

## **New Wine in New Bottles? A Quest to Understand Social Enterprise Complexity and Community-based Co-operative Innovation in rural China**

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**Abstract:** Previous research indicates the emergence of multi-stakeholder co-operatives in the West, and its importance to economic participation and social cohesion. This new kind of co-operative “spirit” (as “new wine”) is generally regarded as one important element to form the domain of social enterprise (as “new bottle”). In recent years, more and more studies on social enterprises in East Asia can be witnessed. However, since “social enterprise” is a predominantly western term, a specific legal framework is mostly absent in the Asian region. Consequently, while analyzing social enterprises in this region, scholars generally examine various broader existing legal frameworks on third sector organizations. Although various situations and current environment of SE development have been greatly examined, and the contribution of these organizations to social and economic development has been widely recognized, the theoretical understanding underpinning the rationale of their emergence and development has so far remained unsatisfactory. Consequently, social enterprise complexity can barely be fully understood by just putting all existing institutions together.

Against this background, the paper aims at revisiting the social enterprise complexity by exploring the theoretical understanding involved. In most cases, exploratory studies by scholars from areas where the term social enterprise is still relatively new tend to cover so broad an area that the analysis and results are often hardly convincing. Therefore, the paper is concerned with recasting the SE image in China by highlighting the so-far neglected “co-operative model” in order to gain a better knowledge of social enterprise complexity. This effort is also beneficial considering the fast growth of multi-stakeholder co-operatives and their growing contributions to satisfying the increasing social needs. Equally important in the paper is the aim of exploring the theoretical understanding on the emergence and development of SEs, which remains an unsatisfactory state of knowledge in the SE studies related. To mend up the existing theoretical defect the paper presents a model of SE emergence and develops further a conceptual framework to illustrate the SEs’ sustainable development, by drawing on the theoretical reasoning from multi-stakeholder theory and institutional theory. Empirical observations on current situation of multi-stakeholder co-operatives in rural China are presented, and a complementary case is further analyzed to illustrate the conceptual framework proposed. Through this analysis, the study concludes by addressing a decisive research question on whether examining social enterprises is just a fancy study which actually means putting old wine in new bottles, or it is indeed a new approach which is strong enough to represent the new “spirit”.

**Key Words:** Social Enterprise Complexity, Multi-Stakeholder Co-operative, China, Rural Community, Stakeholder Theory, Institutional Theory

## I. Introduction

In recent years, more and more studies on social enterprises (SEs) in East Asia can be witnessed. However, since “social enterprise” is a predominantly western term, a specific legal framework is mostly absent in the Asian region (except South Korea, *a.o.*). Consequently, while analyzing SEs in this region, scholars generally examine various broader existing legal frameworks on third sector organizations which are different from country to country. But does social enterprise complexity just mean this mosaic reality of putting all existing institutions together? Or to ask, can the social enterprise complexity be fully understood by just putting all existing institutions together?

Part of the contribution of discussions on SE development in East Asia is that they facilitate an integration of various organizations (formal and informal, newly-emerged and reshaped-old ones) belonging to the “third sector” into one family of SE, therefore conducive to encouraging somewhat dialogues and communications with each other. However, rather than employing this integration to create an area of intrinsic common ground for this *raison d'être* with shared characteristics, scholars with different backgrounds frequently analyze SE-related topics in this way: starting with a general description of the development of SEs and its driving forces (similar to the study of NPO school)<sup>1</sup>, they then put several existing organizations together to name the existing legal frameworks similar to SEs, and list several regulations and laws related, afterwards slip back into their cozy and familiar ways of thinking and raise several cases to conclude a list of challenges they face due to several dominant features in East Asia, such as the strong state, strict regulations or legislation gap, lack of volunteerism culture (or the “voluntary failure”), *etc.*. Inevitably, this inertial thinking may due to the prevailing training background of the scholars involved. Correspondingly, an unfortunate side effect of such “integration” effort is that, it rather produces an image of old/existing organizations with merely a new cover, therefore, appears to be old wine in new wineskins.

Against this background, the paper is concerned with revisiting social enterprise complexity by exploring the theoretical understanding involved, which has so far remained unsatisfactory. In most cases, exploratory studies in this field by scholars from areas where the term SE is still relatively new, tend to cover so broad an area that the analysis and result are often little convincing. Therefore, an initiative to close this gap is needed. This paper takes into consideration the specificity of vulnerability in local communities of rural China in explaining the existence and development of the most dynamic SEs. In other words, it focuses on one approach in this mosaic reality of SE domain, namely, multi-stakeholder co-operatives as an indigenous model of SEs in rural China (Zhao *et al.*, 2009). There are two further explanations for it.

The first reason concerns with the reality of vulnerability in rural China. Currently, there are more than 800 million rural people (approximately 12% of the global population) in China, most of whom belong to various vulnerable groups in China. It is fairly to say that rural population is

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<sup>1</sup> It means that those driving forces of the SE development are generally derived merely from the various demand and/or supply side theories of explaining the existence of NPOs, such as the “government failure” or “market failure”, and entrepreneurial theories, *etc.*

the most vulnerable population, and rural areas are the most vulnerable communities in China. The second explanation is due to the fact that, previous research indicates the emergence of multi-stakeholder co-operatives in the West (Borzaga & Defourny, 2001; Defourny & Nyssens, 2008; Gijssels & Develtere, 2008; Girard, 2009), and its importance to economic participation (Münkner, 2004; Thomas, 2004) and social cohesion (Galera, 2004; MacPherson, 2004). Recently, this new co-operative movement has also been witnessed in China. This new kind of co-operative spirit (as “new wine”) is generally regarded as one important element to form the domain of social enterprise (as “new bottle”), and as the most dynamic organizations nowadays in rural China (Zhao & Develtere, 2010). This dynamics has been highly influenced by various national policies in the 2000s, especially the issuance of seven *Number One Documents* annually concerning the “three rural issues” and the implementation of the national co-operative law in 2007 as well, etc.. Therefore, in what follows I will put my focus especially on SE development in rural areas.

Through this analysis, the study aims to answer the following questions:

- What is the general situation and environment concerning SE organizations in rural China?
- How can SE organizations emerge through existing institutions and creating new space and develop sustainably? What are the triggers and determinants?
- If examining the SE is just a fancy study which actually means old wine in new bottles, or it is indeed a new approach which is “strongly” enough to represent the new “spirit”?

To throw light on these issues, Section II starts with a brief overview of general environment concerning SE organizations in rural China. A specific focus will be on the emergence of multi-stakeholder co-operatives. Afterwards (in Section III) a conceptual framework is developed which draws on institutional theories and multi-stakeholder theories from the perspectives of mainstream corporations, co-operatives and NPOs respectively. I then draw on these theoretical discussions to present a model of SE emergence from an organizational structure perspective (to explain the question how SEs emerge), and a conceptual framework of “multi-stakeholder co-operation” in SEs (to explain how they can develop sustainably). Complementing empirical evidences presented in Section II to illustrate SEs’ emergence, a distinctive case is briefly introduced in Section IV demonstrating the crucial issues on SEs’ sustainable development. Finally, the paper concludes in Section V by presenting main findings from the cases as well as looking for explanations for the questions raised.

## **II. General environment**

### **1. Three models of SEs**

It is generally agreed that ever since 2004, when the concept and studies of SE were formally introduced to China, its notion has become a hot topic among academics, media and social elites from various backgrounds (Ding, 2007; BC, 2008). However, a common understanding is nevertheless far from being achieved due to different academic backgrounds of the scholars. In China, co-operatives are not necessarily regarded as an integral part of NPOs. Therefore, NPOs and co-operatives appear to belong separately to two different schools of thought in China. It is

observed that in most cases, the “NGO/NPO model” and the “company model” have dominated the discourses of SEs in China<sup>2</sup>, being represented by a series of introductions on relevant works from the West as well as various forums and conferences organized to promote the SE concept. Scholars focusing on co-operative development in China are either still relevantly unfamiliar with its notion or its debates, or doubtful of the viability of advising co-operatives open to the whole community in the initial stage of co-operative development in China<sup>3</sup>. Therefore, the “co-operative model” has been generally neglected, and not enough weight has been given to new co-operatives that can play a role in contributing to understanding SE development in China. There are two sad consequences:

In the first place, while it is not difficult to find related studies (although still not much) on SEs in China which actually take the perspective of the “NGO/NPO model” or of the “company model”, research on the “co-operative model” of SEs in China is still a *tabula rasa*. This severely impedes people’s understanding on multi-stakeholder co-operatives in China as an indigenous model of SEs. Second, the two over-emphasized models tend to lead local economic development through the way of what Birkhölzer (2009) calls the scenario of “development from outside”. It means that local actors tend to believe that they are incapable of doing anything on their own, and entrepreneurs (individuals or enterprises) from the outside are needed to bring in the necessary resources. In most cases, the two over-emphasized models are just practicing this way of doing good, thus becoming the exogenous factors of development. In contrast, the “co-operative model” of SEs corresponds to the scenario of “development from within”, in which the local people themselves play the key role. Therefore, social entrepreneurs tend to be found in the local communities instead of coming from outside<sup>4</sup>. Together with the other endogenous factors (such as *a.o.* social capital, culture values, embedded norms), this “co-operative model” represents an important instrument for an endogenously driven process of development (Borzaga and Tortia, 2009). Therefore, multi-stakeholder co-operatives can contribute specifically to the empowerment of individuals, because people in this way feel in control of their life and their sense of accomplishment (Noya, 2009: 24).

## 2. The mutual and co-operative development in China

Like in the West, numerous co-operative and mutual-aid initiatives emerged in China even before they had received legal recognition. Mutual aid societies already existed in the Early Imperial period of China two thousand years ago. The co-operative movement has also a long history in China. More than one hundred years ago, modern co-operative ideas and practices were firstly proposed by a number of Chinese democratic activists who came back from the West to search for a way of helping the poor and saving the nation. During the New Democratic

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<sup>2</sup> Cafaggi and Iamiceli (2009) have once identified three models of SEs developed in different legal systems in an OECD report, the “co-operative”, “company” and “open form” models (the latter meaning that no specific legal form is selected by the law).

<sup>3</sup> There exist very limited exceptions regarding co-operatives as an integral part of SEs in China. One of the few examples can be provided by a rural grassroots’ activist, Li Changping, when analyzing SEs (co-operatives, collective economic organizations, *etc.*) in contributing to the land circulation in rural China.

<http://theory.people.com.cn/GB/41038/10983247.html> (accessed 19 February 2010).

<sup>4</sup> They are also called “co-operative entrepreneurs” in the “co-operative model” of SEs.

Revolution in China (1919-1949), the practices of establishing co-operatives and credit societies were driven by the forces of nationalism and a quest for a “third way”. Afterwards, co-operative movements in China have always risen and fallen with the turns of the economic and political cycles. During the period of centrally planned economy in China, People’s Communes were established in a compulsory way under the government’s command. Their development has restricted the growth of a genuine co-operative movement. However, after the reform and opening-up, a new co-operative movement has been witnessed in rural China, trying to solve the rural crises during the last two decades.

These rural crises have been summarized as the well-known “three rural issues” (i.e. issues of farmers, rural areas as well as agriculture) in China<sup>5</sup>. It has been demonstrated by an imbalance in the development of urban and rural areas; of the rich and of the poor and also of different regions and different sectors. Although agriculture production increased, farmer’s income stagnated. The “company plus farmers model” emerged and has been considered, for a long time, as the path to agricultural modernization in China. As farmers lacked fundamental co-operative theories and experiences, they were inclined to follow a capitalist model to survive. Contrary to the co-operative system, this capitalist model is neither farmer-independent nor farmer-determined. Therefore, it tends to pose a potential crisis, especially if enterprises do not operate well and turn risks of unexpected losses on to farmers, by breaching contracts or agreements<sup>6</sup>. Numerous significant incidents posed by this crisis have been witnessed. Rural tensions have accelerated considerably and a growing number of protests and demonstrations have emerged. I maintain along with other experts that in times of crisis, people tend to work together for mutual-aid, and economic restrictions call for more entrepreneurship than in times of full economic prosperity (Badlet, 2003; Defourny and Develtere, 2009; Curl, 2009: 348; Zhao, 2010). Consequently, as a child of necessity, the “co-operative plus farmers” model has been paid more attention to and thus become more and more popular. Co-operatives have flourished and experienced a surge in membership. At the end of 2009, the registered number of farmers’ specialized co-operatives nation-wide has reached 246 thousand. There were 21 million farmers’ household members, accounting for 8.2% of the total number of rural households<sup>7</sup>. Rural population has returned to working together again, to providing mutual help to each other, as well as to empowering themselves to satisfy various economic, social and even political needs that can otherwise not be met in times of rural crisis.

### 3. The development of multi-stakeholder co-operatives in China

Mutual-aid co-operatives might help farmers in increasing their income through working together, although it is not always the case in reality. However, it is nevertheless clear that numerous yet scatted rural economic co-operatives are still powerless and incapable

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<sup>5</sup> It has been described by a then local cadre Li Changping as “the peasants are really in pain, the rural areas are really in poverty and agriculture is really in danger”, in a famous letter to the Premier of China in 2000.

<sup>6</sup> More on capitalist model versus co-operative model and the example involved in China, please see Zhao (2009).

<sup>7</sup> The information is provided by a Chinese official from Ministry of Agriculture. Available at the website of China Farmers’ Co-operatives:

<http://www.cfc.agri.gov.cn/cfc/html/87/2010/20100222174349079942432/20100222174349079942432 .html> (accessed 22 February 2010).

confronting great social and environmental challenges brought by (1) a severe lack of social service delivery and financial service in rural areas, (2) agriculture's ecological sustainability crisis and land/food pollution, (3) vulnerable employment opportunities, as well as (4) dissolution of rural communities in the process of urbanization and industrialization. All these problems give us reason to believe that in rural China, various pressing needs arise in a vacuum that cannot be effectively filled by traditional co-operatives.

During the period of People's Communes, supply and marketing co-operatives were served as rural centers of providing a series of comprehensive production and social services to the rural population. However, they have afterwards transformed into state-owned, commercial companies, not being real co-operative entities any more. How to meet the need of social services in rural China has become local population's basic problem. Another serious problem they face is the access to credit. Rural credit co-operatives, which were established at about the same time as supply and marketing co-operatives in the 1950s, were once the main source of providing small-scale, rural, local-level financial services. These co-operatives lost their co-operative characteristics while the commune system was in place, and have since become an official financial system – regarded by farmers as a government's branch.

In China, in the early of 1960s after the three years of Great Famine, more emphasis from the traditional farming was shifted to chemical fertilizers. Three decades after the Chinese government initiated a series of institutional changes and reforms designed to boost efficiency in agricultural production, China has now become the world's leader in both chemical fertilizer and pesticide consumption (FAO, 2006). The overuse of fertilizers and pesticides has generated considerable environmental pollution and widespread ecological damage, and thus become a significant problem for rural China. Dale Wen, a China expert, argues that environmental pollution and degradation are most serious in the countryside, yet most NGOs are predominantly focused on urban issues (Wen, 2006). *Nature* recently published an article online, claiming that “acid soil threatens Chinese farms” and “Chinese farmers' rampant use of fertilizers could soon endanger the nation's ability to feed itself”<sup>8</sup>. Consequently, the inorganic and even toxic fertilizers are threatening the food quality and causing negative effects on people's health.

The increase of efficiency in agricultural production has caused the emergence of a great amount of surplus rural workforce that shapes somewhat “disguised” rural unemployment. Although many of them migrate to cities to seek jobs, there still exist abundant hidden surplus labor forces due to the huge population base in rural China<sup>9</sup>. Even for many migrant workers, most of them retain strong links with their rural families. It is important to note that although non-agricultural employment has become common for rural population, such employment tends to be unstable. It is observed that many have recently returned to their rural hometown

<sup>8</sup> <http://www.nature.com/news/2010/100211/full/news.2010.67.html> (accessed 11 February 2010).

<sup>9</sup> It is revealed by Chen Xiwen, Director of the Central Rural Work Leading Group Office. By November 2009, the number of farmers who worked in urban areas hit 152 million.

[http://www.agri.gov.cn/jjps/t20100412\\_1465076.htm](http://www.agri.gov.cn/jjps/t20100412_1465076.htm) (accessed 12 April 2010).

because of various reasons<sup>10</sup>. Therefore, land is still a key element for their life earning and social security. Many scholars insist that the large amount of surplus labor in rural areas continues to exist. Thus how to provide more employment opportunities through farming and land-related work has become a great challenge when confronting the widespread “modern agriculture farming model” nowadays.

Also, over time, this migration trend (especially the young) has presented a severe threat to the survival of local communities, similar to what is happening in many other countries. A mass of coastal areas as well as peri-urban rural areas are characterized by rapid urbanization and industrialization, whose processes are playing a negative role in dissolving local ties and disrupting communities. In consequence of all these needs and challenges, a series of unique and innovative experiences have been witnessed in rural China such as:

- New Rural Reconstruction Movement (NRR)

While being critical of mainstream economic development theories regarding rapid industrialization and urbanization as the panacea, some rural experts propose to build a “farmer-centered” and “rural community-centered” local economy to revive the community spirits and empower rural people. Many activists have practiced many concrete projects which have shaped a vibrant NRR movement, supporting the creation of not only rural economic co-operatives but other forms of social co-operatives as well. This social movement has involved several NGOs and academic institutions, numerous rural co-operatives and associations, and hundreds of self-conscious participants (including academics, social workers, student volunteers, and grassroots’ activists). With great amount of efforts, several institutes have been established, such as: James Yen Institute for Rural Reconstruction in 2003<sup>11</sup>, Liang Shuming Center for Rural Reconstruction in 2004, and Rural Reconstruction Center at Renmin University in 2005, *a.o.*. They have become the training centers for volunteers and grassroots’ activists on how to set up, run and support projects such as co-operatives. Among them James Yen Institute is the first one in rural China to provide trainings for free to farmers who are only required to have a junior high school education and the interest in rural reconstruction effort. After providing the training courses for the first round, they select learners who will be given seed money (in the form of micro-credits) to start co-operatives and credit union, or other social/cultural organizations back in their own localities. The institutes stay in contact with these trainees and bring them back together for re-entry programs where they share experiences. Establishing solidarity co-operatives with economic, social, cultural functions are highlighted. Also organic farming and interaction between producers and consumers has been promoted.

It is indeed a national social movement. Up till now Rural Reconstruction Center at Renmin University, for example, has set up more than 60 experimental villages in more than 15

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<sup>10</sup> These reasons are related, for instance, to unequal treatment rural migrant workers receive concerning economic right and social security in cities, and the recent international financial crisis that causes the closure of many factories in the coastal areas of China.

<sup>11</sup> Its work has been integrated into a later-established social enterprise, the *Guoren Urban-Rural Center for Sci. & Tech. Development* in Beijing in 2008, working together with the latter two centers mentioned in the paper. And this institute has been closed in 2007.

provinces in China. Under this influence, large numbers of grassroots' experiments have been performed although without using this movement's slogan. According to Wen (2006), Even NGOs that are trying to empower the local people may fall into the trap of imposing outside ideas without heeding to local needs. In contrast, this movement, with its members coming not only from the urban elite<sup>12</sup> but also from the rural population, may really empower the local people instead of fostering aid dependency. By encouraging communities to solve problems with their own resources, it follows the old Chinese saying "To help someone, first build up his/her will".

#### - Community Supported Agriculture (CSA) and Fair Trade Movement

Confronted with widespread rural environmental pollution and land degeneration which damage agriculture's ecological sustainability, a multitude of activities have been conducted nation-wide. Among them several CSA social enterprise projects are worth noticing. Being resistant to chemical agriculture, the traditional farming methods are preferred and performed, integrating the land, plants, animals and using polyculture system mix of various crops. Some local farmers (mostly elders) are well aware of the problem and would like to revive traditional farming, but they lack the necessary confidence and energy. Therefore, at the very beginning, the activists need to provide a lot of inputs and effort to convince local farmers to fully abandon chemical fertilizers, as well as to convince conscious consumers from cities of reliable source of organic foods thus ensuring a stable distribution channel and a good price for these labor-consuming products. Some projects started out with urban consumers, while others are promoted by scholars and practitioners with significant support from the volunteers and rural farmers. Some prominent examples are the *Farmer's Friend* in Guangxi<sup>13</sup>, the *Chengdu Urban Rivers Association* in Sichuan<sup>14</sup>, the *Guoren Urban-Rural Center for Sci. & Tech. Development* in Beijing, just to name a few.

To briefly illustrate Guoren Center as an example. This center aims to promote sustainable development by way of pushing forward harmonious urban-rural reactions. Its works are related to the development of co-operative economies, of organic agriculture and ecological

<sup>12</sup> Even so, most urban elites regard themselves as spokesmen of rural population.

<sup>13</sup> Farmer's Friend has expanded to set up two organic-food restaurants in two cities to further support their activities. It is interesting to note that they avoid Western terms such as "organic", preferring the Chinese "tu" (土, literally dirt or earth but also denoting local or native), and regard their project as aimed at celebrating rural traditions while protecting health and environment through direct relations between farmers and consumers, without getting involved in the certified organic market. More information can be obtained from: <http://chinastudygroup.net/2009/10/more-alternative-food-networks/> (accessed 30 October 2009).

<sup>14</sup> This association is dedicated to promoting the natural, recreational, and cultural values of rivers, particularly the upper reaches of the Yangtze River. It supports farmers locally for production of organic food and ecological agriculture. The *An Long Model Village* for Sustainable Peri-Urban Development is one of its projects. The project aims to reduce chemical infiltration and pollution into the river systems that feed into the rivers and also aims to improve livelihoods of farmers in those rural areas by introducing organic agriculture and environmental protection capacity building. It promotes the development of environmental awareness and provides farmer-to-farmer training in ecological agriculture, enabling farmers to conduct good marketing of their organic food. It also helps support the grassroots' volunteer effort of Chengdu's "Field for Hope Organic Market", which is held monthly since summer 2007 to bring fresh products to consumers in Chengdu. For more information, please consult its website: <http://www.rivers.org.cn/>.



construction, of village culture and recreation and of volunteer cultivation, *etc.*. It has supported several projects such as the *Guoren Green Alliance* (a marketing network for environmentally-friendly agricultural co-operatives, combining producers' co-operatives in villages and consumers' co-operatives in cities), the *Little Donkey Farm* (one of China's first experiments of CSA), and the *Organic Agriculture Workshop*, *etc.*. The latter one provides technical support for organic farms, designs ecological toilets and hog houses, and conducts pilot programs working together with local co-operatives and villages to help them in transforming to ecological agriculture model.

#### - New Co-operative Movement

The NRR and fair trade movement aforementioned both belong to a new co-operative movement witnessed in China today. Moreover, the emergence of shareholding co-operatives (SHCs) presents another aspect to illustrate the dynamics of this new co-operative movement.

SHCs used to be regarded as rural enterprises and were criticized for their unorthodox co-operative practices. However, it is observed that this new co-operative system has been recently adopted by newly-established rural agricultural co-operatives, represented by community shareholding co-operatives and farmers' specialized co-operatives. The former type is a China-specific form of farmer-owned co-operatives. This very popular form has emerged in some of the most developed coastal areas as well as in peri-urban rural areas characterized by rapid urbanization and industrialization. Under this social innovation, local residents tend to become shareholders and their land contract rights are converted into shares. But they remain to have their land collectively. Farmers' specialized co-operatives have also in several cases adopted a shareholding structure. This happens commonly in developed areas in China with an advanced level of co-operative development. Our research demonstrates that SHCs have not only proved to be enterprises with social aims - thus different from private companies - but also to be a new co-operative form with a variety of specific features such as the combination of the principles of "one person one vote" and "one share one vote". In contrast to traditional co-operatives, SHCs are more oriented to the whole community and put more emphasis on multiple stakeholder ownership (Zhao and Develtere, 2010). In a rural economy in transition, the SHCs at best represent an attempt to alleviate rural tensions and create employment opportunities. These co-operatives are community-oriented enterprises forging cohesiveness by creating new mechanisms of participation, allowing for the emergence of new solidarities based on bonds of profit-and risk-sharing among stakeholder groups (Clegg, 1998).

#### - The Establishment of Multi-purpose Service Co-operatives (MSCs)

To fill the vacuum of social services in rural China, a number of MSCs have been set up at the village level as pilot projects at the beginning of 2000s. Nowadays almost all the multiply services can be found in village communities having service co-operatives. They function by providing production inputs and consumption goods, culture and sport facilities, health care service, education and training installation, *etc.* all in one. Their establishment is generally the result of multilevel co-operation among public authorities, village collectives, supply and marketing co-operatives at the municipality and township levels, as well as grassroots'

organizations of civil society. Normally, village collectives provide the land as the working place, public authorities offer special funds as initiating capital, supply and marketing co-operatives invest capital and establish community supermarkets and convenient stores. Culture and sport centers as well as libraries are built by local bureaus related, and community health service stations were adopted into the service co-operatives as well. Local social organizations may use service co-operatives as a working platform and co-operate with them to further conduct their specific activities to service the local people. Based on these series of successful pilot programs, in November 2009, The State Council has specially issued a central document to encourage reform and development of supply and marketing co-operatives, identifying and confirming their status as co-operative organizations serving farmers<sup>15</sup>. It inspires them to create new service provisions to render old-age support and child care, as well as employment service for the local communities, etc.. This phenomenon is also recognized and confirmed by Chen Xiwen, Director of the Central Rural Work Leading Group Office of China. He mentions that China continued to attach great importance to the development of social enterprises in rural areas to boost the development in areas such as education, science and technology, culture, sanitation and healthcare, improving the level of basic public services in rural China<sup>16</sup>.

In summary, all these new co-operatives and collective actions aforementioned reflect their basic ideology against the dominant currents of thoughts that emphasize utopian marketization and privatization, as well as industrialization and urbanization as the panacea for local development. These alternative models resonate with Birkhölzer's scenario of "development from within", in which the local people themselves always play a key role in initiating or co-operating to facilitate new initiatives. Actually, these cases are just some among a series which highlight that by combining economic sustainability with a strong social and environmental impact, multi-stakeholder co-operatives can represent the means to ensure the survival of local communities.

### III. A conceptual framework

As mentioned above, the paper is concerned with recasting the SE image in China by highlighting the so-far neglected "co-operative model" in order to gain a better knowledge of social enterprise complexity. This effort is also beneficial considering their fast growth and their growing contributions to satisfying the increasing social needs. Equally important in the paper is the aim of exploring the theoretical understanding on the emergence and development of SEs, which remains an unsatisfactory state of knowledge in the SE studies related. Recognizing this existing theoretical defect, this section starts with looking at two important theories, i.e. the multi-stakeholder theory and institutional theory. Drawing on these theoretical underpinnings and the discussions on general situations of SEs examined above, a model of SE emergence and a conceptual framework to illustrate the SEs' sustainable development will be presented.

<sup>15</sup> See *Several Opinions on Reform and Development of Supply and Marketing Co-operatives* by the State Council, (No. 40, 2009), on the Central Government website: [http://www.gov.cn/zwgg/2009-11/20/content\\_1469137.htm](http://www.gov.cn/zwgg/2009-11/20/content_1469137.htm) (accessed 20 November 2009).

<sup>16</sup> Speech by Chen Xiwen, see: [http://www.china.org.cn/china/2010-02/01/content\\_19343633.htm](http://www.china.org.cn/china/2010-02/01/content_19343633.htm) (accessed 01 February 2010).

## i. The Multi-Stakeholder Theory

Ever since Edward Freeman (1984)'s seminal book, the stakeholder theories have become one of the most influential trends in organizational theories. It is fairly to say that each time the stakeholder theories mushroomed in size too large to structure. Therefore, I can only primarily focus on what kind of main ideas are discussed instead of trying to work out the details of the whole theoretical discussions. The focus on several theorists should however not be interpreted to mean that they are the only important ones influencing discussions on stakeholder theories in the social-political sciences. In the following, the stakeholder theories will be illustrated from the perspectives of the theory justifications in mainstream corporations, co-operatives and NPOs respectively. This analysis should nevertheless not be understood that they are completely different from each other. On the whole, they can all be included into one big family of so-called "organizations". The only purpose of this division-making is to try to make clear their instinct features under the discussions of stakeholder theorizing.

### 1. In mainstream corporations

There exist a multitude of discussions on multi-stakeholder theories in analyzing mainstream corporations, and I do not plan to focus in detail on them (See, for example, Donaldson and Preston for an excellent overall review of the three aspects of the theory; cf. Donaldson and Preston, 1995). However, it is worth noting that numerous discussions on the theory invariably present contrasting views which can be best represented by normative versus instrumental approach respectively<sup>17</sup>. The advocates of the normative approach reach a basic agreement that a corporation's responsibilities should extend to all stakeholders beyond taking conventionally only shareholder/stockholders' interests into consideration (Donaldson and Preston, 1995; Phillips, 2003; *a.o.*).

However, starting from the traditional view of corporation's theory, some others who propose (intentionally or unintentionally) the instrumental approach to stakeholder theorizing, argue that the ultimate purpose of adopting stakeholder practices is the finality of value maximization of the corporations. A similar reasoning is what Michael Jensen, an American economist calls "enlightened stakeholder theory", maintaining that ignoring or mistreating any important constituency cannot help *maximize the long-term market value of an organization* (Jensen, 2002: 77; italics added). Agle *et al.* (1999) and Ogden and Watson (1999) indicate that stakeholders are regarded instrumentally rather than from within a moral frame of reference (cf. Windsor, 2002: 96). In other words, instrumental justifications point to evidence of the connection between stakeholder management and corporate performance (Donaldson and Preston, 1995)<sup>18</sup>. This connection may be linked by motivation<sup>19</sup> or functional relationships<sup>20</sup> to use the

<sup>17</sup> There exists also a descriptive approach to stakeholder theorizing, according to Donaldson and Preston (1995). Freeman in his landmark book also explicitly emphasized this grounding, viewing it as "inherently prescriptive" (cf. 1984: 47). The paper will not put a special focus on it due to the paper length limit, although it regards this also a very important approach.

<sup>18</sup> Donaldson and Preston (1995) present an elaborate literature concerning the instrumental approach, tending to generate implications suggesting that corporations practicing stakeholder management will, other things being equal, be relatively successful in conventional performance terms (profitability, stability, growth, etc.).

theory. But the “entitlements” usage of the theory is misguided and thus flawed (Sternberg, 1999). It is flawed also because it violates the proposition that a single-valued objective is a prerequisite for purposeful or rational behavior by any organization. Therefore, claiming “multiple objectives” means actually “no objective” for the organization and its manager. For this reason, a firm that adopts stakeholder theory will be handicapped in the competition for survival because, as a basis for action, stakeholder theory politicizes the corporation<sup>21</sup> (Jensen, 2002: 68). Correspondingly, a UK social and political theorist Norman Barry holds that “Business practice and business ethics are subject to intellectual strictures that belong to political philosophy because the predominant motive of much business ethics is to *politicize* or *democratize* (emphasis in original) the corporation—to take power away from the stockholders and to vest it in more inclusive groups” (Barry, 2002). Therefore, Jensen concludes that the logical fallacy of these normative arguments should be exposed seeing that “special-interest groups will continue to use the arguments of stakeholder theory to legitimize their positions” (Jensen, 2002: 84)<sup>22</sup>.

The critical argument against normative approach holds further that owners organize the firm (a presumption posited in financial-economics theory) and are (“constitutionally”) entitled to the (residual) fruits of their financial investment: otherwise the organization is definitionally not-for-profit (Windsor, 2002: 87). There exist even some who stand in direct contrast to the theory. To list one example, Friedman's famous pronouncement is that the only social responsibility of corporations is to provide a profit for its owners (1970). Its main justification is that the only bottom line for a business is profit.

However, this critique is regarded by Robert Phillips as one of several “straw-person objections” posed by critics of the theory (2003). Another one, according to him, holds that stakeholder theory implies that “all stakeholders must be treated equally irrespective of the fact that some obviously contribute more than others to the organization” (Jones and Wicks, 1999). This point is highly related to the question of how to balance the various interests of organizational stakeholders. In responding to it, Phillips, also inspired by “Clarkson Principles” (1999), holds the principle of meritocracy as the interpretation of this balance which can also be regarded as the principle of stakeholder fairness<sup>23</sup>. Nonetheless, a distinction is still made between the

<sup>19</sup> It means that people are more likely to take an interest in a process when they consider that they have a stake in its outcome; the stake need not be financial (Sternberg, 1999).

<sup>20</sup> This reasoning is derives from the complexity of the world: many factors must ordinarily be considered when pursuing even ostensibly simple outcomes. This is a basic truth that successful businesses have long understood and respected (Sternberg, 1999).

<sup>21</sup> Because it, in following Jensen's argument, leaves its managers empowered to exercise their own preferences in spending the firm's resources.

<sup>22</sup> According to Jensen, these special-interest groups may well include managers, since “it expands the power of managers, it is not surprising that stakeholder theory receives substantial support from them” (Jensen, 2002: 74).

<sup>23</sup> It means that, according to Phillips, stakeholders should have a slice of the organizational outputs and a voice in how value is added that is consistent with their contributions to the organization. In other words, balance does not imply equality of voice or share of outputs. Voice and share—and therefore a sort of priority—should be based on contribution to the organization. The more a stakeholder group contributes to the organization, the greater their voice and share of value created should be (Phillips, 2003: 162).

organizations in the standard business sense and those with the common goal of fostering social harmony. It is prescribed that in the former case “equity” is most appropriate/dominant principle as a distributive value, which would otherwise be “equality” in the latter case (Deutsch, 1975, 1985; Greenberg, 1990).

Moreover, the proponents of the normative approach believe that if maximizing stockholder wealth is the only ultimate goal for the corporate, other corporate constituencies (stakeholders) can easily be neglected. In a normative sense, stakeholder theory strongly suggests that, ethically speaking, overlooking these other stakeholders is unjustified. Consequently, it makes the theory also prominent in a broader debate on business and ethics.

## 2. In NPOs/NGOs

The necessity to examine the stakeholder theory in analyzing NPOs/NGOs and co-operatives (in what follows) should well become clear in the words of Phillips:

*Stakeholder theory applies [only] to corporations...this focus is only intensified by the tendency of management scholars more generally to concentrate on large, multinational corporations as the objects of their research. This has led to a disproportionate, nearly exclusive attention on the part of stakeholder theorists within business schools on the corporation. Less attention has been paid to stakeholder theory in the context of other organizational forms such as small or family owned business, privately owned concerns of any size, partnerships, nonprofits, and governmental organizations. This may appear appropriate if stakeholder theory's primary role is its opposition to the shareholder wealth maximization view. However, for stakeholder theory to truly come into its own as a theory of strategic management and organizational ethics, it will need to be applied to more than just the large, publicly held corporation.*

(Phillips, 2003: 38-39)

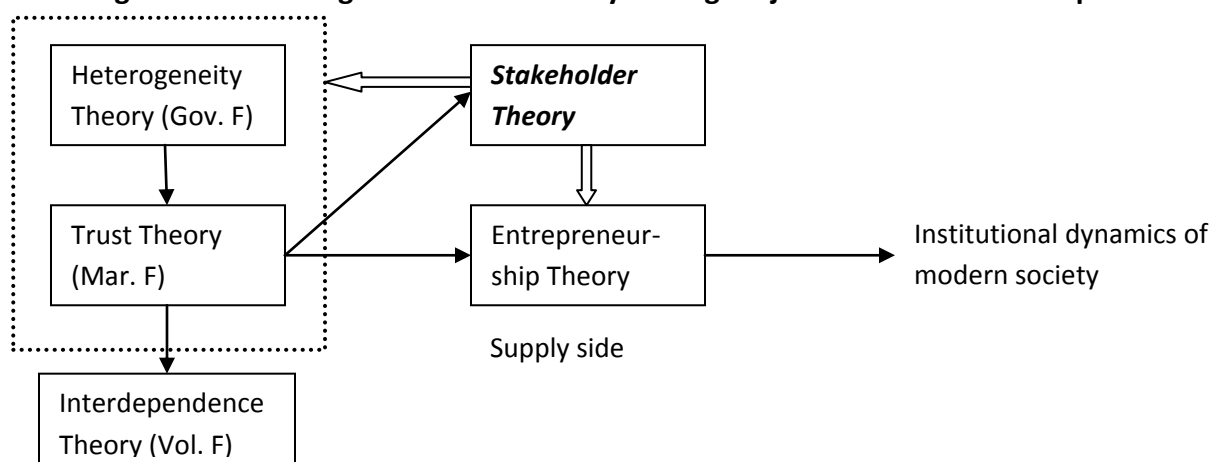
It is acknowledged that the stakeholder theory in NPO studies, associated primarily with the work of Avner Ben-Ner, is also rooted in organizational economics and economic theories of institutions. Ben-Ner and Van Hoomissen combine supply-side and demand-side of non-profits. They argue that non-profits are created by consumers and other demand-side stakeholders in order to “maximize control over output in the face of informational asymmetries.” At the same time, they also acknowledge the supply-side and recognize that non-profits are created by social entrepreneurs, religious leaders, and other actors who are not motivated by profit primarily. They claim that in stakeholder theory, the existence of an entrepreneur is one of the preconditions to be fulfilled so that a NPO is actually formed (Ben-Ner and Van Hoomissen, 1993). They refer to these and all other interested parties on both sides as “stakeholders”. The actions of groups of “stakeholders” are needed. Importantly, these stakeholders require common preferences distinct from governmental preferences or market interests to create sufficient “social cohesion” for the formation and operation of NPOs (Ben-Ner and Van Hoomissen, 1991).

It is widely believed that NPOs are mission-driven rather than profit-driven. Therefore, similar to the question asked concerning mainstream corporations, one tends to ask: what is the bottom line for NPOs, which operate under the non-distribution constraint? One answer is found in conventional approaches to nonprofit governance and management: NPOs have no bottom line

at all<sup>24</sup>. While some others hold that a NPO has several bottom lines. One remarkable example for it is that it is well-quoted that a SE has “triple-bottom lines”, of economic, of social and of environmental. Therefore, it is logical to discern the existence of the debate concerning the agency problem in NPO studies, similar to what has happened to the theory reasoning mainstream corporations discussed above. Steinberg and Gray (1993) coin the term “for-profits in disguise”, to describe the possibility that managers of nonprofits might violate the non-distribution constraint in order to divert the income of the enterprise to their own purposes. This kind of concern is also shared by Hansmann (1980), Ben-Ner (1994), Krashinsky (1997), *etc.*. Ben-Ner (1994: 757) suggests therefore implement legal reforms, which would empower demand-side stakeholders by establishing them as legal “members” and by “linking membership to some status of control” (cf. Krashinsky, 2003).

To better position the stakeholder theory among major theories in the non-profit field, Figure 1 illustrates interlinks between the theory and the other ones. On the basis of Anheier’s introduction, the stakeholder theory builds on Hansmann’s trust argument (Anheier, 2005: 128). As can be seen from above, Ben-Ner and Van Hooissen are one of the few who combine the demand-side and supply-side stakeholders to explain the creation of non-profits. This figure combines also the arguments by the other distinguished non-profit theorists, Weisbrod (1988), Hansmann (1987), James (1987), *a.o.*, who suggested that the very origin of the nonprofit sector is found in demand heterogeneity for quasi-public goods<sup>25</sup>.

**Figure 1 Positioning Stakeholder Theory among Major Theories in the Nonprofit Field**



Source: Author’s configuration.

<sup>24</sup> Peter Drucker once suggested that, because of a missing bottom line, NPOs would be in greater need of management and good governance than for-profit organizations, where performance is often easier to measure and monitor (cf. Anheier, 2005: 227).

<sup>25</sup> It is suggested that even though the theories are examined as “stand alone” bodies of thought, they tend to relate to each other and are more complementary than rival. In other words, even though when taken by itself, a particular theory may have major shortcomings, its explanatory power is significantly strengthened when combined with other approaches (Anheier, 2005: 120). And some other theories should be taken into consideration when examining these “stand alone” bodies of theories. For example, social movement approach can help in understanding the interlink between supply-demand theories focusing on microeconomic level, and interdependence theory from macroeconomic level.

### 3. In Co-operatives

Nowadays, it is widely observed that global changes in the business environments have significantly influenced co-operatives and require new types of co-operative organizations. Numerous cases show that the classic co-operative model with an inward-economic orientation has gradually transformed into a new model with a more outward-community orientation thus forming the emergence and development of multi-stakeholder co-operatives (Pestoff, 1995; Turnbull, 1997; Levi, 1998; Borzaga and Defourny, 2001; Defourny and Nyssens, 2008; Gijssels and Develtere, 2008; Girard, 2009). In 1991, Italy was the first country to adopt a law that formally recognized multi-stakeholder co-operatives as a specific form of social co-operative. Subsequently, Quebec (Canada), Portugal and France also enacted new laws or proposed amendments of existing co-operative laws in 1997, 1998 and 2001 respectively. As Girard (2009) notes, some laws characterize the field of activities of multi-stakeholder co-operatives and others simply focus on the notion of multi-stakeholdership. The cases examined by Gijssels and Develtere (2008) in Europe also prove this trend of co-operative renewal. I argue that, somewhat similar to the supply and demand side theories of non-profits, this co-operative transformation/renewal is by virtue of the pull-and-push efforts from demand and supply sides of co-operatives. These numerous eminent observations make us believe that this phenomenon has become common enough to deserve more profound theoretical consideration.

However, in contrast with countless discussions about multi-stakeholder theories in analyzing mainstream corporations, and several outstanding insights of the theory in non-profit studies, there exist less theoretical underpinnings (especially in English-written literature) for the newly emergent multi-stakeholder co-operatives. As noted well by Phillips, less attention has been paid to stakeholder theory in the context of co-operative organizations. Gijssels (2009) is one of the few who makes this attempt to examine the way co-operatives' stakeholders can be conceived by virtue of the inspiration of the theory<sup>26</sup>. Based upon it she presents a distinction between four models of stakeholder management in co-operatives, a continuum from the classical single-member model to a strong multi-stakeholdership. The division of weak and strong multi-stakeholdership is somewhat similar to Vidal's argument (2009), stating that working as a partnership among different stakeholders has two forms, i.e. multi-stakeholder dialogue (every stakeholder gets a voice) and multi-stakeholder governance (every stakeholder gets a voice and vote).

It is believed that a multi-stakeholder co-operative is, like NPOs, also mission-driven rather than profit-driven, and at the same time, has several bottom lines. Therefore, the potential existence of the agency problem in this new co-operative has also been under debate (Sexton and Iskow, 1993; Cook, 1995; Sykuta and Cook, 2001; Xu, 2005; and Shaw for an extensive overview of corporate governance issues for co-operatives in 2006). Another crucial question under hot debate is concerning the distinction of stakeholders. Based on the attributes of power, legitimacy and urgency Mitchell, Agle and Wood (1997) have identified 8 types of stakeholders.

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<sup>26</sup> Also before, Leys, Van Opstal and Gijssels (2009) have examined the differences of the investor-owned corporations and co-operatively-structured corporations with respect to the position of at least one stakeholder group, whether it is consumers, employees or producers.

A more general division constitutes two main groups: "primary" and "secondary" stakeholders, or "inside" and "outside" stakeholders (Jones, 1995), or "supply-side" and "demand-side" stakeholders (Ben-Ner and Gui, 1993)<sup>27</sup>, or "normative" and "derivative" stakeholders (Phillips, 2003) which follows the taxonomy of Donaldson and Preston (1995). This distinction is surely also varied as a result of a broad or narrow interpretation of the stakeholders. Some prefer the former<sup>28</sup>, while others prefer the latter, and even pragmatically suggest not using "stakeholder" whenever it can be replaced by the other more concrete term (Leys, Van Opstal and Gijssels, 2009)<sup>29</sup>.

## ii. The Institutional Theory

Although the multi-stakeholder theory is very useful in analyzing the complexity of SEs, in general, it is a theory of "conflicting", identified by the literature between various groups of stakeholders: between shareholders and other constituencies (ethical problem), and between managers and owners (agency problem). This contentiousness is due to the complexity of the reality influenced by varied forces of resources (economic, political, social, cultural, ideological, etc.). Therefore, much of the policy discussion refers to "balancing" stakeholders' interests. It not only happens to mainstream corporations, but also to not-for-profits. Krashinsky (2003) argues that a stakeholder approach to nonprofit theory focuses on conflict and ignores some other views of the sector. This balancing among stakeholders tends always to be a result of negotiation or compromise. However, I argue that for an organization that can develop sustainably, like a SE, a true sense of "co-operation" among stakeholders should become the ideological underpinning of the collective action, otherwise it cannot develop sustainably on its own. Consequently, this theory of "conflicting" has to be complemented by a theory of "co-operation"<sup>30</sup>.

Also like multi-stakeholder theories, institutional theories are the ones that have many meanings and engender numerous discussions across and within the social political sciences. Obviously the theories of institution are not necessarily the theories of "co-operation". However, the theoretical findings based upon the reality have recently more and more emphasized this aspect, and an "institutional theory of co-operation" can thus be discerned thanks to this trend. Against the mainstream presumption that rational, self-interested individuals will not act to achieve their common interests due to the free-rider problem, Elinor Ostrom, the Nobel Prize winner, is one of the few political economists to emphasize the collective action, trust, and co-operation. Given the breadth of the topic, I do not plan to give an extensive literature review on her inspiring ideas. Instead, I will focus myself on two important models of her, the models of co-operation in achieving successful collective action.

<sup>27</sup> Krashinsky (2003) further lists private individuals (buyers, donors, and consumers), governments, and producers as "demand-side stakeholders".

<sup>28</sup> Townsley, in a report examining fisheries systems, proposes that the term "stakeholder" needs to be interpreted in the broadest possible sense, at least initially (Townsley, 1998).

<sup>29</sup> They argue that the stakeholder-notion by itself is "empty and often used in vain", and "there is in fact no such thing as 'stakeholder theory'".

<sup>30</sup> Besides, it reflects also a concern in contemporary policy studies to be "multi-theoretic" in reaction to the domination of the single approaches (Gidron and Bar, 2010: 4).

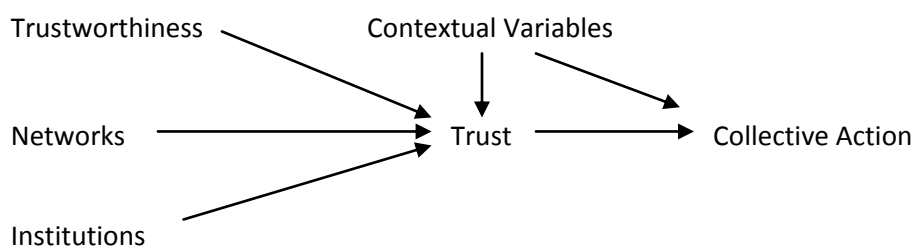


The first model describes the linkage of social capital, trust and collective action. Social capital is considered as an attribute of individuals and of their relationships that enhances their ability to solve collective action problems (Ostrom and Ahn, 2003: xiv). Three broad forms of social capital have been selected: trustworthiness, networks, and formal and informal rules or institutions. According to Ostrom, trust is a key connection point between successful collective action and social capital. Trust is enhanced when individuals are trustworthy, are networked with one another in multiple ways, and are within institutions that facilitate the growth of trust. These relationships are shown in Figure 2. The existence of trust among a group of individuals can often be explained as a result of the presence of some configuration of the forms of social capital (Ostrom and Ahn, 2003: xvi).

Trustworthiness can be explained as “mutual confidence”; repetitive interaction among individuals, a sign of a robust network, provides incentives to individuals to build a reputation of being trustworthy. Institutions are the rules of a game that people devise (North, 1990). This term used by Ostrom here refers to the set of rules actually used—not only rules-in-form but rules-in-use as well—by a set of individuals to organize repetitive activities that produce outcomes affecting those individuals and potentially affecting others. Institutional rules also create incentives for the parties of transactions to behave trustworthily. They can influence behavior directly by establishing mechanisms of rewards and punishment or indirectly to help individuals govern themselves by providing information, technical advice, alternative conflict resolution mechanisms, and so forth. The quality of a rule-in-use depends not only on content but more critically on how they are actually implemented (Ostrom and Ahn, 2003: xviii). SEs are self-governing organizations. According to Ostrom, these self-governing systems in any arena of social interactions tend to be more efficient and stable not because of any magical effects of grassroots’ participation itself but because of the social capital in the form of effective working rules those systems are more likely to develop and preserve, the networks that the participants have created, and the norms they have adopted (Ostrom and Ahn, 2003: xxiii).

**Figure 2 Forms of Social Capital, Trust, and their Linkage to Achieving Collective Action**

*Forms of Social Capital*



*Source:* Adopted from Ostrom and Ahn (2003: xvii).

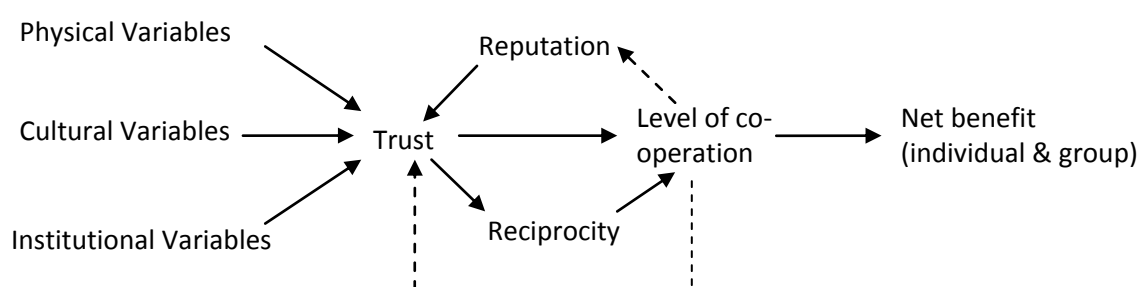
The other inspiring model refers to a model of core relationships among reciprocity, reputation and trust (Figure 3). According to Ostrom, at the core of an explanation of behavior in social dilemmas are the links between the trust that an individual has in others, the investment others make in trustworthy reputations, and the probability of using reciprocity norms. This mutually

reinforcing core is affected by many structural variables as well as the past experiences of participants. She then illustrates it further as:

*If initial levels of co-operation are moderately high, more individuals learn to trust others, and more are willing to adopt reciprocity norms or simply co-operate with others. When more individuals use reciprocity norms, gaining a reputation for being trustworthy is a better investment. Thus levels of trust and reciprocity and reputations for being trustworthy are positively reinforcing. This also means that a decrease in any one of these can lead to a downward cascade. Instead of explaining levels of co-operation directly, this approach leads one to link structural variables to an inner triangle between trust, reciprocity, and reputation as these, in turn, affect levels of co-operation and net benefits achieved both by individuals and groups.*

(Ostrom, 2003: 50-51)

**Figure 3 Feedback in Repeated Social Dilemmas**



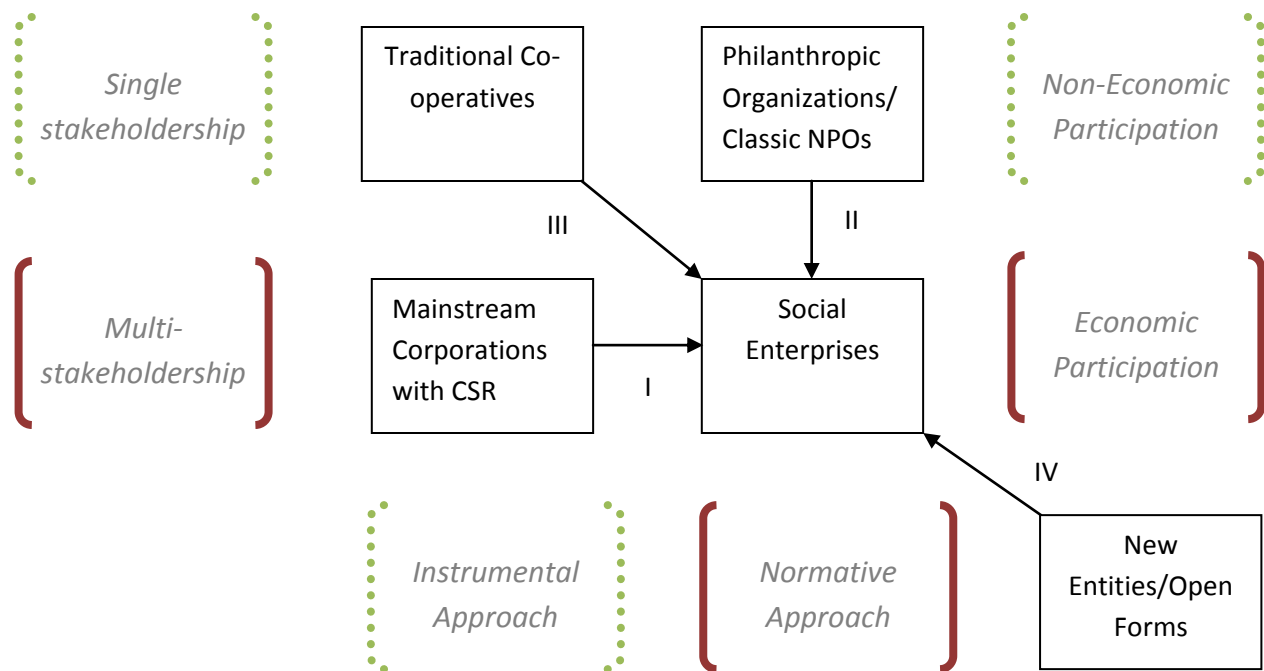
Source: Adopted from Ostrom (2003: 51).

### iii. The Emergence of Social Enterprises—An Organizational Structure Approach

In this part I will address primarily the question how social enterprises emerge, i.e. the origins of SE organizations and the institutional choices involved. Based on the theoretical inputs from multi-stakeholder theories in analyzing three different types of organizations, we can discern how SEs emerge through existing legal entities from mainstream corporations, classic NPOs and traditional co-operatives. An “open form” model of SEs is also identified, representing new spaces created with no specific legal form regulated by the law<sup>31</sup>. Figure 4 illustrates four scenarios of the emergence of SEs.

**Figure 4 The Emergence of Social Enterprises—An Organizational Structure Approach**

<sup>31</sup> For this “open form” model, see Cafaggi and Iamiceli (2009). They maintain that these legal models are likely to create a spectrum of SEs having different legal forms, where the recognized “social finality” of the enterprise will be a better indicator of the SE nature of the enterprise, rather than its organizational form (2009: 15).



Source: Author's configuration.

Note: I-IV scenarios stand for:

I: adding strong social aims in its genes;

II: participating in economic and entrepreneurial activities;

III: orienting to local community;

IV: the consequence of supply-and-demand push-pull forces.

The first scenario is the transformation of mainstream corporations from those adopting pure and ultimate aim of profit maximization toward those by nature having a moral frame of reference embedded in their genes. Acknowledging the instrumental approach of stakeholderhood is in most cases actually driven by motivation of corporate performance in order to achieve profit maximization of the shareholders, or just a display of "culture meme". Nevertheless, it is a weak interpretation of multi-stakeholderhood. Therefore, I maintain that companies adopting corporate social responsibility (CSR) should not necessarily be regarded as SEs initially, especially those whose aim is the finality of value maximization by using CSR as an effective image-propaganda tool. Only are they born to adopt normative approach of stakeholderhood, do they wholeheartedly strive for social finality, care for stakeholder fairness and business justice, and operate as not-for-profit self-sustaining SE model. To raise one example for this scenario, a business program derived from micro-credits is very likely to become a SE by nature.

The second scenario concerns the transformation of classic NPOs/philanthropic organizations from advocacy and non-economic participation to become more open to the economic and

entrepreneurial behavior to achieve their social goals. Nowadays it is widely argued that surplus non-distribution principle cannot serve as a line of demarcation between for-profits and nonprofits anymore (*a.o.* Defourny and Develtere, 2000; Levi, 2005). For example, Estelle James (1987, 1989) argues that the centrality of the non-distribution constraint finds no corresponding weight in the legal and tax systems of most countries. In fact, she finds that the non-distribution constraint may be overstated as organizations can cross-subsidize<sup>32</sup> or engage in indirect profit-taking by increasing personal costs (cf. Anheier, 2005: 126). It refers also to Steinberg and Gray's "for-profits in disguise" case (1993). Actually, various terms once describe this co-existence of nonprofit and economy, such as "nonprofit economy" (Weisbrod, 1988; Levi, 2005), "nonprofit firm" (Easley and O'Hara, 1986; Bonatti, Borzaga and Mittone, 2005), "nonprofit enterprise" (Hansmann, 1980; James & Rose-Ackerman, 1986; Steinberg & Gray, 1993), *etc.*. Therefore surplus distribution cannot be seen as an exclusive feature of for-profits. The cases of this scenario from China are more evident and better observed among the three scenarios, thanks to the efforts of several organizations (like British Council in China, China Social Entrepreneur Foundation, *etc.*) and scholars with nonprofit's training background (Ding, 2007; Chen, 2008; Jin, 2008; Lee, 2009; Yu and Zhang, 2009; *etc.*). Thereby I do not need to repeat and give unnecessary details.

The third scenario refers to the transformation of traditional co-operatives from mutual aims to become more oriented to the whole community, from single stakeholdership to the strong multi-stakeholdership. Why do we need a "strong" multi-stakeholdership here? Cafaggi and Iamiceli (2009: 32) argue that whilst all co-operatives can be characterized as social enterprises, it is possible to distinguish those organizations which are explicitly characterized by social finality and those which are more orientated towards mutuality. Thereby we presume that the former type has a strong multi-stakeholdership while the latter one only has a weak characteristic. Theoretically it finds its potential power thirty years ago in Laidlaw's idea of building co-operative communities (1980)<sup>33</sup>. MacPherson's social dimension of co-operatives is well inspiring with its emphasis of "common capital" system instead of regarding co-operatives as mere agglomerations of members (2004). Empirically, it is widely proved in several countries in the West, one of which is identified by Borzaga and Spear's observation on co-operative movement orienting to the direction of revitalizing the communitarian tradition (2004). In China, the new co-operative movements examined above (NRR and fair trade movements, the emergence of SHCs) answer for this scenario.

The emergence of the fourth scenario is generally attributed to supply and demand theories of social enterprises. The combining effects of the existence of heterogeneous demands of public social services (Weisbrod, 1975, 1988) and the institutional choices of social entrepreneurs (Young, 1981, 1983; James, 1987, 1989; Dees *et al.*, 2001) can trigger new organizations working as SEs with various "open forms". These open forms have also been witnessed in rural China

<sup>32</sup> It means to use surplus revenue from one line of activities to support another, to effect an internal profit distribution to cover deficits. Young states also that "nonprofit may be willing to maximize profits in certain commercial markets where they have a monopoly in order to subsidize their mission-related services (Young, 2003: 163).

<sup>33</sup> It is worth noting that afterwards, ICA adopts the principle of "Concern for Community" and adds it as a seventh co-operative principle in 1995.

nowadays, with the establishment of service co-operatives with multi-purposes presented before as a good example. It shows how these activities are conducted with the multi-level co-operation among various stakeholders in local villages in the normative sense to fill the vacuum of social services in rural China as the ultimate goal. Various services they provide also show that in order to achieve social finality they are operating business to local population. Consequently, we can see that new SE entities created in a local community tend to consciously combine the three prominent features of SEs (multi-stakeholdership, normative approach/social finality, economic participation) ever since the beginning of their existence.

In short, it shows the co-existence of a variety of organizational and legal forms with the similar features and goals (although with different constraints). This line of theorizing holds considerable power in explaining the emergence of various patterns of SEs, which has been testified by numerous cases for each pattern that exists in China.

#### iv. **“Multi-Stakeholder Co-operation” in SEs –A Conceptual Framework**

Following the question answered in the former Part, it comes then naturally to ask: how SEs with various stakeholders aiming at social finality can develop sustainably. Armed with the insights from institutional theories this part will address the question. Although I acknowledge that different legal and “open form” organizations tend to make SEs in reality very complex and far more understandable, I see that there is a large amount of similarities of underlying factors by virtue of institution’s underpinning<sup>34</sup>. Interestingly enough, the complexity of SEs’ activities and organizations are visible, the institutions, as one form of social capital, are yet invisible, especially those working institutions/rules-in-use (Ostrom, 1992: 20). This paradox results in what I ask at the beginning of the paper: does SE complexity just mean this mosaic reality of putting all existing institutions together? Obviously, it can barely be fully understood by this initiative. But still, when one steps back, for all of the complexity, there exist common and shared features of institutions, which shape the patterns and results of individuals’ interactions.

As demonstrated in Figure 5, I call this conceptual framework “multi-stakeholder co-operation” based on two theoretical underpinnings aforementioned. Equally important is the theory of social movement, according to which, ideology, praxis and organization are three interlinked components (see Develtere, 1994). SEs are social value-based or ideology-based organizations, mostly driven by one (or a group) social entrepreneur(s) as local elite. The ideology presents the images of a desirable or ideal model of SE based on a set of values and norms. The achievement of collective actions is under the direct influences from trust that an individual has in others, and indirect influence from a set of variables in a local context in which the SE organization is located (also see Figure 2). These contextual variables are a set of factors that would influence the level of the social cohesion in the local community, such as political preference (local regulations and the attitudes of local officials), economic development level, local cultural value shared by stakeholders in a community, other local entrepreneur-elites’ influences and community support/solidarity, as well as the link to the outside.

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<sup>34</sup> It is inspired by Ostrom (2005).

Trust that an individual stakeholder has in the others is influenced by social capital and various individual's variables of physical, cultural and institutional aspects (also see Figure 2 & 3). These aspects refer to personal economic capability measured by levels of wealth and technology that affect the transformation of activities into outcomes, culture values shared<sup>35</sup>, as well as formal and informal institutions in local situations in which they repeatedly find themselves. These variables, together with the individuals' internal values, constitute four sources of incentives. While the first two are easy to understand, institutional rules are also a source of incentive because they create incentives for the stakeholders during the interactive transactions to behave trustworthily (Ostrom and Ahn, 2003: xviii). It should be noted that the concept of incentives involves more than just financial rewards and penalties (Ostrom, 1992: 24). We see that one important individuals' internal value is stakeholder's trustworthiness. It is also regarded as one source of incentives because it provides incentives to individuals to build a reputation of being trustworthy. Based on the core relationships among reciprocity, reputation and trust (Figure 3), I try to draw up an interactive relationship between two stakeholders by virtue of these three aspects (number 1 and 2 of trust, reputation and reciprocity), in order to exemplify a dynamic interaction between various stakeholders.

Also shown in the Figure, trustworthiness interacts with the network factor, since as aforementioned, repetitive interaction among stakeholders through a robust network provides incentives to individuals to build a reputation of being trustworthy. And at the same time, when individual stakeholders are trustworthy, building a network of commons tend to be much easier and more stable because of this precious assets they share. Another interaction between two different forms of institutions is also marked out in the Figure. It is widely accepted in institutional studies that rules-in-use are not always the same as formal laws and regulations. And changes in formal regulations do not automatically become changes in rules-in-use and thus in incentives. Thereby the incentives facing individuals cannot be determined from a reading of promulgated laws and regulations without examining how those regulations are perceived by participants and how they fit into the physical, economic, and social context of a particular system (Ostrom, 1992: 26-27). That said, these two forms of institutions can convert from one to the other. It can be testified by the fact that many newly-emergent legal institutions for SEs around the world are derived from formerly-existed "open forms" with no specific legal institutions regulated by the law. Even the establishment of national co-operative law in China has followed this logic. The existing formal institutions may also inspire the emergence of new rules-in-use, since the reality varies continuously, and today's written regulations may not meet the need in the field tomorrow. Ostrom puts this argument forward in this way: as environments change over time, being able to craft local rules is particularly important as officials far away do not know of the change (Ostrom, 2005: 263). From the hot debate on NPO's non-surplus constraint regulation and the fact that many not-for-profit SE forms actually operate beyond this regulation, one can also easily discern this argument.

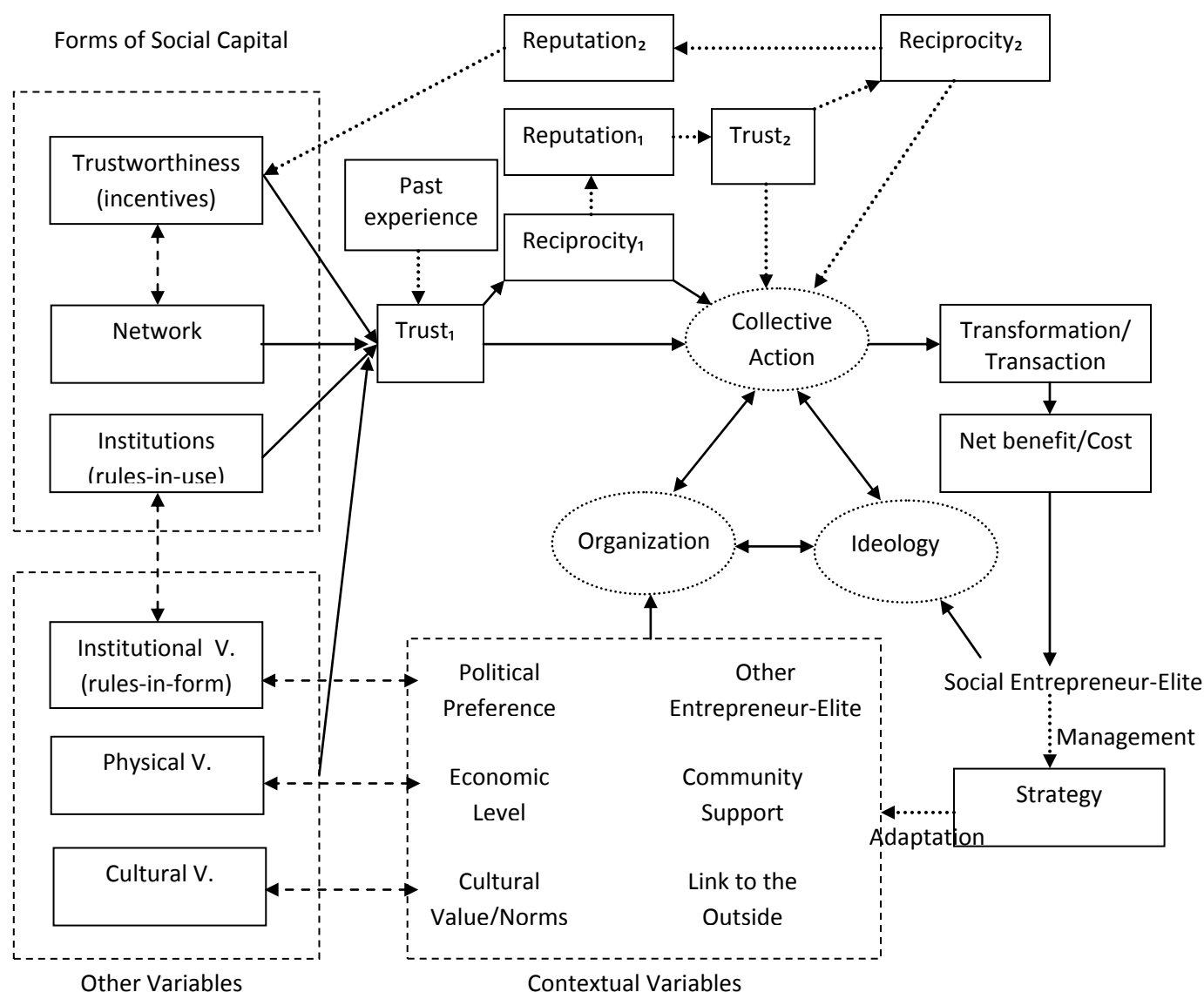
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<sup>35</sup> I agree with Ostrom that if the cultural values of two interacting groups differ substantially, these groups may face entirely disparate incentives even though their physical situations are relatively similar, therefore trust in each other tends to be difficult to achieve.

Let me now illustrate how social entrepreneur/local elite as an initiator of SE can manage the collective action of co-operation thus successfully achieving the normative ideology of SE. Two types of activities among stakeholders should be identified: transformation and transaction (for a general discussion, see Ostrom, Schroeder, and Wynne, 1990; cf. Ostrom, 1992: 27). Transformation activities are directed toward changing one state of affairs into another. Transaction activities are directed toward (1) the coordination of transformation activities, (2) the provision of information, and (3) the acquisition of a strategic advantage over others (Ostrom, 1992: 27). Since transformation activities require the inputs of multiple stakeholders, good physical capital and substantial human capital, and various forms of social capital are needed for complex interconnected activities to be undertaken successfully (Ostrom, 1992: 29). All transaction activities requiring inputs from multiple individuals will lead to transaction costs. The rules that specify who is to coordinate with whom about what, and how information is to be recorded and transmitted, affect the level of transaction costs (Ostrom, 1992: 31). Therefore, who craft institutional rules find creative mechanisms to keep these costs low. When institutions are well crafted, opportunism is substantially reduced. The temptations involved in free riding, rent seeking, and corruption can never be totally eliminated, but institutions can be devised to hold these activities in check (Ostrom, 1992: 35). The social entrepreneur, as the coordinator and (in most cases) the institution's crafter as well, is responsible to mobilize the inputs/contributions of transformation activities from various stakeholders and at the same time keep transaction costs low. If resources required to achieve SE's social goal are not enough, or the costs are too high due to ineffective coordination or slow information dissimulation or information non-transparency, the social entrepreneur should be well aware of the risks impeding a sustainable development, and thus should device management strategies adaptive to the outside environment featured by a set of contextual variables. This adaptation further adjusts the collective action of co-operation by way of improving the coordination and information dissemination in the SE organization, or mobilizes more contributions by enhancing the trust needed in collective action. Sometimes, the success of this input-mobilizing effort lies on the principle of stakeholder fairness which is under controversial debates between proponents of the instrumental approach of the stakeholder theory and those of the normative approach<sup>36</sup>. That said, one can still use Phillips (2003)' distinction for reference. This distinction between normative and derivative legitimacy brings together both moral philosophical and strategic conceptions of stakeholder theory and thereby integrates these two often opposing streams of stakeholder research (Phillips, 2003: 123).

#### **Figure 5 A Conceptual Framework of Multi-stakeholder Co-operation in Social Enterprises**

<sup>36</sup> Ostrom points out this issue as well, stating that considerations of equity and fairness also affect the likelihood of individuals adopting conditional co-operation in collective-action situation (Ostrom and Ahn, 2003: xx).



Source: Author's configuration.

#### IV. More Empirical evidence—A Complementary Case

In Section II I have introduced several empirical evidences of multi-stakeholder co-operatives' emergence in rural China to demonstrate a series of unique and innovative experiences witnessed. Although my conceptual framework is about multi-stakeholder co-operation in SEs, I am fully aware of the fact that, in reality, the action of co-operation between various stakeholders does not always happen, especially for the case of relatively large-scaled SEs<sup>37</sup>. Therefore, a complementary case is presented below, with the purpose of illustrating further my conceptual framework. This distinctive case is meant to present an opposite situation, to

<sup>37</sup> But I do not mean to assert that all local small-scaled efforts work well and all large-scaled efforts work poorly.



show the difficulty a SE has in achieving multi-stakeholder co-operation in reality, which can lead the SE to slow down its speed confronting obstacle to sustainable development.

In Section II I illustrate the emergence of traditional co-operatives in China in times of rural crises and their incapability confronting a series of challenges. It is widely agreed among Chinese co-operative experts that they cannot become strong nor solve the fundamental problems of rural China on their own, because they are small-scaled, atomized and scattered from each other, lack of financial support and community base<sup>38</sup>. Thus an idea of combining various co-operatives together and integrating them into a co-operative association based on its local community has been long desired in China. This comprehensive rural organization has already been established in Japan, South Korea and Taiwan, and it is really suggested as a better way to China's co-operative development comparing with the Western way, because of similar national conditions China shares with these Eastern regions. This experiment has been finally put into practice in one city in Zhejiang Province, promoted by a vice mayor who had been appointed from Beijing after his post-PhD graduation.

As a response to meet the comprehensive demands for the development of the agricultural economy and rural life, a Rural Co-operative Union (RCU) in the city was established in March 2006. With its membership dimensions varying from extremely small to big, it is composed of organizational members such as local farmers' specialized co-operatives (FSCs), supply and marketing co-operatives (SMCs), local rural credit co-operatives (RCCs), local Agricultural Bureau (AB), local Office of Rural Work (ORW)<sup>39</sup>, other financial systems<sup>40</sup>, local Science & Technology Bureau<sup>41</sup>, Youth League Committee at local level<sup>42</sup>, as well as all farmers<sup>43</sup> as individual members and student and youth volunteers. There are two specific features concerning membership design. Firstly, all the members are divided into different categories: FSCs, village economic co-operatives and credit mutual co-operatives are regarded as *basic members*; SMC associations, RCC associations (co-operative banks), and various FSC associations are functioned as *core members*; general farmer householders become *associative members*. Different members enjoy different rights in the RCU, but all of them have the right of suggestion, right of supervision and right to criticize. Secondly, a double-membership system is established, which means the members of co-operatives turn automatically to be members of the RCU once the co-operatives join the RCU to become its members. Through this innovative integral construction,

<sup>38</sup> There exists a wide debate on whether this sort of farmers' specialized co-operatives supported by the government is a form of "big members deprive small members" or "small members eat big members". From this fact one can easily discern that various stakeholders in farmers' specialized co-operatives in China actually tend not to co-operate by nature.

<sup>39</sup> It needs noting that although their works are both related to the "three rural issues", local AB and ORW are still two separate governmental authorities. The former one belongs to the vertical systems of Ministry of Agriculture, the latter one comes down vertically from the Office of the Central Rural Work Leading Group.

<sup>40</sup> They are: local bureau of the China Banking Regulatory Commission, and sub-branch or local office of the People Bank of China.

<sup>41</sup> This bureau comes vertically from the system of Ministry of Science and Technology at the central government level.

<sup>42</sup> At the highest level of the system is Youth League Central Committee.

<sup>43</sup> It is stipulated that all farmers in the City can automatically own their membership qualification, no matter being members of a co-operative or not.

it combines different stakeholders in the local area into one organization. This design aims to fully exploit the rural community advantages by way of integrating various grassroots' organizations, thus establishing a new pattern of organizational work: integration of departments and regions at different levels, putting farmers in the first place of engagement while stipulating community involvement. Various departments are set up in the RCU, including those of credit, of supply and marketing, of co-operative direction, of judicial service, of information communication, and of land circulation, etc..

The promoter of this institution does not regard co-operatives as merely economic organizations but not-for-profits with social (co-operative) missions. He devises this integral construction as a federative system, but not the one of a traditional kind. Through varied member categories and the double-membership system, it represents an emergent form which facilitates both the connection of various scatted co-operatives, and the communication between co-operatives and the farmers, as well as between the RCU and the farmers directly. Based on the current pattern of interests constituted by all the public authorities and civil organizations concerning agriculture and rural works, it aims both to connect different types of third sector organizations working at different hierarchic levels, and to promote a public-civil society partnership. This partnership-building is expected to be multi-purpose: to solve the problem of critical shortage of social and financial services in rural areas, to further promote the SMC and RCC reforms and FSC's standardization building, and to remedy the farmers' vulnerable position thus to increase the social harmony.

It has carried out a number of activities and really been regarded as a social innovation. Ever since its establishment, it has been widely reported<sup>44</sup> and highly awarded<sup>45</sup>. More and more attentions have been paid by politicians of the central government and the other local governments, who have tried to follow suit.

However, after a period of development it has come across more and more difficulties and critiques, less and less attentions and reports, and finally undergone a severe crisis. These critiques are actually the result of conflict of interests among different stakeholders inside and outside the RCU. Various public authorities involved as organizational members have finally conflicted against each other due to their departments' interest groups; local officials are divided as supporters and opposers of the RCU due to their delicate relationships with each other; moreover, conflicts exist between large rural households with more resources and capital and small ones. In the words of that vice mayor, it is a "game of co-operation". Therefore, this beautiful design ended in a deadlock.

Different opinions arise. Some propose that the RCU cannot coordinate all the stakeholders with various groups of interests, some regard it unpractical to crown the RCU with all the laurels, some are worried that the promoter's blind passion would definitively lead to disappointment,

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<sup>44</sup> There exist surely more than 200 media and academic reports.

<sup>45</sup> It was once awarded as one of the most excellent local innovations in China, one of the 10 greatest explorations of China's reform, one of the 30 most innovative cases after China's reform and opening-up, etc.. This practice was also confirmed by Ministry of Civil Affairs and British Council in China on the *Forum of Social Innovation and Social Organizations* in December 2008.

some criticize that this experiment is too ahead of the times to conform with the China's current national conditions, while some think that the RCU goes in all directions at once, which makes it under attack on all sides, thus landing itself in a tight place. During the interview with this institutional design's promoter, I am informed that the RCU is now under the progress of readjustment and contraction. He proposes that the battle field now is not in the City but in Beijing, where he is now making efforts to promote the legitimacy of this organizational arrangement with the formal confirmation from the central government by stipulating a national law of RCU. Without the formal regulation, it would become impossible to promote the RCU to go further in this game of co-operation<sup>46</sup>.

From this case we can see how local elite as the initiator of this social change can successfully manage the collective action of co-operation in the beginning but fails to go further later. Inside the RCU the core relationships among reciprocity, reputation and trust were established in the beginning with the great effort by the initiator to persuade each organizational member individually that its political position would not become lower in the RCU's institutional arrangement. Each stakeholder had thus the incentive to co-operate with the expectation that it would gain more interests without expenses. This co-operation opportunity is expected to glorify their current political images, gain public appraises from the farmers and thus affirmations from each other's upper level of the authorities. It is therefore not a normative value-based co-operation. Those core relationships are not strong by nature, hence when the RCU received wide attentions later and more awards and reports, the organizational member stakeholders were not content that the RCU itself (and its initiator) is highly praised but not them. Moreover, the initiator was appointed from outside (although he is very knowledgeable and widely-experienced), which makes him more difficult to build genuine trust thus strong social capital. It further influences the collective action achievement. Outside the RCU, furthermore, various public authorities at the upper level highly influence the decisions of those organizational members due to their departments' interest groups as mentioned above. Some authorities at the provincial level later promote an alternative form<sup>47</sup> and require their subdivisions in the City to establish similar organizations, thus breaking away from the RCU. It is just one example to show how the contextual factors can influence the level of the social cohesion in the local community. As a result, transformation and transaction activities among stakeholders have become no success due to the fact that motivating inputs and resources from various stakeholders is very difficult, and transaction costs are too high because there exist actually no unanimous agreement on the institutional rules specifying who is to coordinate with whom about what. Confronting the severe crisis of existence, the crafter of this social innovation has now really pinned his hope on converting this experimental, informal institution in the local area into a well-acknowledged, formal law nation-wide. Nevertheless, he is very hopeful that this experiment with civil society's effort will further promote the public-civil society partnership aforementioned.

## V. Conclusions

<sup>46</sup> Interview with the vice mayor of the City, 4<sup>th</sup> November, 2009, Beijing.

<sup>47</sup> An example is "rural co-operative association", which sounds similar with the RCU, or rural co-operative union.

In this paper, I have re-casted the SE image in China by highlighting the so-far neglected multi-stakeholder co-operative model in order to gain a better knowledge of social enterprise complexity. The reality of vulnerability of rural population and rural communities has posed a series of challenges to local development. The existence of demand for rural comprehensive needs has stimulated large amount of social experiments. By presenting empirical studies on a series of unique and innovative practices in Section II, I have introduced the reality of the emergence of multi-stakeholder co-operatives in China. The complementary case examined in Section IV provides some evidences on how a SE with multi-stakeholdership can (or cannot) develop sustainably. It should be noted however that the focus on multi-stakeholder co-operatives in rural communities of China should not be interpreted as a position that they are the most important factor in SEs, nor rural areas in China are the only stage for these SE activities. In times of prosperity, they may diminish greatly in their importance in influencing people's behavior of co-operation. From the empirical evidences only one conclusion is tenable: the multi-stakeholder co-operatives in China are proved to be a model of social enterprise. It turns to be a model of "development from within", a model alternative to industrialization and urbanization as the panacea for local development, a model to ensure the survival of local communities.

Besides the contribution of adding these observations on multi-stakeholder co-operatives as a so far being-neglected yet important supplement to complete empirical evidences on SEs in China, the paper further contributes to making up the theoretical defect in the SE studies. By drawing on the multi-stakeholder theories and institutional theories it has explored the theoretical understanding by presenting a model of SE emergence, to illustrate what trigger the SEs' emergence through existing institutions and through creating new spaces in four scenarios: by adding strong social aims in mainstream corporations' genes, by participating in economic and entrepreneurial activities for classic NPOs, by orienting traditional co-operatives open to local community, and by creating open forms at the consequence of supply-and-demand push-pull forces. Equally important is the attempt to present a conceptual framework to illustrate the determinants of the SEs' sustainable development.

Finally, one last yet very decisive research question raised in Section I should be answered: whether the current SE research is just a fancy study which actually means old wine in new bottles, or it is indeed a new approach which is "strongly" enough to represent the new "spirit". The fact that the studies on SEs in China (and in East Asia) have mushroomed in size makes one tend to believe that the term "social enterprise" has become a symbol for many practitioners and scholars in the field. However, it is not by itself important unless it helps in refining our knowledge and in closing the gap in understanding the integration effort to create an area with common ground and shared values. What is important, especially at this initial period of the concept's adoption and development, are the underlying ways of thinking. Unless the significant thoughts are well-developed, direct attempts at observing existing institutions is a practice of "old wine in new bottles" and will not advance nor accumulate knowledge. Therefore, to incorporate and build a coherent framework helps in studying the process of how old spirit is refined thus becoming new wine good for new wineskins. Although the model and framework presented in the paper are still initial and preliminary, I hope they become a stimulus to still further efforts, in order to make the new spirit more mellow and aromatic.

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