’ social enterprises, such as mutual societies, were set up as co-operatives. There is debate about whether all mutual societies meet definitions of social enterprises such as the FASES definition. This ultimately depends on whether the organisation can be said to be pursuing a community or public purpose.
As with other not-for-profit structures, it is possible to structure a co-operative so that it clearly meets the commonly accepted definitions of social enterprise, for example a co-operative enterprise that works to provide employment opportunities for its members, who are underemployed people with a disability.

There are 2 main types of co-operatives:

- co-operatives that have share capital and can pay returns to members, and
- co-operatives that do not pay returns to members and may or may not have share capital

Co-operatives that make distributions to their members cannot be not-for-profit structures. However, like other not-for-profit structures, co-operatives can trade to make profit and be not-for-profit so long as the profits cannot be distributed to members.

The co-operative structure is a specialist structure, and it can be hard to find pro bono advice on setting up a co-operative. The co-operative movement is actively advocating for improved ecosystems, and have created online resources for non-distributing co-operatives, so this position may change. For more information about starting a co-operative, go to the Get Mutual website.

**Note**

A new uniform national regime known as the Co-operatives National Law came into effect in March 2014. Administration of the uniform laws continues to be the responsibility of each State and Territory, but with a commitment to achieve uniform processes and policies. So far, Victoria, NSW, SA, NT, Tasmania, ACT and WA have signed up and QLD is considering whether its existing co-operatives laws should be changed.

**Indigenous corporations**

Indigenous corporations are established under the Corporations (Aboriginal and Torres Strait Islanders) Act 2006 (Cth) and are regulated by the Federal Office of the Registrar for Indigenous Corporations (ORIC).

Indigenous corporations are registered with ORIC and the laws that apply to them were written to meet the needs of indigenous communities. There are reporting and other compliance and governance requirements, but they are more relaxed than those that apply to other organisations. Like co-operatives, there are fewer lawyers with relevant expertise in indigenous corporations, however there are support services available and the structure can be used to set up a social enterprise. Contact the specialist regulator for indigenous corporations, ORIC, for more information about setting up an indigenous corporation (see the resources section at the end of this guide).
Examples of social enterprise structuring

Example of a not-for-profit social enterprise structure

Like the earlier example, this incorporated association also runs a vintage op shop social enterprise, set up to employ intellectually disabled young people. The op shop was set up as a not-for-profit incorporated association with DGR funding, and received its start-up funding from community donations received through crowdfunding, using a crowdfunding platform. Individual donors can claim a tax deduction for their donation.

The fundamental characteristic of a not-for-profit social enterprise is that all of its profits are reinvested to further the purposes of the social enterprise.

In this example, let’s assume that the op shop now makes a profit. Because the op shop is operated by a not-for-profit incorporated association, all of its profits are reinvested back into the social enterprise to further its social purposes.

Another example of a not-for-profit social enterprise structure

A local migration agent and his wife decided to start up a not-for-profit cleaning business, which employs new migrants who have been settled in their local community, and pays them a fair wage. The business was set up as a company limited by guarantee. The agent and his wife, as well as some of the agent’s colleagues, became the members of the company limited by guarantee, and they each pay an annual $50 membership fee. The business also successfully applied for a grant from the local council, which they used to buy cleaning equipment, train their staff, and buy some vehicles.

The diagram below illustrates the structure of this social enterprise, as well as their funding.
Hybrid structures

As discussed at earlier points in this guide, it’s possible to use a combination of not-for-profit and for-profit structures to achieve an outcome that will suit your business plan, and enable investment opportunities and access to tax concessions.

An existing not-for-profit starts a social enterprise

A not-for-profit homelessness organisation has the relevant skills and expertise to start a rental management business. It decides to create a real estate agency that will generate profits to support the not-for-profit’s work providing accommodation to homeless families. It decides to set the business up as a separate entity to manage risk. It also decides to use a for-profit structure in case it wants to raise equity capital in the future. It receives an impact investment low-interest loan to help cover the costs of setting up the business.

Members

Not-for-profit housing org
(has tax exemptions; runs housing programs)

Sole shareholder of Pty Ltd

Real Estate Pty Ltd
Private company operates the enterprise and can distribute profits to investors

Real estate business

Impact investor

$$ franked dividends

$$ low interest loan

$$ low interest loan
A new structure on the horizon?

The UK and USA have created specific legal structures especially for social enterprises that aim to reduce the tension between social mission and accountability to investors.

There is significant debate about whether a hybrid legal structure for social enterprises would be beneficial in Australia. There is also significant debate about how effective structures overseas have been.

In the UK, a special legal structure was introduced called a ‘community interest company’ (CIC). Those establishing CICs can choose between three versions of structure: a company limited by guarantee (not-for-profit version), a company limited by shares (private for-profit version), or a public limited company (public for-profit version). Those last two types of CIC can issue shares to investors, but with restricted rights attached to these shares, such as a cap on dividends. This allows social enterprises to choose company structures which give them access to equity funding, while still maintaining the character of a social enterprise. There is debate about whether the CIC structure is being used to return capital to investors. It is more commonly used in its not-for-profit form.

In the USA, a special legal structure was created called a ‘benefit corporation’, which has particular legal requirements that allow it to generate both shareholder and social benefit. The US-based not-for-profit organisation called ‘B Lab’ lobbied for this special legal structure. The structure still has all of the features of a for-profit business, but is allowed to consider public or community benefits as well as shareholder
interests when making decisions. It also needs to issue an annual report on its benefit activities. B Lab is a not-for-profit organisation which also certifies some corporations (around the world) as ‘B Corps’, if they meet certain standards of social performance, accountability and transparency. Certification by B Lab is not a legal structure, but is a public endorsement by B Lab that a company meets the standards set by B Lab. There are a small number of businesses in Australia who have been certified as B Corp, such as Small Giants, Whole Kids and TOM Organic. However the benefit corporation legal structure is not available in Australia.

**Ongoing obligations as a consideration**

Different reporting and compliance obligations will apply to your enterprise, depending on which legal structure you choose. You should consider what level of reporting and compliance you and your enterprise can manage before deciding on a legal structure. Also, be aware that some regulators are stricter than others. Some regulators, like the ACNC, take a more educative approach to enforcement, whereas regulators like ASIC generally take a stricter approach.

The reporting requirements are different for each legal structure. They depend on the nature of the regulator, whether only State, Federal, or both State and Federal law applies, and whether or not the social enterprise is a charity. Before choosing a legal structure, you should be aware of the reporting requirements you will need to comply with.

In general, there are more not-for-profit structures available with simpler reporting requirements than for-profit. However, charities and not-for-profits generally need to complete more complex reporting (like a company) if they are large or have been endorsed as DGR.

### Related Not-for-profit Law resource

The table below provides an outline of the different regulators and reporting requirements for different company structures. The Not-for-profit Law website has more detailed resources on reporting for different structures.

<table>
<thead>
<tr>
<th>Entity</th>
<th>Regulator</th>
<th>State or federal?</th>
<th>How onerous are the reporting requirements?</th>
</tr>
</thead>
<tbody>
<tr>
<td>Proprietary Limited Company</td>
<td>ASIC</td>
<td>Federal</td>
<td>Medium – high</td>
</tr>
<tr>
<td>Incorporated association</td>
<td>State regulator</td>
<td>State</td>
<td>Low – medium</td>
</tr>
<tr>
<td>Incorporated association which is also a charity</td>
<td>State regulator + ACNC</td>
<td>State and Federal</td>
<td>Medium</td>
</tr>
<tr>
<td>Company limited by guarantee</td>
<td>ASIC</td>
<td>Federal</td>
<td>Medium – high</td>
</tr>
<tr>
<td>Company limited by guarantee (which is also a charity)</td>
<td>ACNC (with residual aspects regulated by ASIC)</td>
<td>Federal</td>
<td>Low</td>
</tr>
<tr>
<td>Co-operative</td>
<td>State regulator</td>
<td>State</td>
<td>Medium</td>
</tr>
<tr>
<td>Co-operative which is also a charity</td>
<td>State regulator + ACNC</td>
<td>State and Federal</td>
<td>Medium – high</td>
</tr>
<tr>
<td>Indigenous corporation</td>
<td>ORIC</td>
<td>Federal</td>
<td>Low</td>
</tr>
</tbody>
</table>
Adding a social enterprise to an existing not-for-profit organisation

Many not-for-profit organisations are considering starting trading activities to help provide funding certainty into the future. As philanthropic and Government funding becomes harder to secure in some sectors, creating a social enterprise is worth considering for some organisations.

There are, however, some important considerations when undertaking an analysis of the costs and benefits of starting up a social enterprise in addition to their existing organisation’s activities. These are listed below (and are in addition to the consideration outlined above):

• would the starting of a trading enterprise be consistent with the organisation’s purposes? If not, how hard would it be to change the purposes?

• does the organisation access charitable tax concessions? This will be relevant to both starting an enterprise and changing your organisation’s purposes – both of which could affect your continued eligibility. We recommend that you seek tax advice before making any changes;

• could starting the enterprise expose your organisation to financial risk or reputational risk? Are there structures to put in place that could mitigate this risk?

• do people in your organisation have the relevant skills for the enterprise? What would it cost your organisation to recruit the right people?

• is there a compelling business case for the enterprise? Should your organisation get some advice about the market for your purposes enterprise?, and

• will the new enterprise advance your mission or fund your organisation’s activities?
Part 4: Setting up

Once you have decided to incorporate using a legal structure, you can begin setting up your organisation.
Setting up a social enterprise

This section covers:

► forming a committee or board
► finding members
► drafting rules or a constitution
► holding meetings
► registering as a charity (if desired)
► applying for tax concessions (if desired)

The process of setting up a social enterprise under one of the legal structures discussed in part 3 of this guide involves ‘incorporation’. This section is focussed on setting up a not-for-profit social enterprise. If you want to set up a for-profit social enterprise or a hybrid structure, you should seek legal advice. Some, but not all, of the information in this section is relevant to for-profit structures.

Once your organisation has decided which incorporated structure it will use, the next step is to set up your organisation following the process required by the relevant legislation. The incorporation process is different for each type of legal structure; however there are some basic steps that all organisations should take, such as applying for an Australian Business Number (ABN) (subject to certain thresholds) and registering a business name.

There are also several fundamental issues you need to consider when setting up your not-for-profit organisation. Six of those fundamental issues are discussed in this part.

Forming a committee or board

A fundamental incorporation step is forming a governing body, such as a committee of management or a board. The legislation governing incorporated associations refers to the governing body as a ‘committee of management’, and the legislation governing companies limited by guarantee uses the term ‘board’. In this section, we will use the term ‘committee’. The term you use to refer to your committee is not important, but its role, the duties of its members, and its composition are very important, and you should consider them carefully.

Related Not-for-profit Law resource

For more information on forming a committee go to Justice Connect’s ‘Secretary’s Satchel’. parts 1, 2, 3 and 7 of the Secretary’s Satchel are particularly relevant.
The role of a committee

It’s the role and responsibility of an organisation’s committee to govern and direct the strategy of the organisation. The committee is responsible for making decisions about the overall running of the organisation. The committee is elected by the members of the organisation, and in most structures, the committee is accountable to the members.

Who should be on a committee?

To be effective, a committee needs the right group of people, with knowledge and experience that fit with the organisation’s strategic goals. To help you put together a committee of people with those necessary skills, we recommend developing a ‘skills matrix’ specific to your organisation. A committee member should be committed to the mission of the organisation, and prepared to devote time and energy to the committee.

There are several positions that usually make up a committee, such as a chairperson or president, treasurer and secretary. The committee may have other members who do not have a special role, who are sometimes called ‘ordinary committee members’.

The size of the committee is an important consideration for start-ups. When deciding how many committee members you should have, you should take into account the size of your organisation and understand that ‘bigger isn’t necessarily better’ – a board that is too large can be ineffective, or inefficient.

It is important that prospective committee members understand your expectations of them, and their legal duties.

A skills matrix

It is important to have the right mix of skills, experience and diversity on a committee. When you are thinking about committee members, it is a good idea to have a process for identifying the skills you need on your board, which will vary depending on the nature of your organisation.

To develop a skills matrix, you can follow the steps below.

1. What is your strategy?

Your organisation has a mission. What is your strategy to achieve that mission? Write down each strategic priority or goal, and think about the knowledge, skills, competencies and experience required to achieve them, and write them down too. Also think about the skills required for a committee to meet the legal obligations incorporated groups have (reporting, preparing financial statements etc). Don’t forget to think about your vision for the future – what kind of committee, with what kind of committee members, will be needed to take the organisation forward?

2. What issues does your organisation deal with?

Consider the key issues and challenges that face your organisation – particularly in light of its mission and activities. Write these down, and then review what skills or experience is needed to most effectively deal with each of them. If there are any extra skills you didn’t write down in step 1, write these down now.

3. What are your priorities?

All the skills you wrote down in steps 1 and 2 might seem important. However, it is important to prioritise them, and work out which ones are high, medium, and low priority. You might like to rank each skill with a number, such as high = 3, medium = 2 and low = 1.

4. What skills are needed?

Determine what skills and what levels of experience need to be represented on the committee. Remember, you might have volunteers or employees ‘on the ground’ who carry out the activities of the organisation, so some of the skills you have listed might be their responsibility. But some skills, such as financial management, might be best represented at committee level.

5. Create your skills matrix

Finally, create your skills matrix, using the data from steps 1 to 4. The skills or experience needed can go in column 1 of a table and the rest of the columns can be the directors.
Case study example

A young lawyer has a great idea for a social enterprise. She wants to set up an incorporated association called ‘Love, Mum’, which will hold meetings for unemployed young mothers in the Epping area. At the meetings the young mothers have their children cared for while they network and bake healthy treats for kids, which are sold at the local farmers market each week under the business name ‘Love, Mum’. 50% of the earning will be distributed to the young mothers, with the remaining 50% going back into the organisation. The young lawyer has applied for several local council grants to help get her social enterprise off the ground. The young lawyer needs to put a committee of management together.

Here is what her process of creating a skills matrix looks like.

Step 1 – The organisation’s mission is to assist young mothers in the local community by supporting them socially, emotionally, and financially, building their self-esteem and teaching them how to cook healthy food for their families. The organisation’s strategy is to create a business that sells healthy, tasty food for children, whilst assisting disadvantaged young mothers. Its strategic priorities include:

- building a successful business (skills: finance, accounting, legal, management, employment, fundraising, experience building a business from a start-up, managing risk, NFP experience)
- supporting young mothers in a professional manner (skills: social work, managing people, counselling, mental health experience)
- creating a safe childcare environment (skills: childcare qualifications and experience, managing staff, legal)
- giving each mother a small income through receiving a percentage of business earnings (skills: finance, accounting, management, financial counselling)
- preparing safe and tasty foodstuffs for sale (skills: cooking, food safety, sales, marketing and advertising, safe food preparation experience), and
- selling goods in a community, commercial environment (skills: sales, marketing, community liaising)

Step 2 – The organisation faces the following issues:

- food safety (skills: commercial food preparation experience, legal, organisation, management)
- childcare and child safety (skills: management, childcare experience and qualifications, legal)
- providing adequate, professional counselling services (skills: psychological, social and financial counselling, social work, legal)
- mental health of clients (skills: social work, counselling, mental health experience)
- fundraising issues (skills: fundraising experience, accounting, financial management experience), and
- food sales (skills: sales experience, marketing and advertising experience, accounting, management)
Step 3 – Here, the skills identified as being necessary are prioritised (1 = low, 2 = medium, 3 = high)

<table>
<thead>
<tr>
<th>Skill</th>
<th>Member 1</th>
<th>Member 2</th>
<th>Member 3</th>
<th>Member 4</th>
</tr>
</thead>
<tbody>
<tr>
<td>Legal</td>
<td>3</td>
<td>3</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Psychological and social counselling</td>
<td>3</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Accounting</td>
<td>3</td>
<td></td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>Financial counselling</td>
<td>2</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Financial management</td>
<td>3</td>
<td></td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>Social work</td>
<td>3</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Management of staff</td>
<td>2</td>
<td></td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>Mental health experience</td>
<td>2</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Organisational management</td>
<td>3</td>
<td></td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>Experience starting a business</td>
<td>2</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Childcare</td>
<td>3</td>
<td></td>
<td>3</td>
<td></td>
</tr>
<tr>
<td>Fundraising experience</td>
<td>3</td>
<td></td>
<td></td>
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<tr>
<td>Sales</td>
<td>1</td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Food preparation</td>
<td></td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Marketing and advertising</td>
<td>2</td>
<td></td>
<td>2</td>
<td></td>
</tr>
<tr>
<td>Food safety</td>
<td></td>
<td></td>
<td></td>
<td>2</td>
</tr>
<tr>
<td>Managing risk</td>
<td>2</td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Cooking</td>
<td></td>
<td></td>
<td></td>
<td>1</td>
</tr>
<tr>
<td>Community liaising</td>
<td>2</td>
<td></td>
<td></td>
<td>2</td>
</tr>
<tr>
<td>Not-for-profit experience</td>
<td></td>
<td></td>
<td></td>
<td>2</td>
</tr>
</tbody>
</table>

Step 4 – The skills and experience that would be useful on this committee of management are: legal, accounting and financial management, organisational management, social work, fundraising experience, not-for-profit experience, risk management experience and experience starting up a business.

The other skills listed in step 3 can be taken care of by employees or volunteers.

Step 5 – The young lawyer thinks four people would be a good sized committee of management to begin with. She will be seeking members for her committee who have the skills listed in the matrix. Where a candidate has a particular skill, she can put a ✓ in their column alongside that particular skill. By the time she fills the positions, she hopes to have at least 1 ✓ next to each skill needed to run the organisation.
Where do I find good candidates?

Sometimes it can be difficult to find qualified, experienced committee members who have the necessary skills to help govern your particular organisation.

These are some useful websites you can use to recruit committee members:

- Volunteering Australia
- Leadership Victoria
- Good Company
- Pro Bono Australia; and
- Our Community

Finding members

The role of members

Members play a fundamental role in a not-for-profit organisation.

The members of an organisation have certain rights and responsibilities under the relevant legislation, depending on the legal structure of the organisation. Generally, members of the organisation attend general meetings and vote on matters such as:

- electing the committee
- changing the organisation’s name, rules or purpose
- amalgamating the organisation with another organisation
- removing an auditor, and
- winding up the organisation voluntarily

Members have certain rights, such as the right to notices of meeting, the right to attend general meetings, the right to remove committee members by special resolution and the right to access certain records of the organisation.

Importantly, the committee is accountable to the members of the organisation.

The importance of a membership strategy

You will need to consider how many members you want your organisation to have, and in making this decision there are a number of factors you should consider, such as:

- if your members pay a membership fee, it may be good for fundraising to have many members
- don’t forget that the members come together to vote at the annual general meeting. Having too many members may cause an administrative burden, and may make decision making difficult
- having too few members might empower one or two members who are difficult or ‘rogue’, and
- having too few members may make it too easy for the board to be spilled, or directors to be removed

As you can see, it is important to have a membership strategy. You can set down your membership strategy in the form of including membership criteria, limits and other requirements in your organisation’s rules or constitution.

Related Not-for-profit Law resource

The Not-for-profit Law website has information about the rights and responsibilities of members of not-for-profit organisations.
Drafting your rules or constitution

Incorporated organisations such as incorporated associations or companies limited by guarantee are required to have a set of rules, or a constitution, which governs the internal affairs of the organisation. There are laws as to what matters must be covered by the rules, depending on the legal structure of your organisation.

The committee and the members are bound by the rules of the organisation.

Where do we start?

There are model rules published by many regulators for incorporated associations which can be adopted, or used as a starting point and varied and adopted. Not-for-profit Law also has a set of Simple Rules for incorporated associations in Victoria (and will publish rules for other states and territories soon). The ACNC has published a precedent constitution for charitable companies limited by guarantee. There are also resources available on the Justice Connect website which can help you draft your rules or constitution or vary your rules or constitution. It is important to think carefully about your rules because any changes to your rules must be approved by your members at a general meeting, and depending on your structure may require payment of a fee for lodging the updates.

Holding meetings

Meetings are an important part of the operations of any organisation. Meeting requirements differ depending on the legal structure, but generally, the meetings required will include:

• committee meetings (for committee members), and
• annual general meetings (for members)

It’s important for your organisation to conduct meetings in accordance with the relevant laws and regulations. Once a meeting has been conducted, there may be requirements for forms to be completed and filed with the relevant regulator, as well as records to be made for the organisation itself, such as minutes and resolutions.

Related Not-for-profit Law resources

See the section of our website that discusses rules. Also, see the factsheets in the sections that explains incorporation and legal structures (these factsheets include guidance on drafting rules for specific types of organisations).

Registering as a charity (if desired)

Whether or not you should register your organisation as a charity is something you should consider at the incorporation stage. You should consider how ‘charity’ is defined, and whether or not your organisation is eligible to become a charity. There are advantages and disadvantages in doing so, which are discussed above in part 2.
Related Not-for-profit Law resources

For more information about whether or not your organisation should be registered as a charity, and for more information about what organisations are eligible for charity status and what that status means, see our charities webpage.

Applying for tax concessions (if desired)

Your organisation may be eligible for tax concessions. You should think about applying for tax concessions at this incorporation stage. Tax concessions were discussed in detail in part 2 of this guide.

Related resources

For more information about tax concessions, eligibility and how to make the necessary applications see the tax page on our website. The ATO also has an excellent resource called the GiftPack, which contains detailed information about tax concessions for not-for-profit organisations.
Part 5: Operating a social enterprise

Once you have incorporated, there are many other things you should consider, depending on the nature of your social enterprise and the activities it undertakes.
Operating a social enterprise

This section covers:

► insurance
► employment
► occupational health and safety
► documents and record keeping
► intellectual property
► advertising
► running events
► privacy, and
► ongoing compliance and governance requirements

Once you have set up your organisation, there are many other things you should consider. Running a social enterprise involves following many regulations and laws about lots of different things.

Insurance

There are many risks and legal issues associated with running a social enterprise. Some risks simply cannot be avoided, so it is a good idea for your enterprise to have adequate insurance. As well as taking a common sense approach to getting insurance for your enterprise, you should carefully consider the specific risks your enterprise faces, and make sure that your insurance covers those specific risks. You should also check the laws that apply to your organisation regarding insurance and make sure you follow them.

Related Not-for-profit Law resource

For extensive information on risk and insurance, go to the Not-for-profit Law website for information on risk and insurance.

Employment

Even if your social enterprise begins with only volunteers, there are still legal obligations you need to follow. Before your social enterprise starts working with its first volunteer, and especially before it hires its first employee, you should familiarise yourself with the legal obligations relating to volunteers, employees and independent contractors.
Occupational health and safety

Occupational health and safety (OHS) laws vary between states. OHS laws are important, and onerous, however they don’t apply to certain organisations. If the legislation applies to your social enterprise, you need to be aware of your responsibilities. The laws in both Victoria and NSW also include personal obligations which must be met by ‘officers’ of organisations, such as directors or committee members. Some of these obligations have criminal penalties for breach. It is vital you are aware of what laws apply to you personally, your directors and committee members, and your organisation, and ensure that you meet your obligations.

Some of the obligations are general, such as the duty to provide and maintain a working environment that is safe and without risks to health, and some obligations are very specific, such as the obligation to establish a health and safety committee, if requested.

Documents and record keeping

Your document and record keeping obligations largely depend on what legal structure you decide to adopt for your enterprise. As discussed earlier in this guide, some structures have different document and record keeping obligations to others, and depending on how much document and record management your enterprise can handle, this may affect what structure you choose.

Intellectual Property

When starting up a social enterprise, you will need to think about a name, a logo, business know-how and maybe a website. You need to consider intellectual property legal issues and make sure that your intellectual property is protected. You should also make sure that you don’t infringe anyone else’s intellectual property. Infringement can be accidental, such as by creating a logo which is almost identical to someone else’s, or using someone else’s intellectual property in your marketing communications.

There are laws about marketing and advertising in Australia. If your social enterprise wishes to advertise, or say anything about itself in public (such as on a website), it needs to comply with Australian consumer law. There are also specific laws relating to different mediums of communication, such as television, radio, print...
and online. Before you start your website, and before you start marketing or advertising your enterprise, you should make sure you aren’t breaking any laws.

Related Not-for-profit Law resources
Go to our website for more information on intellectual property and the laws of advertising and promotions.

Events and fundraising activities
Unfortunately, running an event for your social enterprise is (often) not as simple as it sounds. There are many things you need to consider and various laws you need to comply with when organising events and activities. An important issue to consider when organising an event is licensing. Community organisations require licenses for certain activities. After you decide on what sort of events and activities your enterprise will be involved in, you should investigate what licenses are required.

Related Not-for-profit Law resources
Our website has more information on running events and raising money.

Privacy
Privacy is an important part of Australian law. You should be aware of privacy laws, because they can affect you in many ways, such as if you have employees and hold information about them, or if you have a donor mailing list, or if you have access to people’s health records.

Related Not-for-profit Law resources
Our website has more information on privacy laws.

Governance and ongoing compliance
Different legal structures require organisations to meet different ongoing compliance and governance requirements. Once you decide what legal structure your enterprise will use, you should become very familiar with the compliance and governance obligations you will be required to meet.

Example
Private companies are required to comply with the Corporations Act. The Corporations Act contains a number of duties the directors of the company must comply with, such as the duty to operate in the best interests of the company. Private companies are also required to adopt constitutions, or follow the replaceable rules contained in the Corporations Act.

The Act also contains governance requirements that the company must follow. The compliance and governance obligations for private companies are different (and more onerous) than those which apply to not-for-profit corporate structures.
Related Not-for-profit Law resources

The Not-for-profit Law website has information on positions in a not-for-profit organisation and the legal duties that apply to office-holders, on the governance page.
Part 6: If things change or go wrong

After your organisation has been running for a while, issues may come up which have a legal component.
If things change or go wrong

This section covers:
► when things go wrong
► when your structure is no longer working
► deciding to work with other organisations
► ending your organisation(s)

Things don’t always go to plan when you are operating a social enterprise. Conflict may arise between employees, someone might take your enterprise to court, or you may encounter financial difficulties sooner than you expected.

Some issues that may come up include:
• breakdowns in agreements
• loss of key staff or committee members
• governance issues
• property issues
• being taken to court
• losing funding
• investor relations, and
• public perception issues

There are also times where your organisation will go through change – at times of growth, retraction and even in response to changes in the law. When things change, you should stay on top of what is happening in your organisation, and be mindful of the options available to you, such as changing the nature of your organisation, working with another organisation or winding up.

Further reading
For more information on what to do when things go wrong, visit our website.

When your structure no longer works
As your organisation changes and evolves, the legal structure you choose at the start may no longer be appropriate. It may be that your organisation is incorporated in Victoria and you want to start operating nationally, or your organisation may decide to apply for DGR endorsement, and need to change its rules or constitution to make sure it reflect its current activities. Your group might increase significantly in size, or
you may become registered as a charity. There are many different circumstances which will require an organisation to change its governing documents or its entire legal structure.

**Changing your governing documents**

Different organisations have different governing documents, depending on their legal structure. For example, companies have constitutions, and if a company wants to change its constitution it must follow the procedure outlined in the Corporations Act. Whichever set of procedures apply, your organisation must follow them carefully.

**Deciding to work with other organisations**

It may be appropriate to combine with another organisation for any number of reasons. It may be more efficient to work with another organisation of the same purpose, another organisation may give you access to more funding, or you might find that joining forces with other like-minded people can help you accomplish your mission faster and more effectively!

There are a variety of ways you can work with another organisation, such as merging organisations, entering into auspicing arrangements (as discussed earlier in this guide), forming joint ventures or forming partnerships. These are legal arrangements which require negotiating and the signing of legal documents, and should be discussed with a lawyer.

**Caution**

Even if you completely trust the people working in the other organisation and have no concerns at all, you should always put any kind of arrangement into writing.

For more information, see our website section on working with other organisations.

**Ending your organisation**

Sometimes a decision needs to be made to end an organisation. This decision may be appropriate for a variety of reasons, such as if your organisation runs out of funding, or if your organisation no longer wishes to pursue its social mission. The way to end your organisation will depend on the legal structure you have chosen. Your legal structure will determine what must be done with any surplus funds or assets, and depending on how complicated your legal structure is, you should see a lawyer and ask them to help you.

**Related Not-for-profit Law resources**

For more information, see our website section on winding up.
Extra Help
Organisations that work with Social Enterprises
Organisations that work with Social Enterprises

Organisations
The following organisations provide various forms of assistance to Social Enterprises.

They each have different criteria, some are free and some charge for their services. This list is not comprehensive, and we do not specifically endorse these organisations. We always recommend that you conduct your own research.

► Social Traders
► The Difference Incubator
► Social Ventures Australia
► Social Enterprises Sydney
► Centre for Social Impact
► B Lab
► Business Council of Cooperatives and Mutuals
► One10
► Business Models Inc
► Chartered Secretaries Australia
► Governance Institute of Australia
► Volunteering Australia
Resources

Not-for-profit Law resources

- Getting started
- Tax
- Risk and Insurance
- People Involved
- Running the Organisation
- Communications and Advertising
- Fundraising and Events
- Reporting to Government
- Changing or Ending your Organisation
- Working with Others
- Important Agreements
- Disputes and Conflict

Government Agencies

- The Australian Charities and Not-for-profits Commission
- Consumer Affairs Victoria
- Office of Fair Trading NSW
- The Australian Securities and Investments Commission
- Office of the Registrar of Indigenous Corporations
- The Australian Taxation Office