

PROFIT-WITH- PURPOSE BUSINESSES

Subject paper of the Mission Alignment
Working Group

**SOCIAL IMPACT
INVESTMENT TASKFORCE**

Established under the UK's
presidency of the G8

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Cliff Prior

***Chair, Mission Alignment Working Group
September 2014***

Dedication

This Report is dedicated to the life and work of our respected colleague, Stephen Lloyd, who created so much of the framework for social ventures and social investment in the UK, and who was a tireless champion and supporter of the social economy. Stephen was highly involved as a member of the Mission Alignment Working Group until his untimely death in August 2014. His legacy lives on through the thousands of social ventures that use the legal structures he developed and through the new initiatives contained in this Report.

EXECUTIVE SUMMARY

Across the world, attitudes are changing. Old certainties about tightly defined roles for government, civil society and business are dissolving. Social sector organisations are becoming more business-like, and business is looking ever more to delivering sustainable value.

The Deloitte Millennials Report in 2013 showed that young people believe that the number one purpose of business is to benefit society, and the 2014 report showed that fifty per cent want to work for a business with ethical practices.¹

A number of countries have already created the legal mechanisms to allow for an intermediate type of organisation, which generates revenues from commercial activity to support its social mission and reinvests most or all of its profit to further its social mission. Sometimes called social enterprises² or solidarity enterprises³, these businesses are delivering social impact in exciting ways.

A growing number of for-profit companies are going more social, to focus on creating positive impact, and reporting on their progress in achieving it. We welcome this trend, and the work of investors to scale up the impacts they create.

We now see a further evolution as entrepreneurs create a new style of business: fully profit-distributing, and with a long-term commitment to prioritise, deliver and report on their social impact. We refer to these as **profit-with-purpose businesses**.⁴ **They are the centrepiece of our recommendations.**

Profit-with-purpose businesses form part of the wider group of 'impact-driven organisations', as defined by the Social Impact Investment Taskforce. They are flanked by non-profits and social and solidarity enterprises on one side, and on the other side, 'businesses-seeking-impact' which set significant outcomes objectives but do not lock in their mission.

The Mission Alignment Working Group believes that profit-with-purpose businesses will create substantial social impact and will attract investment to enable growth. Building the right frameworks will encourage more entrepreneurs to commit to delivering social impact. Profit-with-purpose businesses are at the junction of impact and investibility, particularly at the early and growth stages of the enterprise journey, where the risks are high and investment through equity is most appropriate.

We identify a definition, a legal framework, starting positions, market mechanisms, and existing systems to build upon. The core model we propose has three pillars: Intent, Duties, and Reporting. Intent to achieve social impact, a duty to strive to achieve that impact, and reporting to demonstrate the impact created.

Our model will allow impact-driven businesses a mechanism to commit to this for the long term, should they wish to do so. Other entrepreneurs may choose to use standard legal forms that do not include a mission lock and instead seek to continue the mission of their business in another way.

1 www.deloitte.com/MillennialSurvey.

2 For the purposes of this report, 'social enterprise' refers to a business with a primary social mission, which has partial or full restrictions on the use of its assets and/or profits in line with that social objective. It is distinguished from a traditional non-profit or charity in that it generates a substantial proportion of its income through trading rather than through grants and donations. It may or may not be associated with a particular legal form, depending on the country.

3 For the purposes of this report, 'solidarity enterprise' refers to the category of businesses that qualify as 'entreprises solidaires' in France. It is roughly equated with 'social enterprise', but has various alternative qualification criteria including those related to the proportion of employees that have particular challenges in accessing the labour market; democratic governance; salary ratios of the highest- and lowest-paid employees, etc.

4 For the purposes of this report, 'profit-with-purpose business' refers to a business which has a primary social mission and has restrictions on amendments to that mission through locking it in or embedding it in its business, but has no restrictions on the use of its assets or profits. We describe the defining characteristics in more detail in this report.

We believe that there is good evidence that a substantial number of entrepreneurs, investors and customers are already on this path: there could already be at least as many profit-distributing, impact-focused businesses as there are social/solidarity enterprises and trading non-profits.

We also include routes for countries which still have no intermediate form between non-profit and commercial business, and which may not yet feel it appropriate to adopt profit-with-purpose business, to allow for social enterprise or solidarity enterprise as their next step.

Our recommendations are also relevant for other for-profit businesses. We include reporting mechanisms and legal changes which would also be useful to 'businesses-seeking-impact', which are prepared to focus on impact and report on progress, but which do not feel it appropriate to commit to an impact mission for the long-term.

Throughout our report, we use the term 'social' as a shorthand to also include environmental benefit. In addition, we include co-operatives, mutuals, limited liability partnerships, and other forms of business organisation in the term "enterprises", recognising the very different traditions across countries and cultures.

Adoption of the recommendations contained in this report will open up a new set of social impact opportunities – for entrepreneurs, for investors, and most important of all, for the people who will benefit from the impacts delivered. This report offers a structure for businesses to commit to, implement and report on social impact, and some tools to make this easier.

Our report is the starting point for a new and thriving sector of profit-with-purpose business, which could stimulate a major increase in impact investment.

INTRODUCTION

It is becoming clear that substantial numbers of entrepreneurs are interested in creating profit-distributing businesses for social impact.⁵ The best available data suggests that there could be at least as many profit-distributing, impact-focused businesses as there are asset- and profit-locked⁶ social enterprises and trading non-profits. For example, in the UK, there are approximately 100,000 such businesses focused on creating social impact, representing 8% of all UK small- and medium-sized enterprise (SME) employers.⁷

If we can create the legal and market mechanisms to allow these businesses to thrive as identified, profit-distributing and mission-driven enterprises, they have tremendous potential to create social impact. As profit-distributing businesses, they are likely to attract capital to deliver this potential more easily than asset- and profit-locked enterprises. And creating ways to allow these businesses to firmly lock in their social mission will give confidence that the businesses will continue to achieve social objectives in the long-term, helping to attract socially-minded investors.

In practice, there are a variety of legal forms that such 'profit-with-purpose businesses' can take. In some countries, new legal forms are being introduced that are specifically intended for this class of business. Beyond this, social entrepreneurs choose from the wide range of existing forms and hybrids that are available to all businesses, which vary across countries and legal traditions.

This diversity makes it hard to recognise profit-with-purpose businesses at present. Their legal form may be indistinguishable from traditional businesses. They may find it hard to convince critical stakeholders – social impact investors included – of their social mission and their commitment to it, as the old dichotomy of non-profit versus for-profit becomes blurred.

How can we tap in to this opportunity, and provide the mechanisms for these businesses to hold true to their social mission, creating confidence for regulators, customers, investors, employees and beneficiaries? Fundamentally, the challenge is about trust: it is about creating the confidence, that we are talking both about real businesses, and about real commitment to create social impact for the long term.

This was the starting point for the Mission Alignment Working Group of the Social Impact Investment Taskforce established under the UK's presidency of the G8. We focused on the aim of attracting capital for investment in profit-distributing businesses that lock in a social mission and that deliver social impact. The objective is for these businesses to scale up their social impact.

⁵ Throughout this document, we use the term 'social' in a broad sense, to include social and environmental purposes and impacts.

⁶ For the purposes of this paper, we refer to 'asset lock' as a combined restriction that (i) during the life of a company its assets will not be disposed of for less than their value except in furtherance of the social impact purposes of the company, and (ii) upon winding up, the assets of the company remaining after all debts have been settled will be transferred to a company with an asset lock and similar social impact purposes. An asset lock does not apply to profits when initially earned by a company, but will apply to any profits reinvested in the company in lieu of distribution to the owners. We refer to 'profit lock' as a restriction on the distribution to the owners of a company of the profits earned by the company, either during the life of the business or upon liquidation. Note that 'asset lock' is sometimes used more generally, to refer to both of the above.

⁷ Calculated from data in BMG Research (2013) Social Enterprise: Market Trends (Based upon the BIS 2012 Small Business Survey), UK Cabinet Office: London. 98,366 (54.8%) of the 179,500 employer SMEs that have a good fit with a social enterprise definition are registered as private limited companies, partnerships and PLCs. The total number of SMEs that employ staff is 1,230,395.

Box 1: The Working Group's mandate

“For the field (of social impact investment) to develop, investors need confidence that the profit-with-purpose companies they finance... will continue to achieve social objectives even beyond change of ownership. The [Mission Alignment Working Group] will examine ways of achieving this through corporate form, governance, and legal protection and make recommendations.”

The investment could be made by social investors, commercially-oriented investors, or a combination of both, at both institutional and retail levels. This report summarises our conclusions and recommendations.

Our recommendations focus particularly on profit-with-purpose businesses. We believe the

solution is greater clarity and recognition of what could be regarded as a new class of business, together with an enabling legal and policy framework in each country, and a set of tools and mechanisms to demonstrate the impact delivered. We propose an international framework that is necessarily high-level, dealing with principles, to allow for the very different legal, political and cultural starting points in each country. Finally, we provide a selection of case studies illuminating how profit-with-purpose businesses work and how investors can provide capital for growth.

We recognise that there is a wide range of impact investing methods, and an equally wide range of investors seeking social impact, each with their own priorities, boundaries and preferred methods. We do not seek to constrain the activities of impact investors to any particular approach. Rather, we focus on the enterprise side, providing a new opportunity for entrepreneurs to ensure their impact-driven businesses can both raise investment finance and lock in their social missions even beyond a change of ownership.

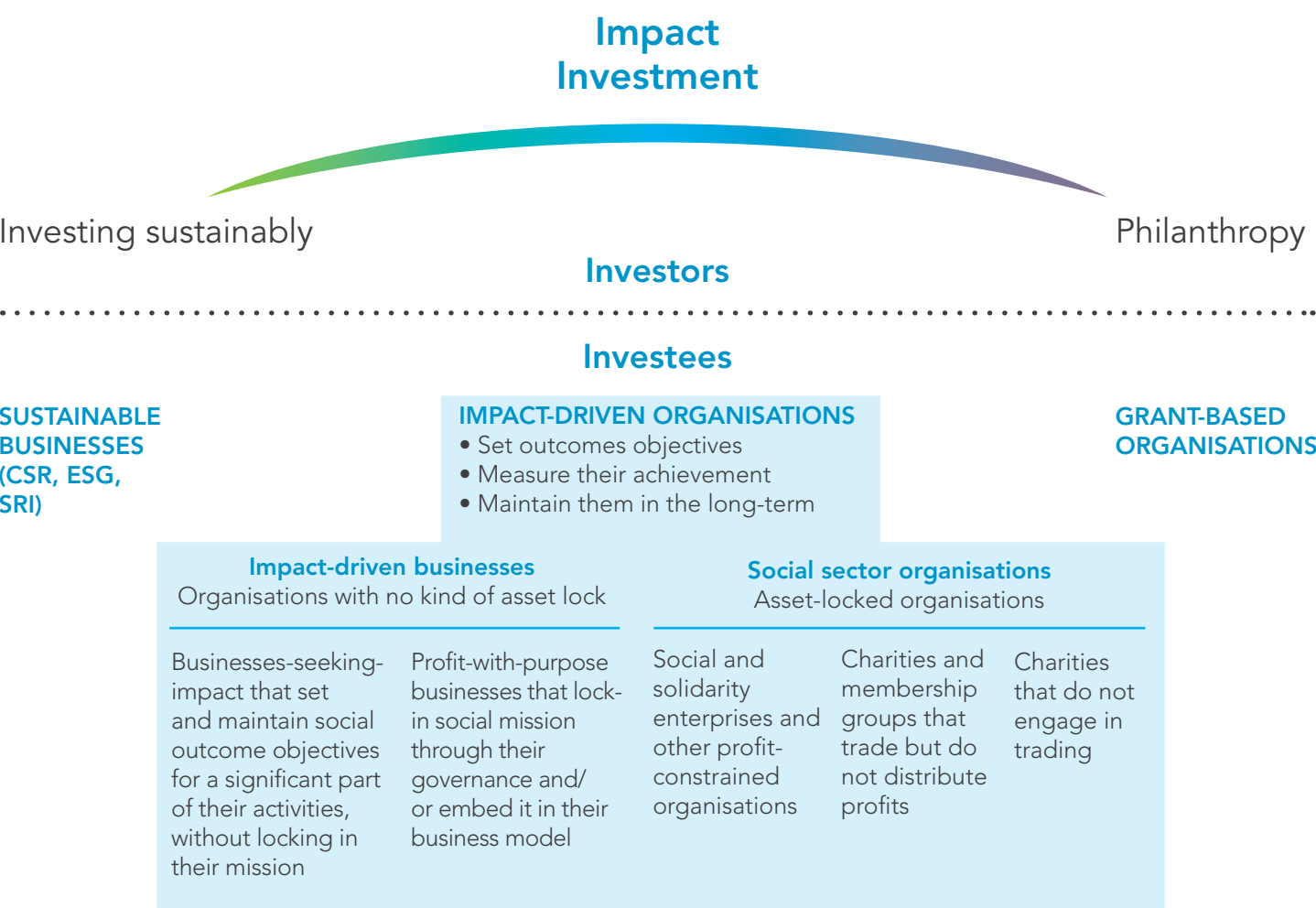
PROFIT-WITH-PURPOSE BUSINESS: A NEW SECTOR FOR SOCIAL IMPACT

This report focuses on the creation of a new form of enterprise: profit-with-purpose businesses. They sit within the spectrum of impact investees as described by the Taskforce (see figure below).

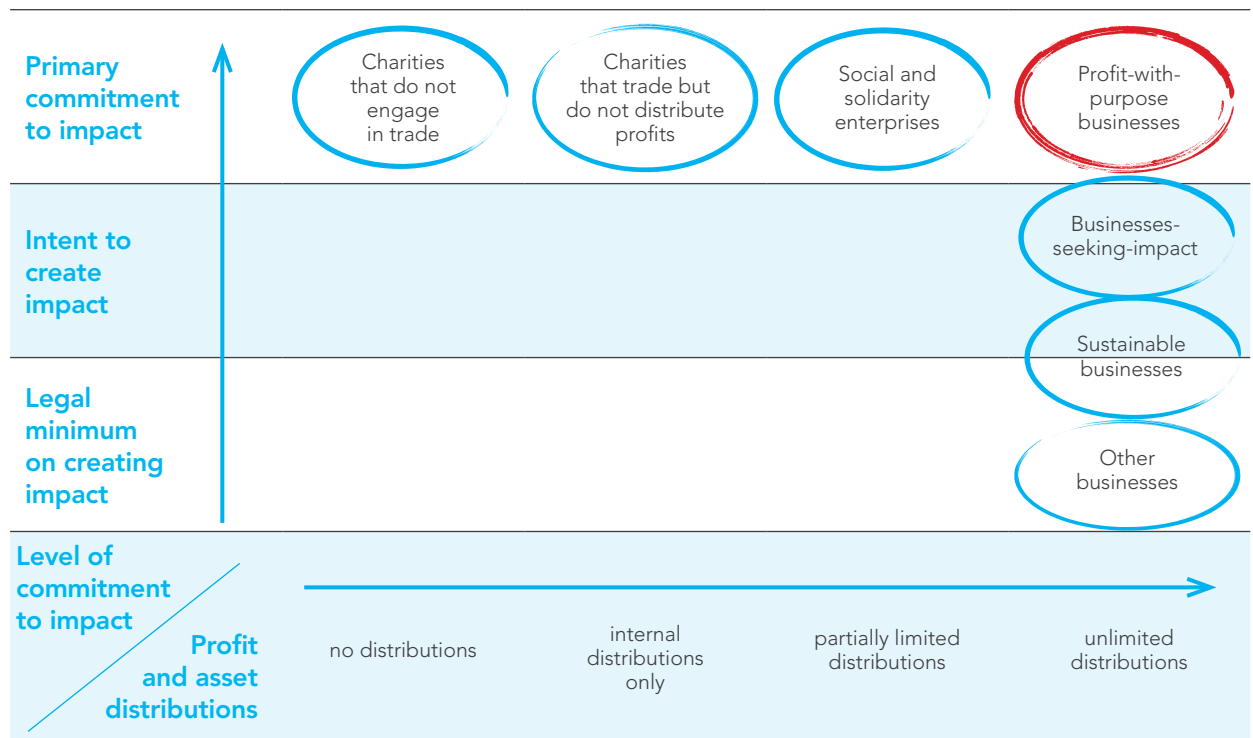
In common with social sector organisations, profit-with-purpose businesses have a primary and long-term commitment to impact, which distinguishes them from businesses-seeking-impact and other conventional businesses. They place duties on their directors to deliver against this commitment, encouraging confidence amongst socially-minded investors, customers and employees. They also report on their impact, and are transparent on wider environmental, social and governance criteria. What sets them apart from social sector organisations is that profit-with-purpose businesses have no asset lock or restrictions on the distribution of profits, encouraging more commercial investment and thereby allowing for more rapid growth and impact.

It may be helpful to consider these segments in relation to two key parameters – the extent of social focus and the distribution of profits and assets, as follows on the following page:

THE IMPACT CONTINUUM



Combining social impact and profitable business



To take an example, **Patients Know Best (PKB)** is a health informatics start-up which puts health data in the hands of the patients rather than selling it on, and which brings together all the data from different clinics and social care agencies to improve the lives of people with complex conditions. By not selling patients' data, PKB restricts its revenue potential compared with its competitors, but it is confident that this commitment is socially valuable in protecting patients' interests. PKB is the kind of venture than needs to move fast if it is not to be outrun by purely commercial competitors with no commitment to putting patients first. As a high-risk digital start-up, only equity investment can provide realistic risk-adjusted returns to investors. To offer equity, it needs a profit-distributing legal structure – and to offer trust to its clients and investors, it needs to show it is fully committed to its social model. PKB is now a multiple award-winning growth venture, and an exemplar of the kind of profit-with-purpose business which this report is all about. For more information on the way PKB embeds its social mission through its contracts, see Annex C.

A further example is **d.light**, which manufactures and distributes solar lighting and power products to

those who do not have access to reliable electricity in the developing world. d.light has reached more than 30 million people over eight years of growth. It recently completed an \$11 million financing round from impact investors. d.light is a certified B Corp, a step it took *"to showcase but also formalize our commitment to social impact."*⁸ For more information on B Corp certification, please see Annex C.

Data on profit-with-purpose businesses is lacking and weak, as these kinds of businesses are not easily identified or counted in official statistics. Profit-with-purpose businesses have not yet formed their own identity and voice in most countries.

However, evidence of the increasing significance of profit-with-purpose business is emerging from various countries. An increasing number of growth-oriented social entrepreneurs are choosing for-profit models, and committing to deliver impact.⁹ Legislators are introducing new hybrid legal forms for profit-with-purpose businesses, notably in the United States, and considering new legislation for social and solidarity enterprises, for example in Canada, France, Italy and Japan.

8 Sources: US NAB on Impact Investing (2014) Private Capital Public Good; www.dlightdesign.com/impact-dashboard/; www.bcorporation.net/community/dlight-design.

9 For example, over half of applications to UnLtd's Big Venture Challenge are now from Companies Limited by Share (<http://unltd.org.uk/2014/04/10/findings-7-pushing-boundaries/>). Echoing Green reports similar trends in its application data in the USA and elsewhere, and notes that for-profit applicants have been most successful in accessing funds (<http://www.echoinggreen.org/sites/default/files/2014-EG-Applicant-Snapshot-Brief.pdf>).

We believe that the profit-with-purpose approach will be welcomed by a significant group of social entrepreneurs. We aim to draw in entrepreneurs and businesses which would not establish asset-locked social sector organisations, but which would commit to a long-term social mission and be prepared to be transparent about and accountable for the delivery of that social mission. It will attract entrepreneurs who wish to take some capital gain to compensate for low or nil salary and high risk in the early stages, but who are committed to achieving social impact. It may also be attractive to family firms and other commercial companies that wish to formalise their values and explicitly recognise a social mission.

We also believe that profit-with-purpose business will be welcomed by a significant group of impact investors, who wish to invest in impact-driven businesses but require formal protection against mission drift.

Social impact investment is already possible into asset-locked social sector organisations, where

the investment is backed by collateral, where the social venture has a track record and can issue social impact bonds and other debt instruments, and in countries and impact themes where there is sufficient philanthropic or government money. Impact investment can also be made into organisations which distribute profits, and which deliver impact even without long-term organisational commitment to impact.

We believe that the profit-with-purpose approach set out in this report is most likely to attract additional social impact investment in start-ups and in ventures capable of rapid and transformational growth. In both cases, the risk/return equation means that equity investment is most likely to be appropriate.

Overall, we believe that this work will deliver a substantial net increase in social impact and benefits for multiple stakeholders:

For social entrepreneurs and profit-with-purpose businesses	For investors	For beneficiaries, clients and consumers
<ul style="list-style-type: none"> • Helps them to self-identify and to articulate their social credentials to investors and other stakeholders • Allows them to specify and stay true to social mission, and to increase their social impact • Protects the legacy of founder social entrepreneurs • Allows them to secure investment on reasonable, risk-adjusted terms, potentially from social investors and more commercially-oriented investors 	<ul style="list-style-type: none"> • Allows social investors to identify eligible investees with confidence and familiarity • Empowers social investors to prevent changes in the mission of the business • Allows investors to monitor performance on social mission • Allows exit without compromising the mission • Broadens the available universe of investments for social investors • Builds bridges between social and commercial investment • Provides for equity returns on risk investment to enable promising ventures to grow, compared to asset locked businesses • Allows commercial investors to make reasonable risk-adjusted returns from social ventures 	<ul style="list-style-type: none"> • Brings more commercial investment into profit-with-purpose businesses compared to asset or profit locked social enterprises or non profits • Allows customers to choose to “buy social” on a much wider basis • Draws some entrepreneurs into explicit social commitments alongside commercial objectives • Draws more businesses generally towards pro social activity • Enhances the experience of customers and beneficiaries and drives positive social change
For regulators and policy makers		
An international framework allows for global recognition of best practice and local application of clear principles		

Although our focus is on profit-with-purpose businesses, we recognise that the non-profit and social/solidarity enterprise sectors are doing incredibly valuable work in many areas of social impact. We endorse the efforts to bring more social investment into these sectors, so that the best organisations in them can grow and increase the social impact they create. For this reason, our recommendations also apply to countries which currently have no intermediate form between non-profit and commercial business, and which may not yet feel it appropriate to allow for the unrestricted profit distribution of profit-with-purpose business forms.

Accordingly, our legal framework allows for social or solidarity enterprise forms, which may be the best next step in these countries. From a legal and policy point of view, the difference between profit-with-purpose business and social or solidarity enterprise

is simply the degree of flexibility regarding the distribution of profits and use of assets. The key principle that a primary focus on impact can be combined with at least a partial distribution of profits is common to both, and our proposed legal framework allows for either.

In addition, we welcome the corporate responsibility activities and social value delivered by other sustainable businesses, and we encourage corporations to do more. We also recognise that a significant proportion of social investors work through profit-distributing companies, which do not formally lock in social mission, yet still set and deliver against significant outcome objectives. The Taskforce refers to such businesses as 'businesses-seeking-impact'. In our recommendations we include reporting mechanisms and legal changes which could also be useful to these businesses.¹⁰

¹⁰ See Recommendation 20 in Annex A in particular.

BALANCING RISKS AND REWARDS

In putting forward our framework, we recognise that there are no perfect solutions. There are many ways of achieving social impact, and many ways for impact investment to be deployed. All approaches have risks as well as rewards. The balance of those risks and rewards are judged differently across countries, cultures, entrepreneurs and investors.

At heart, the risk/reward question is one of balancing commitment to social impact, and financial returns to allow investment.

The social mission of traditional social sector organisations such as charities is usually locked in, with regulatory oversight to ensure that it is maintained. They have often been tightly restricted in terms of distributing profits or assets. As such,

they may find it difficult to raise investment capital, particularly at the early stages or for transformational growth. This position is often exacerbated by a risk-averse approach as a reaction to regulation. For these organisations, there is a risk of underperformance in terms of social impact, if they are not able to raise sufficient capital – underperformance which hits the poorest and most disadvantaged amongst us.

Social or solidarity enterprise is being developed to help overcome some of these restrictions. However, social enterprises are typically defined by an asset lock and restrictions limiting the distribution of surpluses to no more than, say, 50% of profits. From a commercial investor standpoint, this may be too tight a restriction, and such enterprises run the risk of underperforming on growth and impact because they cannot raise the investment capital they need. From the perspectives of some social investors, they may offer a useful balance of long-term social commitment and some level of investment return.

A growing number of for-profit businesses aim to achieve a social purpose and are prepared to report on this. As fully profit-distributing enterprises, they find it easier to raise commercial investment, especially at the critical early stages and for transformational growth. Investors are therefore likely to see more rapid growth with commensurably higher financial returns. However, impact investment in an organisation which is not fully committed to social impact for the long term may backfire because of mission drift. A significant number of businesses which started out to achieve a social mission have drifted away from it or lost it completely on a change of control.

Requirements to report on impact, and to be transparent on wider environmental, social and governance performance, can assist both to encourage social impact and to create confidence amongst stakeholders, provided that the reporting requirements are proportionate and do not create excessive barriers to market entry. Yet many countries do not require impact reporting from traditional social sector organisations or social enterprises, let alone from impact-driven businesses.

We believe that the profit-with-purpose model provides a useful balance between investibility and reduced risk of mission drift, as compared to either traditional social sector organisations or businesses which have no locked-in social mission.

THE NATIONAL CONTEXT IS CRITICAL

Each of the Taskforce countries has a specific context that influences the opportunities for profit-with-purpose business and how our proposed framework can be implemented.

Some of the critical issues are cultural and institutional – including the level of acceptance of business approaches and models to tackle social issues, and the relative trust in business, government and civil society. This affects the likely balance between regulatory and voluntary approaches to embedding social mission into profit-with-purpose businesses, and the overall interest in doing so. Many countries have strong cultural norms, reflected in a binary approach to social purpose and private gain which sees these in opposition rather than synergy. There is often resistance to the notion that social purpose entities should be allowed to earn income and distribute profit. These cultural norms have been embedded into regulatory measures, which separate the for-profit and not-for-profit sectors, and which often do not recognise or allow for blended social and financial value.

As a result, social entrepreneurs are often forced into social sector organisational structures that limit their flexibility and market opportunity. And those who opt into for-profit legal forms can be viewed with suspicion by some investors and other stakeholders, amid concerns about ‘social washing’, ‘mission drift’, and loss of trust.

The key drivers for change also matter – in particular, whether interest in investing in profit-with-purpose businesses comes primarily from the impact investment community, or from more commercially-oriented investors. Attitudes differ across countries and across the range of investors within those countries – foundations, pension and insurance funds, commercial investors, retail investors, governments and international bodies, all of which have their own motivations, priorities and boundaries.

Other contextual issues are legal, including the range of existing legal forms elsewhere on the non-profit/for-profit spectrum, and experience with these. Countries have different sets of rules for companies and for charities, and some have intermediate structures. Some have a substantial co-operative and mutual sector, and a greater emphasis on forms that have traditionally comprised the social or solidarity economy. Our work attempts to provide opportunities for impact-driven business activity in all such contexts. We include in our report recommendations for social and solidarity enterprise, where countries do not yet have these intermediary forms and do not feel it appropriate to adopt profit-with-purpose business at this stage.

Most critical is the legal flexibility to embed a social purpose into the objects, governance and operations of a business. Some countries require businesses to maximise financial return, which has resulted in the emergence of new legal forms in order to secure a social purpose – such as the Benefit Corporation and similar forms in the USA. The Working Group commissioned an analysis of the legal options for profit-with-purpose businesses across seven Taskforce countries, the summary of which is provided in Annex C.

We propose a high-level framework which we believe can be adopted widely and provide a useful balance between international consistency and national specificity.

FINDINGS

The Mission Alignment Working Group has analysed the opportunities and barriers, and identified five key findings:

1. Recognising and developing a sector of profit-with-purpose businesses is likely to attract additional entrepreneurs into economic activity that is driven by social impact. Overall, this will boost social impact and impact investment.
2. One of the most effective routes to achieving this will involve measures to create confidence about the social mission and social impact of the business amongst its critical stakeholders, without limiting profit distribution or over-

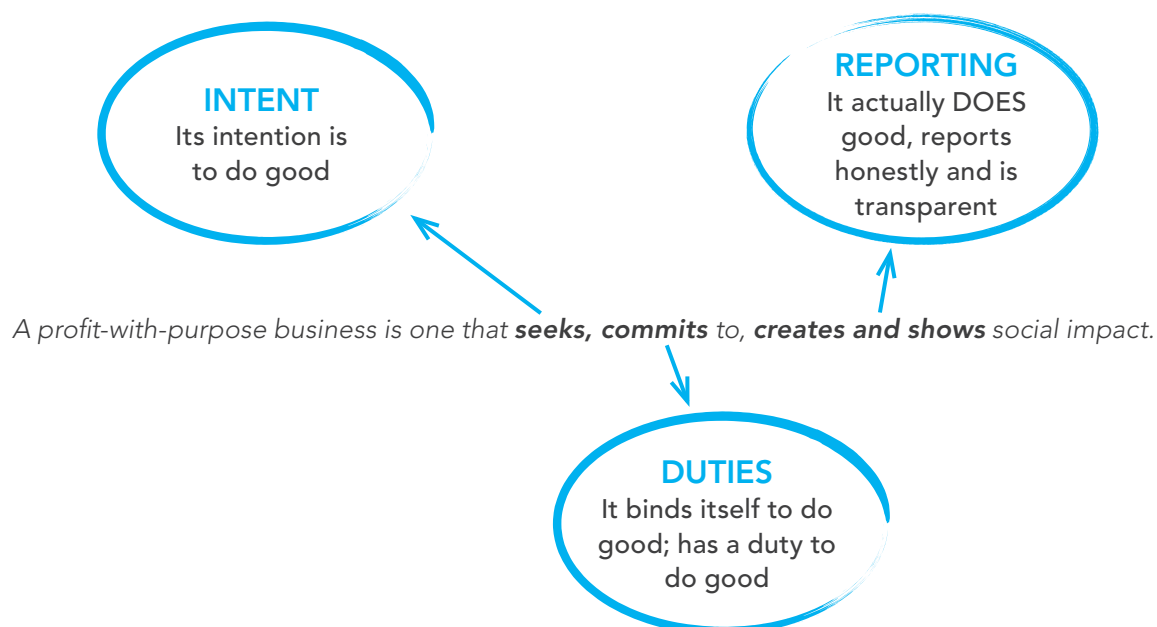
regulation. The critical stakeholders include entrepreneurs, customers, investors, and employees. We seek to attract stakeholders into an impact-driven space, as well as to lock the business into that mission.

3. A mixture of regulatory measures, express agreement options, transparency mechanisms and market tools can help to achieve this goal.
4. The key requirements are intent, duties, and reporting on impact, as set out below.
5. Some of the required mechanisms are in place in one or more of the Taskforce countries, and can be built upon quickly.

In order to respond to these key findings, the Working Group took the following approach:

Characteristics	<ul style="list-style-type: none"> • Define the characteristics of a profit-with-purpose business as well as social enterprise and solidarity enterprise
Legal measures	<ul style="list-style-type: none"> • Describe an adequate legal basis that allows for businesses with these characteristics • List additional options for legislators • For each country, analyse the current legal position and identify a key next step
Policy & market measures	<ul style="list-style-type: none"> • Identify supportive policy and market measures that could be applied across countries
Stimulate implementation	<ul style="list-style-type: none"> • Identify starting points for rapid implementation • Showcase examples

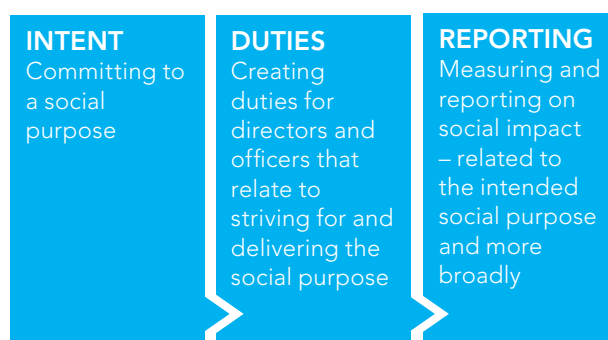
RECOMMENDATIONS



CHARACTERISTICS THAT DEFINE A PROFIT-WITH-PURPOSE BUSINESS

The Working Group recognises the need for multiple methods of embedding a social mission into a profit-with-purpose business, which are mutually reinforcing, just as a stool requires three legs for stability. In particular, we believe that both social intent and social impact reporting are necessary for a business to be profit-with-purpose.

The Working Group therefore proposes the following minimum requirements, which effectively define a profit-with-purpose business:



The **social purpose** should be broad enough to avoid the risk of becoming obsolete, but specific enough to set objectives and measure their achievement for purposes of accountability.

A variety of mission lock mechanisms may be used, depending on the legal and institutional context. It may be useful to distinguish between permanent mission locks and locks which can be exited, for example on a super-majority vote of shareholders.

Measuring and reporting social impact should focus on the extent to which the specified social purpose is delivered. However, it should also report on broader environmental, social and governance issues, to be fully transparent on its total net impact. For example, a manufacturing business whose primary purpose is to provide training and employment opportunities for people with disabilities should report on how many people have been trained or helped into work, but should also report on other material impacts, such as the environmental impact of its manufacturing process, or the way it treats its staff.

Impact reporting should be proportionate.

We recognise that start-up and early stage profit-with-purpose businesses may not yet be able to show delivery of social impact, so intent and duties may be more relevant at this early point in the enterprise journey than reporting. For further consideration of appropriate impact measurement and reporting frameworks, we refer to the recommendations of the Impact Measurement Working Group.

PROVIDING AN ADEQUATE LEGAL BASIS

The Working Group is grateful to the thorough work of William Clark, in turning our recommendations into an international model to which legislators can make appropriate changes in their countries. In recognition, we call this the Clark Bill, and it is included in full in Annex A to this report. Here we provide a summary of the Bill.

Although the Working Group's focus is primarily on profit-with-purpose businesses, the Bill and the recommendations therein refer frequently to 'social mission business'. We introduce this term to refer to both profit-with-purpose businesses and social/solidarity enterprises as we intend the recommendations to cover both of these categories. Many of the recommendations are also applicable to 'businesses-seeking-impact', as Recommendation 20 of the Bill describes. Indeed, many of our recommendations encourage legislators to provide options for entrepreneurs, their preferences over which would effectively position their businesses in one of these three segments.

The Working Group makes the following recommendations to countries, in terms of the minimum legal foundation for profit-with-purpose businesses and social/solidarity enterprises:

- **No legal impediments:** The law of the country should permit such a business to be organised.
- **Available legal forms:** The defining characteristics of such a business should be available under each basic legal form that may be used in the country to organise a business.
- **Methods of implementation:** The country may permit the defining characteristics of such a business to be implemented either by (i) making available legal forms that have those characteristics by law, or (ii) permitting the private parties organising the business to contract for those characteristics.
- **Investment fiduciaries:** The law of the country should not prohibit investment managers or fiduciaries responsible for investing pension funds or endowments from (i) investing some portion of those funds in such businesses, or (ii) applying a positive impact screen to some or all of their investments.
- **Charity regulation:** The law of the country should not automatically subject such a business to regulation as a charity, simply due to its social mission. Generally, such businesses should be treated as for-profit entities. Regulators may reserve the right to apply additional regulation to such a business for specific reasons, for example if it is granted exemption from taxation on the basis of its social purpose.
- **Definition of purpose:** Such a business must have a purpose to create (i) general social impact, (ii) one or more specific social impacts, or both.¹¹ The law of the country should either impose such a purpose or provide for the enforcement of an election of such a purpose in the constituent documents of the business.
- **Duties:** The duties of the directors and officers of such a business must include furthering the social impact purpose of the business and require them to have regard for stakeholder interests affected by the business. The law of the country should either impose these duties or provide for the enforcement of the imposition of these duties by the constituent documents of the business.
- **Minimum level of transparency:** Such a business must be required to prepare and periodically make available a report of the impact performance of the business using a qualifying independent standard. The law of the country should either impose such a requirement or provide for the enforcement of such a requirement in the constituent documents of the business. The reporting approach should be appropriate for the range of businesses and their stakeholders' requirements, and not be unnecessarily onerous. For example, the law may vary on how detailed the report must be, based on the turnover of the business. The Working Group recognises the work being done by the Taskforce's Impact Measurement Working Group and in other international fora to establish agreed principles and approaches for social impact measurement, and encourages the application of these principles where appropriate to profit-with-purpose businesses and social/solidarity enterprises.

¹¹ We reiterate here that by social, we refer to social and environmental impacts and purposes.

ADDITIONAL OPTIONAL REGULATORY MEASURES

Further to the above, the Working Group recommends that countries consider the following additional regulatory measures, which may be desirable for some profit-with-purpose businesses and social/solidarity enterprises.

- **Additional transparency options:** The country should encourage such businesses to consider a higher level of transparency than identified above as the minimum. Options include auditing or certification, specifying the frequency of reporting (e.g. annual), and specifying conditions related to the public availability of reports.
- **Asset lock:** The law of the country should permit such a business to be organised either with or without an asset lock.¹²
- **Profits lock:** The law of the country should permit such a business to be organised with or without restrictions on the distribution of profits to the owners of the business.¹³
- **Mission lock:** The law of the country should provide mechanisms that can be elected by such a business to restrict the ability of the owners to change or abandon the social impact purpose or purposes of the business. Such mechanisms could include regulation, express agreement (by constituent documents or contract), and reputational or market-based levers which rely on transparency, market awareness, and similar factors. The latter could include encouraging such businesses to state that they are committed to the said purpose into the future.
- **Enforcement of purposes:** The law of the country should provide one or more means by which the social impact purpose of such a business may be enforced. Countries should consider whether non-owner constituents should have standing to bring a lawsuit or the right to elect a representative to the board; whether a government monitor should be created; and the costs of any mechanism chosen. The Working Group notes that the current scope for enforcement of purpose is relatively weak across the seven countries, and recommends that countries consider appropriate steps to address this.
- **Change of control:** The law of the country should provide mechanisms by which investors in and owners of such a business may provide for

the continuation of the mission of the business upon a sale of control. Such mechanisms could include allowing for a controlling ownership or special voting or approval rights by a third party; validating the use of a golden share; or permitting investors to contract for special voting or approval rights regarding a change of control.

ADDRESSING THE CURRENT LEGAL SITUATION IN EACH OF THE TASKFORCE COUNTRIES

The Working Group commissioned detailed analysis of the legal position across the Taskforce countries as it relates to profit-with-purpose businesses. This work was carried out on a pro bono basis by Orrick, Herrington and Sutcliffe LLP, and kindly facilitated by TrustLaw Connect. The Working Group thanks Orrick warmly for this substantial work. Orrick's summary is included as an annex to this report. The full analysis is being shared with each of the countries' National Advisory Boards to inform future policy development in each Taskforce Country.

Drawing on this analysis, the Working Group has examined the extent to which the desired legal framework is currently in place, and identified a range of further measures which could be helpful. The key components of a desirable legal framework are summarised on page 15.

Some countries already have a legal and regulatory framework which fits the template we propose and which provides the basis for profit-with-purpose businesses and/or social/solidarity enterprises. Some countries need modest tweaks to their system, for example taking models created at local or regional level to national availability. Others would need more substantial change if they wish to provide for profit-with-purpose businesses, including several countries which have new and helpful legislation already in process. We hope that the Working Group's "Clark Bill" will assist policy makers across the world to make their country more favourable for profit-with-purpose business and social or solidarity enterprise.

Across the Taskforce countries, the strongest area in terms of the legal foundation for profit-with-purpose businesses is the flexibility to include social mission at least as a secondary object in a profit-distributing entity. The weakest area is the lack of enforceability, particularly related to accountability

KEY COMPONENTS OF A DESIRABLE LEGAL FRAMEWORK

Characteristic	Explanation
Can include social mission as secondary object for profit distributing entity?	This is the basic requirement for profit distributing entities to be able to carry out social mission activity
Can include social mission as primary object for profit distributing entity?	Allowing for social mission as a primary object means that the entities can be “social first” or “social and financial equal”
Is there an established legal precedent and practice or clear civil code?	Most countries have existing detailed company law, both in statute and case law, and it may take some time or specific regulation or guidance to give certainty of how new corporate forms will be treated in practice
Are there mechanisms to embed social purpose in a profit distributing entity?	What practical methods of implementation for social purpose are available? Are these easy to use and effective in practice?
Are there specific legal forms designed for profit-with-purpose businesses or social/solidarity enterprises?	Some countries have chosen to create new profit-distributing corporate forms specifically for such businesses
Is social purpose included in fiduciary duties, and clearly enforceable?	For the social mission to become real, directors should have fiduciary duties towards all the objectives of their company, the social object as well as financial return

for implementation of a social mission being clearly included in directors’ duties: this is a topic where further work would be of particular value.

POLICY AND MARKET MEASURES

In addition to the above regulatory measures which relate to the required and optional characteristics of profit-with-purpose businesses and social/solidarity enterprises, countries may also consider other policy measures that seek to support their development. These could include:

- **Investor tax incentives** to stimulate investment in such businesses.
- Measures related to government procurement and other **public expenditure**.
- Ensuring that **business development programmes** apply to such businesses.

All of the above measures should be designed and implemented with due regard to their impact on

impact investment more broadly, in order to avoid unintended negative consequences.

There is also a need for market mechanisms that put our recommended approach into effect. These would allow profit-with-purpose businesses to be recognised as such by customers and investors – for example related to impact measurement, third party certification or audit, or other forms of assurance; or social stock exchanges and other forms of market listing.

There is a growing number of effective models to put this approach into practice. There are some areas still to be developed, but much can be replicated or adapted from successful experience in other countries. Our short library of examples in Annex C is a starting point, but we believe there would be value in building on this further.

We encourage an existing international agency to pick this up and create a shared learning platform of exemplars and contacts.

Impact reporting and accreditation is undoubtedly the most challenging aspect of the model we propose, and one which is the focus for another of the Taskforce Working Groups. We believe that the models developed by B Lab for ventures, and by Finansol for social investors¹⁴, represent the most promising platforms to build upon. However, individual countries will need to decide how to organise accreditation systems – including the roles of government and the market, consideration of thresholds, costs, and who pays.

There is also a need for better data and market research. As a new field, lacking an identifying label, we are operating in the absence of reliable data. Equally, we do not yet know the most effective long term methods for the joint tasks of crowding in entrepreneurs and investors, and locking in social mission and impact. We strongly recommend that market-based research, as real-time as possible, is conducted on a common basis across multiple countries. This will help to identify problems and improvements; to evidence the value of the sector to encourage more countries, more investors and more entrepreneurs; and facilitate more volume and more cost-effective investment flows to achieve the social impacts we all wish to see.

Finally, we recognise that the framework we have proposed has been developed rapidly and with limited engagement of policy makers, social entrepreneurs and investors. We recommend a more **comprehensive consultation** at the national level with large numbers of social entrepreneurs and investors, to refine and introduce the framework. Continuing oversight of the emerging sector will be required in order to sustain the

confidence of all stakeholders that profit-with-purpose business will continue to be both impact-driven and business-like.

STARTING POINTS FOR IMPLEMENTATION

The framework proposed by the Working Group allows for flexibility at the national level.

However, we have identified several promising exemplars that could point to the way forward for implementation. These are included in Annex C to this report, covering the following topics:

Investments in profit-with-purpose businesses

Transparency and impact reporting

Using legal form to embed social mission

Using legal objects to embed social mission

Using contracts to embed social mission

Using a Board position to embed social mission

Using market 'lockstep' to embed social mission

Learning from experience with profit locks

Investment fiduciaries

Attracting commercial investors

Attracting entrepreneurs

¹⁴ For more information on these, see Annex C to this report.

ANNEX A: THE CLARK BILL: RECOMMENDATIONS FOR A LEGAL FRAMEWORK

Recommendations for a Legal Framework to Promote Profit-with-Purpose Businesses and Social/Solidarity Enterprises

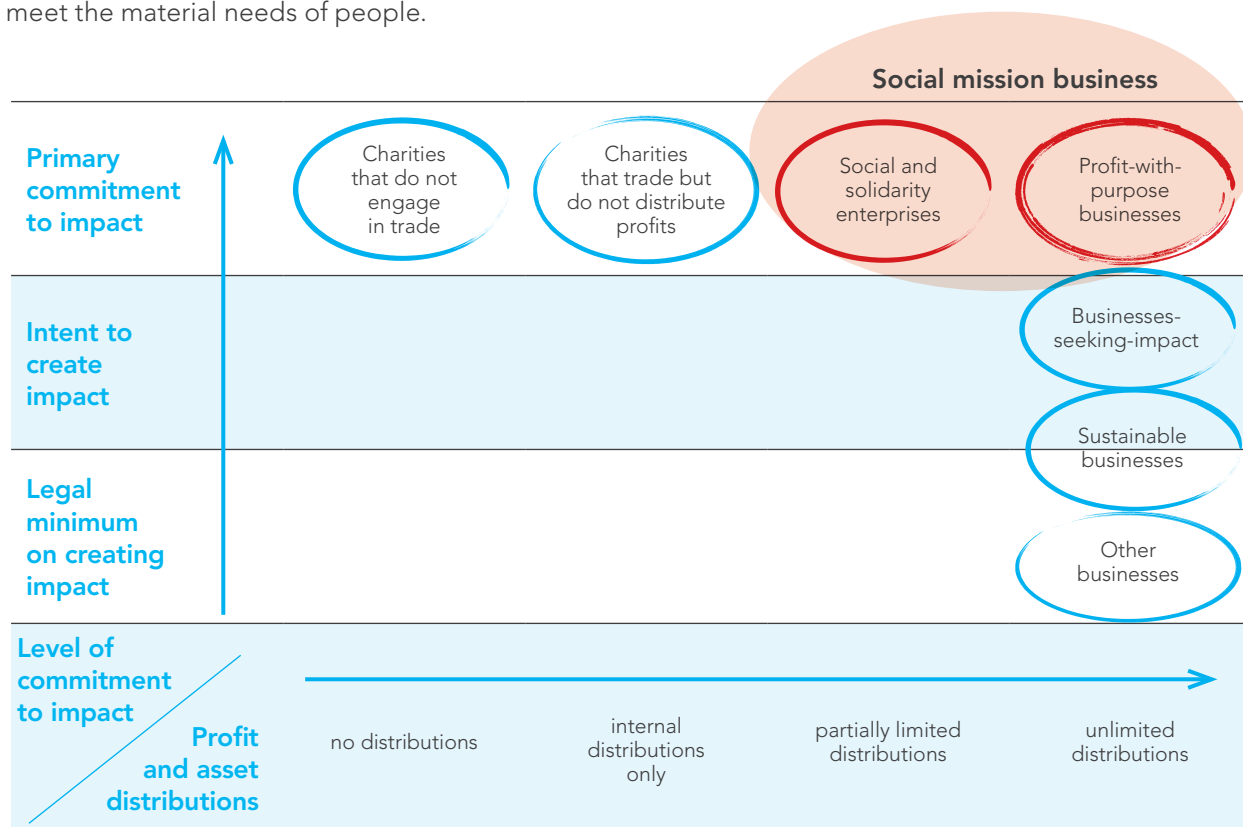
Mission Alignment Working Group of the Social Impact Investment Taskforce established under the UK's presidency of the G8

INTRODUCTION¹⁵

The spectrum of private organizations that benefit society in some fashion is very broad and stretches from grant-funded charities, which receive contributions specifically to address defined societal or environmental issues,¹⁶ to pure for-profit businesses, which provide gainful employment and meet the material needs of people.

One way that private organizations can be analysed is by looking at the level of commitment to creating social or environmental impact that guides the actions of the owners, directors and officers of an organization. Another way that organizations can be analysed is to look at the degree to which the legal forms in which they are organized restrict distributions of assets or profits. Combining the two factors of intent to create impact and distribution limitations provides the following diagram describing how various forms of organization relate to one another with respect to those two characteristics.

We propose a high-level framework which we believe can be adopted widely and provide a useful balance between international consistency and national specificity.



¹⁵ Information about the Mission Alignment Working Group which prepared these Recommendations is set forth in Annex D.

¹⁶ These Recommendations speak in various places about "social mission," "social return," "social value," "social impact," and similar concepts that include the term "social." Whenever the word "social" is used it should be understood to include "environment" as well. That usage is made express in the definition of "social impact purpose" in the Glossary which makes clear that both social and environmental issues and impacts are included in the concept of social impact purpose. The inclusion of environmental issues and impacts within the usage of the term "social" is also consistent with the definition of social impact investing developed by the Taskforce which notes that the approach it has "articulated for achieving social impact is equally applicable to environmental impact." In limited instances, both social and environmental impacts are referred to expressly for purposes of emphasis, but that usage is not intended to detract from the general principle that references to social impact include environmental impact.

These Recommendations focus on businesses in the categories of “social/solidarity enterprise” and “profit-with-purpose business.” Businesses in those two categories are referred to collectively in these Recommendations as “social mission businesses.” The Mission Alignment Working Group believes that it is appropriate to focus on social mission businesses because of the increasing interest in a number of countries on promoting the growth of those types of businesses. At the same time, the Working Group also believes that all countries will benefit from the clarity that these Recommendations will provide about social mission businesses.

From a legal point of view, the main difference between profit-with-purpose business and social or solidarity enterprise is the degree of flexibility regarding the distribution of profits and use of assets. The key principle that a primary focus on impact can be combined with at least a partial distribution of profits is common to both, and our proposed legal framework allows for either.

Another way of thinking about social mission businesses is in terms consistent with the definition of impact investing that has been adopted by the Taskforce. Seen from that perspective, a social mission business is one that (i) intentionally targets social return along with financial return, and (ii) sets measurable social objectives and regularly measures their achievement.

Social mission businesses are not the only businesses that may create significant social impact or be appropriate recipients of impact investments. To that end, the final Recommendation describes how each of the preceding Recommendations should apply to businesses-seeking-impact.

As Recommendation 20 demonstrates, the category of businesses-seeking-impact is less well defined than that of social mission businesses and essentially includes any business that intends to create a social impact but does not share all of the defining characteristics of a social mission business. Although the Recommendations are focused on social mission businesses (and businesses-seeking-impact in the case of Recommendation 20), the Comments to several of the Recommendations note how the principles underlying those Recommendations can also apply to sustainable businesses.

Issues Addressed by the Recommendations

The Recommendations address both the desirable characteristics of social mission businesses and the legal impediments currently facing those businesses.

The characteristics seen as desirable in a social mission business from the perspective of social impact entrepreneurs include:

- ability to specify the mission of the business;
- ability to retain control of the business;
- ability to participate in the equity gain of the business;
- securing the mission both (i) during the operation of the business and (ii) upon a change in control or dissolution;
- protection from demands to increase financial performance at the expense of the mission; and
- ease of establishing a venture.

The characteristics seen as desirable in a social mission business from the perspective of social impact investors include:

- ability to prevent changes in the mission of the business;
- right to participate in the governance of the business;
- ability to participate in the equity gain of the business;
- ability to monitor performance of the business in pursuing its mission; and
- ability to exit without compromising the mission.

The legal impediments currently facing social impact entrepreneurs and social impact investors include:

- limits on distributions of profits or equity gains applicable to some legal forms;
- legal requirements to maximize the financial return of a business for the benefit of its owners; and
- inability to secure adequately the mission of a social mission business under some legal forms.

The Recommendations seek to create a framework that will have sufficient flexibility to be used in different political, cultural, and economic contexts and that will provide:

- measurable social benefit;
- straightforward, workable models for the organization of profit-with-purpose businesses;
- attractions for entrepreneurs to adopt a social mission;
- a way for social investors to identify eligible profit-with-purpose businesses with confidence and familiarity;
- realistic information and reporting requirements;
- low costs of compliance;
- trusted models that are marketable to relevant stakeholders;
- ease of entry to markets without high barriers; and
- appropriate levels of stakeholder engagement.

Overview of the Recommendations

The Recommendations are organized under the following topics:

A. Providing an adequate legal basis for social mission businesses. The Recommendations in this section deal with aspects of a country's legal system that must be present for social mission businesses to be established and prosper.

B. The defining characteristics of social mission businesses. The Recommendations in this section deal with the characteristics shared by all social mission businesses. For a country to have a viable social impact sector, its legal system must permit businesses to be organized with all of these characteristics.

C. Optional features of social mission businesses that will be desirable in some circumstances. The Recommendations in this section address characteristics of social mission businesses that are often desirable, but are not shared by – or necessarily appropriate for – all social mission businesses.

D. Government support for and promotion of social mission businesses. The Recommendations in this section move from a focus on how a country's legal system can promote the organization of social mission businesses to steps

a country can take proactively to promote the growth of social mission businesses.

E. Businesses-seeking-impact. The final Recommendation describes how the preceding Recommendations can apply to the broad category of businesses-seeking-impact.

RECOMMENDATIONS

A. Providing an Adequate Legal Basis

Recommendation 1 (no legal impediments):

The law of the country should (i) permit a business to be organized with the defining characteristics described in Recommendations 6 through 9; and (ii) provide at least one option for addressing each of the issues described in Recommendations 10 through 15.

Comment

Satisfying Recommendation 1 is the most basic requirement that should be asked of countries. It is a necessary precondition to developing the social mission business sector in any country. Recommendations 6 through 9 relate to the defining characteristics shared by all social mission businesses and thus the law of the country needs to permit businesses to be organized with all of those characteristics. The issues covered by Recommendations 10 through 15 are important to the development of a healthy social mission business sector, but do not apply to every social mission business.

Recommendation 2 (available legal forms): The defining characteristics of a social mission business described in Recommendations 6 through 9 should be available under each of the basic legal forms that may be used in the country to organize a business.

Comment

In most countries, more than one legal form may be used to organize a business (in common law jurisdictions such as the UK and US, those forms include structures such as corporations, partnerships, limited liability companies in the US, etc.). Some countries have legal forms created specifically for use by social mission businesses (e.g., benefit corporations in the U.S. and community interest companies in the U.K.), but usually the choice of which legal form to use when organizing a business is dictated by considerations other than the social impact nature of the business.

To avoid unintended consequences in areas outside of social impact, each basic legal form that might be chosen for reasons not related to social impact should accommodate its use by social mission businesses. Otherwise, social mission businesses may be forced into choosing a legal form for reasons unrelated to their social impact purpose, particularly as a result of tax considerations, with the result that the choice forced on the business may interfere with the ability of the business to accomplish its social impact purpose.

In the United States, for example, a business is usually organized as either a corporation or a limited liability company, with the choice between those two options being determined by tax considerations. The freedom of contract available to a limited liability company when designing its internal governance will permit it to be organized as a social mission business, but a business that wants to be organized as a corporation will need to be incorporated in a state that has authorized a form of corporation that has the characteristics of a social mission business because a traditional corporation cannot be organized with all of those characteristics.

In contrast to the required characteristics, the optional characteristics described in Recommendations 10 through 15 may be available for some legal forms and not other forms.

Recommendation 3 (methods of implementation): The country may permit the required characteristics of a social mission business to be implemented either by (i) making available legal forms that have those characteristics by law, or (ii) permitting the private parties organizing the business to make an enforceable contract that the business will have those characteristics. Regardless of which approach is taken, provision should be made for businesses to be able to adopt some or all of the optional features described in Recommendations 10 through 15.

Comment

Legal forms that include specified characteristics have the benefit of lower transaction costs because they can be established without the need for customized drafting of the constituent documents for a business. Freedom of contract, on the other hand, has the benefit of greater flexibility to address the specific needs of a particular business. These competing concerns suggest that the country should consider authorizing legal forms

that provide the optional characteristics described in Recommendations 10 through 15 and also allow the parties involved with a particular social mission business the freedom to choose which optional characteristics they wish and how those characteristics will be implemented.

Recommendation 4 (investment fiduciaries): The law of the country should not prohibit investment managers or fiduciaries responsible for investing pension funds or endowments from (i) investing some portion of those funds in social mission businesses, or (ii) applying a positive impact screen to some or all of their investments.

Comment

The problem addressed by this Recommendation is illustrated by the experience in the US under the Employee Retirement Income Security Act (ERISA) which governs the responsibilities and conduct of pension plan fiduciaries. In 1994, the US Department of Labor issued an Interpretive Bulletin that described the circumstances in which plan fiduciaries could make socially oriented investments without contravening their fiduciary responsibilities. In 2008, however, the Department of Labor altered this interpretation of ERISA with supplemental guidance. The new guidance narrowed the previous interpretation, emphasizing the duty of a fiduciary to focus only on the economic implications of an investment, and provides that fiduciaries may not select investments on the basis of any factor outside the economic interest of the plan.

In contrast to the experience in the US, all large French companies and some small businesses offer corporate savings plans for their employees. The plans offer a choice of investments from among at least three different funds. Since 2010, one of those funds must invest between 5 and 10% of its assets in “solidarity-oriented” companies, which is the term used in France for organizations similar to social enterprises.

Recommendation 5 (charity regulation): The law of the country should not subject a social mission business or its activities to charity regulation simply because of its social impact purpose. Rather, social mission businesses should be treated presumptively as for-profit entities and, as a default rule, exempt from charity regulation. Taxing authorities and charity regulators may reserve the right, however, to regulate social mission businesses as charities

when the circumstances of a business warrant that regulation, such as when a social mission business is more favorably taxed or receives other government support differently from a similar business without a social impact purpose.

Comment

This Recommendation reflects the basic nature of a social mission business as a for-profit organization. To treat social mission businesses as generally subject to charity regulation would be a fundamental misunderstanding of what social mission businesses are. Charity regulation in this context includes both regulation of the activities of a business as charitable solicitations and regulation or supervision of the business itself as a charity. Although this Recommendation exempts social mission businesses from charity regulation, it recognizes that there are circumstances where charity regulation may be appropriate.

The solicitation of an investment in a social mission business, for example, should not be treated as a solicitation for charitable purposes. Similarly, the sale of goods or services or otherwise conducting for-profit activities in the ordinary course should not be seen as charitable activities. Exemption of the foregoing activities should apply even where the social mission business makes representations to the public that a percentage of its revenues or profits will be directed to charities or charitable purposes or that goods or services will be donated or distributed for free or at a reduced price to charities or for charitable purposes. However, if a business names a specific charity as the beneficiary of its activities, the result could be different. For example, a business that advertises “50% of profits given to charity” should not be subject to regulation as a charity on that basis alone, while a country may take a different view of a business that advertises “50% of profits given to XYZ” or “50% of profits used to support the work of [stated charitable purpose].” In the latter case, the close association of the business with an identifiable charity or purpose gives the advertisement an air of charitable solicitation not present in the former case, and thus a country may conclude that regulation of the latter form of advertising as a charitable solicitation may be appropriate.

If a social mission business is exempt from taxation on the basis of its social impact purpose, it may be appropriate to regulate it as a charity.

If a social mission business has evolved out of a nonprofit organization or charity, this

Recommendation does not mean that the business will be able to avoid asset or profit locks that attached to it as a nonprofit organization or charity. In such a case, aspects of its prior regulation as a charity may continue to apply to it. This Recommendation only addresses whether certain activities or actions by a social mission business are a reason to regulate the business as a charity.

B. The Defining Characteristics of a Social Mission Business

Recommendation 6 (defining characteristics generally): The characteristics that define a social mission business and should be found in every social mission business organized under the law of the country are:

- (i) a social impact purpose as provided in Recommendation 7,
- (ii) duties of its directors and officers consistent with its social impact purpose as provided in Recommendation 8, and
- (iii) transparency regarding its creation of general social and environmental impact as provided in Recommendation 9.

Comment

A business must have all three of the stated characteristics for it to have the status of a social mission business. A business that has less than all of these characteristics, for example because it does not report transparently on its social impact purpose, may be performing an important social purpose but it will not have the status of a social mission business for purposes of these Recommendations.

Recommendation 7 (purpose): A social mission business must have a purpose to create:

- (i) general social and environmental impact;
- (ii) one or more specific impacts, but need not have a purpose to create general social and environmental impact so long as it reports on its creation of general social and environmental impact as required by Recommendation 9; or
- (iii) both general social and environmental impact and one or more specific impacts.

The law of the country should either provide legal forms in which a company organized as that form has such a purpose or provide for the enforcement of an election of such a purpose in the constituent documents of the company.

Comment

This characteristic is at the heart of what it means to be a social mission business. The characteristics treated in the following two Recommendations involving duties and transparency flow from and support this basic characteristic.

Implementation of this Recommendation in some countries will involve a change in the basic understanding of the purpose of for-profit businesses as focused only on maximizing the financial return of the business for its owners. As a way of providing an alternative to that basic understanding, such a country may decide to authorize a new legal form that provides for a broader purpose, but in doing that the country should have regard to Recommendation 2.

*The country should consider implementing this Recommendation in a manner that applies more broadly than just to social mission businesses. By doing that, the country will enable a sustainable business to pursue a social impact purpose even though the business does not have all the characteristics of a social mission business. An approach along these lines can be seen in the decision of the Supreme Court of Canada in *BCE Inc. v. 1976 Debentureholders*, [2008] 3 S.C.R. 560, which speaks generally of a “corporation’s duties as a responsible corporate citizen.”*

“General social and environmental impact” is defined in the Glossary as “a material positive impact on society and the environment, taken as a whole, from the activities of a business.” The second option under this Recommendation allows a business not to make a commitment to creating general social and environmental impact and only be committed to creating a specific impact so long as the business reports on its creation of general social and environmental impact.

The owners and directors of a company should focus on having a shared and clear understanding of the value propositions and mission needs of the company and how they are reflected in the articulation of its social impact purpose. A business focused on improving educational opportunities for vulnerable children, for example, should not be overburdened or constrained by demands to focus on women beneficiaries or the environmental footprint of the company. As noted, however, the ability to prioritize the mission and focus of the company do not relieve it of the obligation to report generally on its general social and environmental impact.

The purpose of the business required by this Recommendation is defined in the Glossary as the “social impact purpose” of the business.

The social impact purpose of a social mission business as required by this Recommendation implements that portion of the definition of impact investing adopted by the Taskforce that requires a social mission business to “set measurable social objectives.”

Recommendation 8 (duties): *The duties of the directors and officers of a social mission business must include furthering the social impact purpose of the business and require them to have regard for stakeholder interests affected by the business. When discharging this duty, the directors and officers should be free to weigh the various stakeholder interests that will be affected by an action as the directors and officers consider appropriate. The law of the country should either impose these duties or provide for the enforcement of the imposition of these duties by the constituent documents of the business.*

Comment

This characteristic follows logically from the basic notion that a social mission business must have a social impact purpose. The bedrock responsibility of directors and officers is to act in the best interest of their company. Because every social mission business has a social impact purpose, furthering that purpose must be part of the duties of the directors and officers of a social mission business.

The directors and officers are also required to have regard for stakeholder interests. Applying that requirement to all social mission businesses including those that only have a purpose to create a specific impact is consistent with the requirement that businesses with only a specific impact purpose must nonetheless report on their creation of general social and environmental impact.

If a company has elected to pursue a specific impact, the ability of the directors and officers to weigh the interests of the stakeholders as they consider appropriate will permit the directors and officers to have particular regard for the interests of those stakeholders affected by the company’s specific impact purpose.

The definition of “stakeholder interest” and the accompanying Comment in the Glossary provide examples of the interests for which the directors and officers must have regard. The requirement in this

Recommendation to have regard for stakeholder interests is similar to Section 172 of the UK Companies Act 2006 which is quoted in that Comment, except that the reason for considering the interests of stakeholders under this Recommendation is to promote the social impact purpose of the company and not just to benefit the success of the company for the benefit of its owners as under Section 172. See also the statement of the Supreme Court of Canada in *BCE Inc. v. 1976 Debentureholders*, [2008] 3 S.C.R. 560, referring to the duty of directors to act “in the best interests of the corporation, having regard to all relevant considerations, including – but not confined to – the need to treat affected stakeholders in a fair manner.”

The country should consider implementing this Recommendation in a manner that applies more broadly than just to social mission businesses. By doing that, the country will enable the directors and officers of a sustainable business to take a broader view of how they operate the business even though the business does not have all the characteristics of a social mission business. An example is Section 172 of the UK Companies Act 2006 regarding the duties of directors, which is not limited in application to social mission businesses. Similarly, the Supreme Court of Canada in the *BCE* case has stated with respect to all Canadian corporations that:

“There is no principle that one set of interests – for example the interests of shareholders – should prevail over another set of interests. Everything depends on the particular situation faced by the directors and whether, having regard to that situation, they exercised business judgment in a responsible way.”

The country may wish to authorize governance mechanisms for social mission businesses to support the exercise of the duties required by this Recommendation. For example, the US Model Benefit Corporation Legislation authorizes the optional election of a “benefit director” or “benefit officer” who have special responsibilities relating to the social impact purpose of a benefit corporation. Another approach might be to create a second board to monitor and advise on the pursuit of the social impact purpose of a profit-with-purpose business.

Recommendation 9 (required transparency):

A social mission business must be required to prepare and periodically make available a report

on the performance of the business as it seeks to create general social and environmental impact. If the business is committed to a specific impact, the report should also address the performance of the business in creating that impact. The report must use a qualifying independent standard to assess that performance. The law of the country under which a social mission business is organized should either impose such a requirement or provide for the enforcement of such a requirement in the constituent documents of the business. The law of the country may vary how detailed the report must be based on the turnover or stage of development of a business.

Comment

The definition of “qualifying independent standard” in the Glossary includes important restrictions on the standard a social mission business may use to prepare its transparency reports. Those restrictions are important because they protect against the required transparency being used to “greenwash” or incorrectly portray the performance of the business. Validation of transparency reports is not required, but is one of the optional best practices discussed in Recommendation 10.

It is important to emphasize that transparency is not an end in itself and that merely having a social impact purpose without achieving real impact will be insufficient. The transparency required by this Recommendation should be an important impetus for a business to produce genuine impact.

While a commitment to transparency is a required characteristic of every social mission business, there should be some flexibility in how a particular business satisfies that commitment. The report required of a large or mature business may properly be different from the report required of a small or early stage business. Before mandating a transparency requirement, or changing an existing requirement, the country should evaluate whether a new requirement will be unduly burdensome or create an unreasonable barrier to entry for new social mission businesses.

The obligation to prepare the report is on the company and will presumably be an expense borne by the company. This Recommendation should not be read as calling into question an arrangement under which investors, contracting parties, or others bear, or share, the cost of preparing the report.

Consistent with Recommendation 7, this Recommendation requires every social mission business to report on its creation of general social and environmental impact even if the business has a mission only to pursue a specific impact.

The transparency required by this Recommendation implements that portion of the definition of impact investing adopted by the Taskforce that requires a social mission business to “regularly measure [the] achievement” of the social objectives it has set.

The country should consider implementing this Recommendation in a manner that applies more broadly than just to social mission businesses. By doing that, the country will enable a sustainable business to adopt transparency measures even though the business does not have all the characteristics of a social mission business. Examples are Section 414C of the UK Companies Act 2006 and the proposed amendment to Articles 19-20 of EU Directive 2013/34/EU which impose reporting obligations on larger companies. Those provisions are discussed in the Comment to “qualifying independent standard” in the Glossary and are not limited in application to social mission businesses.

The Recommendations in this Section B and in Sections A and C address issues that relate to the law of the country under which a social mission business is organized. That point is made explicit in this Recommendation to avoid the incorrect conclusion that a company with operations in more than one country would be subject to the transparency requirements in each country where it does business. It was not considered necessary to address this issue in the other Recommendations in Sections A through C because they more clearly on their face relate to issues arising just under the law of the country in which a company is organized.

C. Optional Features of Social Mission Businesses that Will Be Desirable in Some Circumstances

The Recommendations in the preceding two sections relate to issues that are fundamental to establishing a thriving community of social mission businesses in the country. The Recommendations in this section, in contrast, address optional characteristics that may be desirable for some social mission businesses, but not all such businesses.

Recommendation 10 (transparency options):

The country should encourage social mission businesses to consider a higher level of transparency than what is required by Recommendation 9. Options to consider include:

- **Validation.** The recommended best practice in this regard is for transparency reports to be validated in some manner by an independent party. But due regard should be given to the expense that this would impose on the business.
- **Frequency of reporting.** The recommended best practice in this regard is for the business to prepare the report annually.
- **Public availability of reports.** The recommended best practices in this regard are for the business to make the report available (i) to the public and (ii) without cost.

Comment

This Recommendation is phrased in terms of best practices because there are wide variations in transparency practices and the best practices described in this Recommendation have not yet become the accepted norm. In the US, for example, the Model Benefit Corporation Legislation requires annual reporting and public availability of the reports, but the State of Delaware only requires public benefit corporations to report every other year and does not require the reports to be publicly available. Compare Sections 401 and 402 of the US Model Benefit Corporation Legislation with 8 Del. Code § 366.

This Recommendation speaks of “validating” a transparency report because there are a variety of ways of assuring the reliability of a report in addition to hiring an independent auditor. Independent firms that validate transparency reports are beginning to emerge, but this area is still nascent. As an alternative to using an outside firm, a proposal has been made in France for the use of a second board with independent members to monitor the company’s performance and approve its transparency reports.

Recommendation 11 (asset lock): The law of the country should permit a social mission business to be organized either with or without an asset lock.

Comment

An asset lock is defined in the Glossary as:

“A combined restriction that (i) during the life of a company its assets will not be disposed of for less

than their value except in furtherance of the social impact purposes of the company, and (ii) upon winding up, the assets of the company remaining after all debts have been settled will be transferred to a company with an asset lock and similar social impact purposes. An asset lock does not apply to profits when initially earned by a company, but will apply to any profits reinvested in the company in lieu of distribution to the owners.”

While some social impact entrepreneurs and investors may decide that an asset lock would be appropriate in a particular situation, the country should not impose an asset lock on all social mission businesses. The experience in countries that have imposed an asset lock on forms of social mission business has been mixed because the restriction is sometimes an impediment to attracting investment and may discourage entrepreneurs from founding social impact businesses. But an asset lock may be an important feature in some situations, such as (i) a transfer of public services to private sector companies where a high level of public trust is required, or (ii) where social mission businesses receive special tax treatment.

Examples of legal forms created for use by social mission businesses that include an asset lock are the community interest company in the UK, community contribution company in British Columbia, and community interest company in Nova Scotia.

Recommendation 12 (profit lock): The law of the country should permit a social mission business to be organized either with or without a profit lock.

Comment

A profit lock is defined in the Glossary as “A restriction on the distribution to the owners of a company of the profits earned by the company, either during the life of the business or upon liquidation.” A profit lock is different from a restriction on the ability of the owners to sell their ownership interests in the business.

The experience in countries that have imposed a profit lock on forms of social mission business has been mixed because the restriction can be an impediment to attracting investment and may discourage entrepreneurs from founding social mission businesses. But a profit lock may be an important feature in some situations, such as (i) a transfer of public services to private sector

companies where a high level of public trust is required, or (ii) where social mission businesses receive special tax treatment.

Recommendation 13 (mission lock): The law of the country should permit a social mission business to be organized either with or without a mission lock.

Comment

A mission lock is defined in the Glossary as “A restriction on changing the social impact purpose of a company.”

Mission locks are often important for social impact entrepreneurs and investors. Among the benefits of mission locks in appropriate circumstances are that they:

- help social mission businesses to stay true to social mission and to increase social impact
- protect the legacy of founder social entrepreneurs
- allow social mission businesses to secure investment on reasonable, risk-adjusted terms
- allow social investors to identify eligible investees with confidence and familiarity
- ultimately, enhance the experience of customers and beneficiaries of social mission businesses
- provide appropriate securing of mission without locking in to the point of obsolescence

There are four basic ways in which a mission lock can be created:

1. **Regulatory.** Under this approach, the law of the country imposes the mission lock by a means such as: (i) making the mission lock part of the terms of a legal form that may be used to organize a business; (ii) imposing the lock as a condition to favorable tax or other treatment; or (iii) providing or validating mechanisms that can be used to create the mission lock, such as a golden share.
2. **Express agreement embedded in the constituent documents of the business.** An agreement of this type will be binding on all of the owners of the business, both current and future.
3. **Express agreement among some or all of the owners of the business.**
4. **Reputational/market based.** Under this approach, enforcement of the mission lock relies on transparency, market awareness, and similar

factors. One form of this type of mission lock is found in the case of a company making a product that by its very nature embodies the social impact purpose of the company (e.g., solar powered household appliances or lighting fixtures, educational products or services for at-risk populations, or portable drinking water purification systems).

As the Comment to the definition of “mission lock” in the Glossary notes, a mission lock does not have to be absolute. There is a tension between a commitment to a social impact purpose and the need for flexibility as a business and its industry evolves. Countries considering using a regulatory approach to imposing a mission lock should consider how strong the mission lock should be (i.e., how difficult it will be to change the social impact purpose of a business).

Recommendations 11, 12, and 13 treat asset locks, profit locks, and mission locks separately because all three need not be present in the case of any particular social mission business. Mission locks are also substantively different because they can be imposed by private agreement while asset locks and profit locks are usually imposed by law.

See also Recommendation 15 relating to securing the mission of a social mission business upon a change in control. That Recommendation includes a discussion of some of the specific ways that a mission lock can be created by agreement.

Recommendation 14 (enforcement of purposes):

The law of the country should provide one or more means by which the social impact purpose of a social mission business may be enforced. Issues for the country to consider in this regard include:

1. Whether non-owner constituents should have standing to bring a lawsuit to challenge how a social mission business is pursuing its social impact purpose.
2. Whether a government monitor should be created.
3. Whether certain constituencies should be given the right to elect a representative to the board of the business.
4. The costs of any mechanism chosen from the perspectives of both the business and the persons with the right to seek enforcement or redress.

Comment

Issue 1: In most legal forms in most countries, the directors and officers are subject to suit by the owners alleging breach of the duties of the directors and officers, but standing to bring those types of suits is not extended to other parties. There are considerable operational and financial risks associated with granting broad enforcement rights to non-owners of a social mission business struggling to accomplish its social impact purpose. These risks should be considered in assessing whether to extend enforcement rights to stakeholders that are not owners.

Section 305 of the US Model Benefit Corporation Legislation limits standing to owners and directors, but permits the constituent documents of a benefit corporation to grant standing to other stakeholder interests.

Issue 2: Creation of a government monitor raises difficult issues as to the basis for its jurisdiction over social mission businesses and the sanctions it may impose, unless the monitoring is coupled with some form of tax preference or government support for those businesses.

Issue 3: Examples of how this type of requirement could be implemented are the laws in several European countries requiring employee representatives on the supervisory boards of larger companies. Another approach is the proposal in France that companies have a second board focused on social impact.

Issue 4: This issue highlights the fact that seeking legal redress may both (i) impose significant costs on the business that may be unwarranted, and (ii) conversely, discourage parties from pursuing a legitimate complaint.

Recommendation 15 (change of control): The law of the country should provide mechanisms by which investors in and owners of a social mission business may provide for continuation of the mission of the business upon a sale of control. The mechanisms for the country to consider include:

1. Having a foundation or trust aligned with the mission of the business as a controlling owner.
2. Giving special voting or approval rights regarding a change of control to a foundation or trust aligned with the mission of the business even though the foundation or trust does not hold a controlling interest.

3. Validating the use of a golden share held by a person aligned with the mission of the business.
4. Permitting investors to contract for special voting or approval rights regarding a change of control.
5. Requiring supermajority approval of any action or transaction that would materially change or remove the social impact purpose of the business.
6. Requiring a payment to a social agency or government agency in the event the social impact purpose of the business is abandoned within a defined period of time following a change of control.

Comment

Mechanisms 1 through 3 each require that the party with control be aligned with the mission of the business. Before control is ceded to a party pursuant to one of those mechanisms, consideration should be given to how that party's alignment with the mission of the business can be assured.

An important difference between mechanisms 2 and 4 is that the rights under mechanism 4 may be sold or transferred by the investor but the expectation is that the foundation or trust under mechanism 2 would not do so.

A significant issue with respect to golden shares that should be addressed by the law of a country wishing to provide for that mechanism is the separation between ownership and control inherent in a golden share. If golden shares are desired, the law of the country should expressly validate an ownership interest in which voting rights carrying control are divorced from an economic stake.

Mechanism 5 may be implemented as part of a legal form, by provision in the constituent documents of a company, or by agreement among the owners of a company. It is perhaps the most flexible mechanism listed because it permits a shifting group of the owners to decide the future direction of the business.

This Recommendation is a specific application of the broader concept of mission locks under Recommendation 13.

D. Government Support and Promotion of Social Mission Businesses

The Recommendations in the preceding two sections relate to the required and optional characteristics of social mission businesses. The focus of the Recommendations in this section is not on social mission businesses themselves, but rather on issues a country should consider to support the development of social mission businesses.

Recommendation 16 (investor incentives): The country should consider providing incentives that will encourage investors to invest in social mission businesses. These incentives could take such forms as:

- tax credits or subsidies (such as, for example, reduced tax rates on distributions from social mission businesses, or shortened holding periods for long-term capital gains treatment of investments in social mission businesses); or
- credit enhancements (such as, for example, providing guarantees or first-loss capital).

Comment

For details of the UK tax relief for investment in social enterprises, see the factsheet available at <https://www.gov.uk/government/publications/social-investment-tax-relief-factsheet/social-investment-tax-relief>

As its name suggests, first-loss capital involves capital provided by a party that agrees to bear first losses, in an amount typically agreed upon in advance. By altering the risk-return profile of the investee, first-loss capital can catalyze the participation of investors that otherwise would not have participated.

Recommendation 17 (existing incentive programs): The country should evaluate its existing business incentive programs, such as community reinvestment, small business promotion, etc., to make sure they encourage the formation and growth of social mission businesses.

Comment

This Recommendation adopts the obvious policy position that being a social mission business should not disadvantage the business from participation in programs for which it would otherwise qualify.

Recommendation 18 (new incentive programs):

The country should consider how its procurement and public expenditures might appropriately benefit social mission businesses. Any new incentives, contracting preferences, or other benefits should not be coupled with regulatory requirements that go beyond what is necessary to monitor entitlement to participate in, and compliance with the terms of, the program.

Comment

When government preferences are provided to a class of business, there is usually a need to monitor the participating businesses to avoid abuse. But the monitoring should be tailored to that purpose. Monitoring the performance of a social mission business generally – as opposed to monitoring necessary to avoid abuse of the purpose or terms of a specific program – is inconsistent with the basic notion of harnessing the power of the private sector to promote social impact.

Recommendation 19 (avoiding negative effects):

The country should review the administration of its tax and other laws to make sure they do not discourage the formation of social mission businesses. For example:

The country should ensure that businesses can be formed with a minimum of red tape and delay. A robust community of entrepreneur-led businesses needs the ability to react quickly to market developments and new ideas.

Expenses incurred by a social mission business in pursuing its social impact purpose should receive the same tax treatment as other expenses incurred by the business.

A profit-with-purpose business should not be at a disadvantage in bidding for public contracts and participating generally in procurement and public expenditures when compared to a company that is not a social mission business.

Comment

Issue 3 addresses a concern that is similar to the issues addressed in Recommendation 17. The difference is that the focus of this Recommendation is on the administration of the country's laws generally as opposed to the specific incentive programs addressed in Recommendation 17.

E. Businesses-Seeking-Impact**Recommendation 20 (businesses-seeking-impact):**

The country should encourage the growth and funding of the category of organizations referred to in these Recommendations as “businesses-seeking-impact.” The preceding Recommendations with respect to social mission businesses apply to businesses-seeking-impact as follows:

- *No legal impediments.* Recommendation 1 is generally applicable to businesses-seeking-impact. The law of the country should permit a company to be organized as a business-seeking-impact.
- *Available legal forms.* Recommendation 2 is generally applicable to businesses-seeking-impact. The law of the country should permit a business-seeking-impact to be organized in each of the basic legal forms that may be used in the country to organize a business.
- *Methods of implementation.* Recommendation 3 is generally applicable to businesses-seeking-impact. The country may permit a company to be organized as a business-seeking-impact to be implemented either by (i) making available legal forms that have those characteristics by law, or (ii) permitting the private parties organizing the company to make an enforceable contract that the company will be a business-seeking-impact.
- *Investment fiduciaries.* Recommendation 4 is generally applicable to businesses-seeking-impact. The law of the country should not prohibit investment managers or fiduciaries responsible for investing pension funds or endowments from investing some portion of those funds in businesses-seeking-impact.
- *Charity regulation.* Recommendation 5 is generally applicable to businesses-seeking-impact. The law of the country should not subject a business-seeking-impact or its activities to charity regulation simply because of its social impact purpose. In most circumstances, there should be less reason to subject a business-seeking-impact to charity regulation than there may be with respect to a social mission business.
- *Defining characteristics generally.* The principal characteristic that defines a business-seeking-impact is the intention to create a social or environmental impact as described in Recommendation 20.7. In the case of most such businesses, that intention will affect the duties of its

directors and officers. The business or its owners may also conclude that it would be valuable to provide some transparency regarding the performance of the business in creating impact.

- *Purpose.* By definition, a business-seeking-impact will have a purpose to create either (i) general social and environmental impact, or (ii) one or more specific impacts. Unlike a social mission business that must report on its creation of general social and environmental impact even if it only has a purpose to create one or more specific impacts, a business-seeking-impact that only has a purpose to create specific impact should not be required to report more broadly. The social impact purpose of a business-seeking-impact may be expressed in a less legally binding fashion than is the case with a social mission business.
- *Duties.* The duties of the directors and officers of a business-seeking-impact should include furthering the social impact purpose of the business as far as that purpose is formally specified. The law of the country may also permit the directors and officers to have regard for stakeholder interests affected by the business. When discharging their duties, the directors and officers should be free to weigh the various stakeholder interests that will be affected by an action as the directors and officers consider appropriate.
- *Required transparency.* A business-seeking-impact need not be subject to a requirement to report on its accomplishment of its social impact purpose, but the company or its owners may commit to a reporting obligation. If a business is subject to a voluntary reporting obligation, the law of the country should provide for the enforcement of that obligation.
- *Transparency options.* If a business-seeking-impact is subject to a reporting obligation, it should consider whether to follow the best practices developed by social mission businesses but following those practices should not be required.
- *Asset lock.* A business-seeking-impact should not be subject to an asset lock.
- *Profit lock.* A business-seeking-impact should not be subject to a profit lock.
- *Mission lock.* Recommendation 13 is generally applicable to businesses-seeking-impact. The law of the country should permit such a business to be organized either with or without a mission lock.
- *Enforcement of purposes.* Recommendation 14 is generally applicable to businesses-seeking-impact. The law of the country should provide one or more means by which the social impact purpose of a business-seeking-impact may be enforced if that purpose is expressed in a fashion that is intended to be legally binding.
- *Change of control.* Recommendation 15 is generally applicable to businesses-seeking-impact. The law of the country should provide mechanisms by which investors in and owners of a business-seeking-impact may provide for continuation of the mission of the business upon a sale of control.
- *Investor incentives.* Recommendation 16 is generally applicable to businesses-seeking-impact. The country should consider providing incentives that will encourage investors to invest in those businesses.
- *Existing incentive programs.* Recommendation 17 is generally applicable to businesses-seeking-impact. The country should evaluate its existing business incentive programs, such as community reinvestment, small business promotion, etc., to make sure they encourage the formation and growth of businesses-seeking-impact.
- *New incentive programs.* Recommendation 18 is generally applicable to businesses-seeking-impact. The country should consider how its procurement and public expenditures might appropriately benefit those businesses. Any new incentives, contracting preferences, or other benefits should not be coupled with regulatory requirements that go beyond what is necessary to monitor entitlement to participate in, and compliance with the terms of, the program.
- *Avoiding negative effects.* Recommendation 19 is generally applicable to businesses-seeking-impact. The country should review the administration of its tax and other laws to make sure they do not discourage the formation of those businesses.

GLOSSARY

Asset lock	A combined restriction that (i) during the life of a company its assets will not be disposed of for less than their value except in furtherance of the social impact purposes of the company, and (ii) upon winding up, the assets of the company remaining after all debts have been settled will be transferred to a company with an asset lock and similar social impact purposes. An asset lock does not apply to profits when initially earned by a company, but will apply to any profits reinvested in the company in lieu of distribution to the owners.
Company	A legal entity of any form that is used to conduct a business. <i>Comment: The term “company” is used broadly in the Recommendations and is intended to include any form of legal entity in which a business may be conducted.</i>
Constituent documents	The charter or articles of incorporation that are publicly filed as part of the process to incorporate a corporation and the bylaws or other internal regulations of the corporation, and similar types of documents for companies that are not corporations (e.g., the partnership agreement of a general partnership)
Director	A person under whose authority the powers of a company are exercised and under whose direction the activities and affairs of the company are managed. <i>Comment: This definition applies broadly to all legal forms of entities. In the case of legal entities that are not corporations, this definition includes persons in positions similar to the directors of a corporation.</i>
General social and environmental impact	A material positive impact on society and the environment, taken as a whole, from the activities of a business. <i>Comment: The purpose of this definition is to provide a way of referring to the people and planet aspects of the triple bottom line. The language follows the definition of the term “general public benefit” in the US Model Benefit Corporation Legislation.</i>
Golden share	An ownership interest that gives its holder the right to veto or decide the outcome of a vote on an issue, such as a change to the constituent documents of a company. The voting rights of the ownership interest will be (i) disproportionately greater than the economic rights of the interest and (ii) greater than the voting rights of any other interest.
Mission lock	A restriction on changing the social impact purpose of a company <i>Comment: This definition does not require that a mission lock be absolute. Any restriction on changing the purpose of a company beyond what would be required to change its purpose if it were not a profit-with-purpose business will constitute a mission lock. See the Comment to Recommendation 13 which describes the various ways in which a mission lock may be created.</i>
Officer	A person with day-to-day responsibility for running some or all of the affairs or activities of a company, subject to the authority of the directors of the company. <i>Comment: This definition applies broadly to all legal forms of entities. In the case of legal entities that are not corporations, this definition includes persons in positions similar to the officers of a corporation.</i>
Owner	A person holding an interest in a company that entitles the person to receive distributions from the company or to vote for the election of directors or other matters involving the internal affairs of the company.
Profit lock	A restriction on the distribution to the owners of a company of the profits earned by the company, either during the life of the business or upon liquidation. <i>Comment: A profit lock is similar to an asset lock. The Recommendations treat asset locks and profit locks separately and thus separate definitions have been created to facilitate that separate treatment.</i>
Profit-with-purpose business	A social mission business that has neither an asset lock nor a profit lock.

Qualifying independent standard

A standard for defining, reporting, and assessing the social and environmental performance of a business that is:

- (1) **comprehensive** because it assesses the effects of the business and its operations on all of the relevant stakeholder interests of the business;
- (2) **independent** because it is developed by an organization that is not controlled by the business;
- (3) **credible** because it is developed by an organization that both:
 - (i) has access to necessary expertise to assess overall social and environmental performance of a business; and
 - (ii) uses a balanced multi-stakeholder approach to develop the standard, including a reasonable public comment period; and
- (4) **transparent** because the following information is publicly available:
 - (i) about the standard:
 - (A) the criteria considered when measuring the overall social and environmental performance of a business; and
 - (B) the relative weightings, if any, of those criteria; and
 - (ii) about the development and revision of the standard:
 - (A) the identity of the members of the governing body, officers, and material owners, if any, of the organization that developed and controls revisions to the standard;
 - (B) the process by which revisions to the standard and changes to the membership of the governing body are made; and
 - (C) an accounting of the revenue and sources of financial support for the organization, with sufficient detail to disclose any relationships that could reasonably be considered to present a potential conflict of interest.

Comment

This definition is central to the transparency requirement that must be met by social mission businesses because those businesses are required to report on their achievement of their social impact purposes using a standard that satisfies this definition.

The language of this definition follows the definition of the term “third party standard” in Section 102 of the US Model Benefit Corporation Legislation.

A requirement similar to part (1) of this definition regarding comprehensiveness appears in Section 414C(7) of the UK Companies Act 2006 which requires quoted companies to include in their annual strategic report:

“(b) information about –

“(i) environmental matters (including the impact of the company’s business on the environment),

“(ii) the company’s employees, and

“(iii) social, community and human rights issues, ...”

Also similar to this definition is the proposed amendment to Articles 19-20 of EU Directive 2013/34/EU which requires a company over a prescribed size to prepare a fair review of the performance of its business and specifies that:

“(b) For companies whose average number of employees during the financial year exceeds 500 and, on their balance sheet dates, exceed either a balance sheet total of EUR 20 million or a net turnover of EUR 40 million, the review shall also include a non-financial statement containing information relating to at least environmental, social and employee matters, respect for human rights, anti-corruption and bribery matters, including:

“(i) a description of the policy pursued by the company in relation to these matters;

“(ii) the results of these policies;

“(iii) the risks related to these matters and how the company manages those risks.”

Social/solidarity enterprise.

Either (i) a business with a social impact purpose and a full or partial asset or profit lock; or (ii) an “enterprise solidaire” under French law.

Comment: The first part of this definition includes companies organized under Canadian (community contribution company in British Columbia and community interest company in Nova Scotia) and UK law (community interest company).

An enterprise solidaire under French law is similar to the businesses described in the first part of this definition, but has various alternative qualification criteria including those related to the proportion of employees that have particular challenges in accessing the labour market; democratic governance; salary ratios of the highest- and lowest-paid employees, etc. Amendments to the legislation that governs these criteria are currently being considered.

Social impact purpose

The purpose that a social mission business has elected to pursue, as required by Recommendation 7, involving the creation of (i) general social and environmental impact or (ii) specific impact.

Social mission business

A business that has the characteristics described in Recommendations 6 through 9.

Comment: The term includes social / solidarity enterprises and profit-with-purpose businesses.

Specific impact

Any of the following:

- (1) providing low-income or underserved individuals or communities with beneficial products or services;
- (2) promoting economic opportunity for individuals or communities beyond the creation of jobs in the normal course of business;
- (3) protecting or restoring the local or global environment;
- (4) improving human health;
- (5) promoting the arts, sciences, or advancement of knowledge;
- (6) increasing the flow of capital to entities with a purpose to benefit society or the environment; and
- (7) conferring any other particular benefit on society or the environment.

Comment: The purpose of this definition is to provide a way of referring to a particular mission to which a social mission business may be committed. The language follows the definition of the term "specific public benefit" in Section 102 of the US Model Benefit Corporation Legislation.

Stakeholder interest

Any of the following:

- (1) the owners of the business;
- (2) the employees and work force of the business, its subsidiaries, and its suppliers;
- (3) the interests of customers as beneficiaries of the general social and environmental impact or specific impact purpose of the business;
- (4) community and societal factors, including those of each community in which offices or facilities of the business, its subsidiaries, or its suppliers are located;
- (5) the local and global environment;
- (6) the short-term and long-term interests of the business, including benefits that may accrue to the business from its long-term plans and the possibility that these interests and the social impact purpose of the business may be best served by the continued independence of the business; and
- (7) the ability of the business to accomplish its social impact purpose or purposes.

Comment: This definition follows the language of Section 301 of the US Model Benefit Corporation Legislation which prescribes the interests that directors of a benefit corporation must consider.

A similar concept appears in Section 172 of the UK Companies Act 2006, which requires directors to have regard to:

- "(a) the likely consequences of any decision in the long term,*
- "(b) the interests of the company's employees,*
- "(c) the need to foster the company's business relationships with suppliers, customers and others,*
- "(d) the impact of the company's operations on the community and the environment,*
- "(e) the desirability of the company maintaining a reputation for high standards of business conduct, and*
- "(f) the need to act fairly as between members of the company."*

ANNEX B: ORRICK REPORT SUMMARY: AN INDEPENDENT STUDY OF THE LEGAL POSITION IN SEVEN TASKFORCE COUNTRIES

Across the seven countries, increasing emphasis among entrepreneurs and investors on businesses that set out to generate profits while achieving a social or environmental purpose coupled with

Note: Orrick, Herrington & Sutcliffe LLP was commissioned by the Working Group to carry out an independent study of the legal position in seven of the Taskforce countries as it relates to legal form, governance and legal protection for profit-with-purpose businesses. In line with the Group's mandate, this focused primarily on profit-distributing but social mission-driven businesses, and the legal possibilities for these in each jurisdiction.

increasing consumer demand for products and services that reflect their personal values, has highlighted the challenges facing those seeking to establish businesses with a social purpose.

One such challenge is legal recognition of this "triple-bottom line",¹⁷ which can conflict with fundamental business law principles in many jurisdictions. This has prompted some advocates to call for greater flexibility in applicable business

organisation law and for reforms to recognise expressly for-profit businesses that adopt a social purpose.

In this Report, businesses that conduct profit-generating activities with the right to distribute some or all of their profits to their owners but also operate to fulfil a social purpose are referred to as "profit-with-purpose businesses" ("PPBs"). Aside from having no restrictions on profit distribution, PPBs have three defining characteristics. First, they expressly espouse a mission to advance the common good. This may take the form of a general social purpose (i.e., a beneficial impact on society and/or the environment as a whole), a specific social purpose (i.e., a more tailored mission to advance a particular goal, such as providing products or services to underserved communities, preserving particular aspects of the environment or promoting economic opportunity) or both a general and specific social purpose. Second, the duties of those making management decisions for a PPB, such as its directors or officers, should include a duty to further the social purpose of the business. Third, the PPB should evaluate and report on its success in achieving its social purpose using a standard means of measurement. This could take the form of an impact assessment standard promulgated and/or verified by an independent third party.

This Report examines how and to what extent legal regimes in the seven countries permit the formation of PPBs with the key characteristics described above as well as other traits that could serve to secure the social purpose. All of the G7 countries have corporate forms that allow for the integration of a primary or secondary social purpose into one or more for-profit entities, while still ensuring the full or partial distribution of profits. There are thus no legal prohibitions to creating PPBs.

However, in a first set of countries, the absence of a specific type of corporate form for PPBs makes the enforceability of social purpose clauses in, for example, the corporate governance documents, a potential risk since such clauses are at odds with the profit maximisation principle that applies to for-profit corporations. Given the absence of a clear regulatory framework, and a lack of precedent cases for corporations that seek a "triple bottom line", there is real legal uncertainty regarding the extent to which PPBs will gain full respect and enforcement in the legal system. This is likely why PPBs are not prevalent in these countries.

¹⁷ A "triple bottom line" refers to businesses with both a conventional bottom line to measure their financial profit/loss and which aim to measure their performance in terms of positive social and/or environmental impact (for which there is no GAAP equivalent).

A second set of countries also do not have any corporate forms specifically designed for PPBs. However, the corporate legal principles in these countries allow for the social purpose to be embedded in the definition of the corporate purpose in the articles of association, and there is greater certainty that those non-economic purposes will be enforced, at least in comparison to the situation in the first set of countries.

In the remaining countries, there are many legal structures that a PPB can adopt. In each of these countries, legal forms have been legislated that are specifically designed for PPBs and which permit entities to further a social purpose while also allowing for full or partial profit distribution. In addition, conventional legal structures can be used by any business, whether or not it has a social purpose. However, in these countries, it is unclear whether decisions of directors or managers would survive legal scrutiny if they prioritised the social purpose of the company at the expense of profit maximisation. Even where the law does not impose legal barriers to the inclusion of a social purpose into the constitution of a for-profit entity, notwithstanding that its constitution contemplates the distribution of profits, the directors of such entities will, have to balance the promotion of such social purpose against the numerous other factors which it is part of their statutory and fiduciary duties to the entity (and its members) to consider when determining to adopt any course of action.

A few key trends also emerge from this cross-country analysis:

- Tax relief for businesses and investors correlate with assets/profits lock. Generally, governments only make tax relief available to organisational forms in which the social mission is paramount and which do not seek to return profits to interest holders. In most jurisdictions, there are bright lines between for-profit entities, which are subject to tax, and not-for profit or charitable entities, which are not. One of the main barriers to tax relief for PPBs are concerns over the potential for abuse. As a result, most legal forms that have been specifically designed for PPBs do not qualify for tax relief.
- Third party rights to enforce the social purpose of a PPB are limited or non-existent. In those countries, including those which have developed new legal forms for PPBs, non-owner stakeholders do not generally have standing to enforce the social purpose of the company or otherwise hold it accountable. Indeed, there are considerable operational and financial risks associated with granting broad enforcement rights to non-owners if a PPB struggled to satisfy

its social purpose. These risks merit consideration in assessing whether broad enforcement rights would benefit the PPB sector.

- New forms of business entities often involve additional legal risks. In the jurisdictions that have legislated new designations for PPBs, the use of these new forms for PPBs carry certain attendant legal risks to the extent they represent modifications to existing corporate law. This risk is heightened in common law jurisdictions where key legal principles, such as the notion of shareholder value maximisation, are articulated in judicial precedent rather than statutory law. In a claim for breach of fiduciary duty against directors of one of these new entities, there is uncertainty as to whether existing legal precedents would apply. In addition, some commentators have suggested that an express statutory directive to consider other interests common among PPB legislation creates an unhelpful distinction between PPBs and traditional companies and may unnecessarily and unintentionally restrict the exercise of conventional fiduciary duties.

Significantly, PPBs are attracting the attention of legislators as is reflected by proposed or possible legislative developments in many countries. In 2012, the European Commission presented a proposal for a European Foundation Statute in order to facilitate the cross-border activities of public benefit purpose foundations and to make it easier for them to support public benefit causes across the EU. It remains to be seen if, when, and to what extent this and various national initiatives will become effective. However, what is clear is the need for legislative reform should be studied by each country. The examples of recent legislative activity in this sector warrant further review and analysis.

Our Reports highlight the key legal issues facing PPBs and, where relevant, describe the reforms that have been enacted or which are contemplated in each country. The Reports focus on whether for each country, the relevant legal system has developed specific corporate legal structures for PPBs. In particular, the reports include the legal impediments to establishing a business seeking to distribute profits while pursuing a social impact, whether directors and managers can consider the interests of groups other than the owners, and whether and how the directors and managers can be held accountable for furthering the social purpose of the business.

Orrick, Herrington & Sutcliffe LLP
August 2014

ANNEX C: CASE STUDIES

- C. 1 Bazile Telecom and Citizen Capital (France)
- C.2 Nutriset (France)
- C.3 Co (France)
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C. 1 BAZILE TELECOM AND CITIZEN CAPITAL (FRANCE)

Themes: Investments in profit-with-purpose businesses; impact reporting

Bazile Telecom (www.bazile.fr) is the first French mobile phone operator dedicated to elderly people. It was launched in 2005 with the aim of improving the everyday life of the elderly, and to tackle social isolation. It offers contracts and phones which are adapted to old people's needs, including telephone book management, emergency mobile assistance, medication reminders, home delivery of online purchases, and medical advice.

Citizen Capital Partenaires SAS (www.citizencapital.fr) is a private equity and venture capital firm founded in 2008 that invests in socially innovative initiatives and in small and medium sized companies in the urban areas or underprivileged areas of France. The firm also invests in companies managed by entrepreneurs that could encounter potential social barriers to develop their company due to education, nationality or disability. It typically makes minority equity investments.

In February 2013, Citizen Capital made a €1.2m equity investment in Bazile Telecom. In principle, enterprise growth and social impact achieved are directly aligned for this business. However, the investor carried out social impact due diligence in connection with the investment, which clarified the strategic goals and social KPIs. Social impact is now measured against these metrics. A first independent social impact study was conducted in 2013. It found that a third of customers are first-time buyers of a mobile phone; two-thirds have improved their social relations through the service; 40% have increased their autonomy and have been able to recommence activities that they had previously stopped (e.g. taking the bus alone again); and three-quarters now feel safer since subscribing to the service.

C.2 NUTRISET (FRANCE)

Theme: Using legal objects to embed social mission

Headquartered in Normandy, Nutriset (www.nutriset.fr) is a family-owned and -operated food manufacturing company with a 25-year history of research and innovation to make nutritional products available for the benefit of children. Michel Lescanne, founder of Nutriset, set an ambitious purpose for the company: To invent, produce and make accessible solutions for the treatment and prevention of malnutrition, thereby contributing to the nutritional autonomy of developing countries.

The commitment to this purpose has led to radical innovations: through research; in distribution with exclusive partnerships with humanitarian players; and in production thanks to a sustainable network of local producers. Nutriset is effectively a corporate organization at the service of humanitarian action.

For the future, Nutriset is keen to embed its mission into its constitution. The Board of Directors has recently decided to revise its

corporate Charter to refer explicitly to the mission of the company (to develop innovative and accessible solutions for the treatment and prevention of malnutrition). According to the founder and the CEO of the company, this extension of the corporate purpose will play two roles: First, it will reassess and anchor the purpose in the long term, with any further change to the Charter requiring a supermajority of shareholders. And second, the governance will be aligned with the mission: the Board will report specifically on the way the mission is addressed.

C.3 CO (FRANCE)

Theme: Using legal objects to embed social mission; impact reporting

Co is a new consulting company, with a special purpose to address the strategic needs of social enterprises and the not-for-profit sector ("Economie Sociale et Solidaire" in France: ESS). Co is original in many ways:

- The consulting activity will be exclusively devoted to the ESS and to those organizations, which normally don't have access to professional consulting services.
- It is a joint venture, created by four major consulting firms in France (Algoé, Colombus, Kéa&Partners and Weave), which have decided to detach some consultants to Co periodically.
- While Co aims at developing new and specific consulting methods for the ESS, it also seeks to train both highly skilled consultants and managers to the specificities of ESS and thus, to contribute to the growing development of the social sector in France and worldwide.

To anchor its mission in the foundations of the company, Co will soon evolve as a SCIC (a cooperative company with different members: founding firms, financing partners, employees and representatives of ESS). The specific purpose of the company is stipulated in the constituent documents of the cooperative. Its executives will have to report on the positive impact of the activities not only for the mother firms, but also for funding partners, and upon the detached consultants and more generally upon the growth of the ESS. Tailored reporting and evaluation mechanisms are introduced to ensure transparency.

C.4 KINDERZENTREN KUNTERBUND AND THE SOCIAL VENTURE FUND (GERMANY)

Theme: Using a Board position to embed social mission

Kinderzentren Kunterbund (www.kinderzentren.de) is a social enterprise that provides affordable childcare services for working parents. Unlike most childcare centres, it offers extra-long, year-round opening times and flexible booking times. It runs over thirty daycare centres, located near workplaces. Its mission is to enable and promote a real balance between work and family.

The Social Venture Fund (www.socialventurefund.com) financed Kinderzentren Kunterbund with €1m to support the development of additional daycare centres. The investment provides valuable short-term liquidity for the renovation and conversion of rental space, funding for nursery start-up costs and working capital.

From the entrepreneur's point of view, the financial support comes with the Social Venture Fund's mindset of impact goals and is therefore an ideal investor to maintain the right balance between financial and social outcomes. The Social Venture Fund additionally supports the company through a position on the Advisory Board, leveraging the network of the fund's active investors, particularly in attracting and establishing partnerships with new companies looking for childcare services for their employees.

C.5 FINANCING AGENCY FOR SOCIAL ENTREPRENEURSHIP (GERMANY)

Theme: Using contracts to embed social mission

The Financing Agency for Social Entrepreneurship (FASE – www.fa-se.eu) was launched by Ashoka, to make growth for social enterprises financially viable and to help them to raise seed capital. FASE helps social entrepreneurs to develop hybrid business models and tailored financing models, sometimes based on conditional revenue sharing, and facilitates access to investors through the Ashoka Angels Network.

Typically, FASE applies various mission lock mechanisms in the financing contract between the investor and the social entrepreneur. These can include:

- A paragraph specifying that the growth capital can only be used in line with the current overall social mission of the social enterprise, which is defined in a preamble.
- Specific information rights (e.g., regular reporting on social impact) and control rights (e.g., investor approval of strategic shifts), which allow the investor to closely monitor the social mission of the investee.
- Withdrawal rights if there should be any mission drift of the social enterprise.

Overall, FASE is confident that there are strong economic incentives in place for the social enterprise to stick to their social mission, which is the basis for the initial investment decision of the investor.

C.6 OOMPH! WELLNESS (UK)

Themes: Attracting entrepreneurs; using legal objects to embed social mission; using contracts to embed social mission

Oomph! (www.oomph-wellness.org) provides exercise classes for older adults who are in care homes, with the aim of improving their mobility, social interaction and mental stimulation. Its founder, Ben Allen, is clear about its social purpose but chose a for-profit business model to allow the investment required to go to scale.

In Ben's words, "I also had a clear idea of the kind of investor I wanted: an investor that allowed us freedom to grow the company in the way we wanted while adding real value through their skills, networks and expertise. I knew I wanted equity investment (I didn't want to be paying back loans whilst profits were still slim and, more importantly, wanted a meaningful relationship with our investor that had a vested interest in our long term success). I also wanted investors that shared our values: namely a commitment to strong commercial returns but never at the expense of the health and wellbeing of the older adults we exist to serve.

When we found our investor (Nesta Impact Investments www.nestainvestments.org.uk), they ticked every box for us: we liked, respected and trusted the team, shared the values of the fund absolutely and recognised their expertise and networks in the ageing sector. We worked with them to add three things into our governing documents: a clear statement of our social purpose taking precedence over our commercial purpose; a commitment to transparently reporting on our

social impact; and a commitment to reinvesting the majority of our profits towards this social purpose. We then locked into our Investment Agreement that, even as a minority shareholder, our social investor now protects this social charter: we cannot change it without their permission.

My investors are taking big risks and I've taken a risk too. I had a nice cosy well paid job travelling the globe giving lectures. I gave it all up to return to Scarborough to knock on doors to care homes and not draw a salary for over two years. I am driven by the social impact of what we do. But not at any cost. I passionately believe we need to bring highly talented, hugely ambiguous, risk taking entrepreneurs to our sector and to offer them incentives that mean they're not compelled to return to safe, well-paid jobs that contribute nothing to society because there's a mortgage that needs paying."

C.7 PATIENTS KNOW BEST (UK)

Theme: Attracting entrepreneurs; using market 'lockstep' to embed social mission; using contracts to embed social mission

Patients Know Best (PKB) offers a digital patient record sharing system, meaning that a patient's records can be shared with their doctor, hospital, social workers and other professionals, enabling more efficient and cost-effective care. PKB's customers are primarily hospitals and pharmaceutical companies. The company is also starting to work with social workers, doctors and pharmacy chains.

The key element is that the patient him/herself decides who has access to their records, and all healthcare professionals need their permission to look at these – and that ownership of the data rests with the patients themselves, so it cannot be sold on or commercialised.

From the beginning, equity in the business was held closely among the founders and family who understood the social mission. To date, PKB has not felt it necessary to include references to its mission in its Articles of Association, but this may soon change – PKB is about to close an investment round, and two of the prospective social venture capital investors have asked for this inclusion.

Aside from this, PKB embeds its social mission through contract with its customers. All of its contracts state that "The copy of data in a patient's

account is owned by the patient”. This contractual commitment is reinforced by a technical solution, which encrypts the data so that only the patient has the private key for decryption, and the patient decides who is allowed to use this.

This form of mission lock is market-facing rather than investor-facing. It works because the social mission is directly aligned with the customer offer and commercial success of the business – so called ‘lockstep’. PKB’s founder Mohammad Al-Ubaydli notes that this lockstep also aligns investors’ interests with the mission: “from a shareholder perspective, that’s why customers are buying from us and it’s why our investors want to invest”.

C.8 B LAB (US/GLOBAL)

Theme: Transparency and impact reporting; Using legal objects to embed social mission

B Lab (www.bcorporation.net) is a US-based non-profit organization that seeks to develop a global movement to redefine success in business so that all companies compete not only to be the best in the world, but the best for the world. At the core of its operations are B Analytics, a customizable platform for measuring, benchmarking, and reporting on impact and driving mainstream capital to high-impact enterprise; and the B Impact Assessment, a tool for businesses to measure, compare and improve their social and environmental performance. It also promotes the development of innovative legal forms, such as the Benefit Corporation and similar forms in the United States, which allow companies to institutionalize their commitment to create material positive impact on society and the environment.

There are 1,000 Certified B Corps in 32 countries, over 1,200 GIIRS Rated companies globally, and over 700 companies have legally incorporated as benefit corporations in 27 states in the United States. There are over 100 institutional investors and fund managers including JP Morgan, UBS, and Prudential using B Analytics for their impact investments. Over 17,000 companies are using the B Impact Assessment to measure their impact. Worldwide, 30 million consumers are engaged in the B Corp movement through the recently launched B the Change Campaign; B Lab has created partner organizations in Canada, Latin America, Europe, and Australia to serve and support this growing global movement.

Certified B Corps choose to hold themselves to high standards of social purpose, accountability, and transparency. B Corp certification is to the whole company what Fair Trade certification is to coffee or LEED certification is to green buildings. To be certified, a company must:

- receive a minimum score of 80 out of 200 on the B Impact Assessment, a comprehensive, comparable, and transparent assessment of the impact of the company’s products and practices on its workers, community, and environment; and
- change its legal articles to include explicit consideration of the interests of its stakeholders, not just its shareholders, when it makes both operating and liquidity decisions.

Once a company has achieved a satisfactory score on the B Impact Assessment and completed their Assessment Review with a B Lab team member, the next step in the process of becoming a Certified B Corporation is to meet the legal requirement. The details of this requirement vary depending on a company’s legal structure, place of incorporation, and ownership structure. B Labs argues that the value of meeting the legal requirement for B Corp certification is that it bakes sustainability into the DNA of a company as it grows, brings in outside capital, or plans succession, ensuring that its mission can better survive new management, new investors, or even new ownership.

The benefits of the legal requirement:

- Give legal protection to directors and officers to consider the interests of all stakeholders, not just shareholders, when making decisions
- Create additional rights for shareholders to hold directors and officers accountable to consider these interests
- Limit these expanded rights to shareholders exclusively

C.9 BENEFIT CORPORATION LEGISLATION (US)

Theme: Using legal form to embed social mission

Over half of the 50 states of the United States have authorized a new form of for-profit corporation, which is known as a “benefit corporation” and is designed for businesses that want to maximize their performance as measured by the triple bottom line of people, planet, and profits. Benefit

corporations are subject to the laws governing traditional business corporations, except that they have the three basic characteristics of a profit-with-purpose business: (i) their purpose includes having a positive impact on society and the environment, (ii) the duties of their directors include furthering that broaden purpose, and (iii) they must report on their creation of positive impact.

Businesses may be organized in a variety of different forms under United States law. The two most popular are the business corporation and the limited liability company (LLC). The purposes and governance of LLCs are largely determined by a private contract among the owners. The purposes and governance of a business corporation, in contrast, are largely controlled by the statutory law on corporations. Because of the flexibility of the LLC form, businesses may be organized as LLCs under existing law with the three characteristics of profit-with-purpose businesses. Not so with business corporations. Although a business corporation may adopt a specific purpose or mission, it is not possible to adopt a broad commitment to pursuing the triple bottom line. The benefit corporation form solves that problem for existing businesses organized as corporations and newly formed businesses that wish to be corporations.

Benefit corporations appeal to both ends of the political spectrum in the United States. They appeal to liberals because of their commitment to the triple bottom line, and they appeal to conservatives because they are a way of using the free market to solve social problems without the need for government involvement. That bipartisan appeal is seen in the fact that there have been 25 unanimous votes in state legislative chambers on passage of benefit corporation laws and in 11 states the legislation passed both chambers of the legislature unanimously. Since the adoption of the first benefit corporation law in 2010, over 1,000 benefit corporations have been created.

C.10 SOCIAL ENTERPRISE LEGISLATION (ITALY)

Theme: Using legal form to embed social mission

Italian law allows for the status of 'social enterprise' to be applied to a range of legal entities including for-profit structures such as limited liability companies and cooperatives. However, in order to qualify, businesses must give up their ability to distribute any profits to owners, and they are

subject to other restrictions. The status has seen very limited take-up.

In May 2013, the Italian government undertook a consultation on possible reform of this legislation, which resulted in the presentation of a Bill to Parliament in July 2014. This laid the foundations for a further Legislative Decree that would, among other things, extend the scope of activities that can be carried out by a social enterprise and their freedom to undertake commercial activities that are not related to the social purpose. Crucially, the Decree would also allow for the distribution of profits, "in accordance with predetermined limits and conditions". It is not yet clear what these limits and conditions will be, and the timeframe for the further elaboration and introduction of this legislation is as yet unannounced.

C.11 LEARNING FROM EXPERIENCE WITH LEGAL FORMS AND PROFIT LOCKS (UK)

Theme: Using legal form to embed social mission

The UK introduced a specific legal form for social enterprises in 2005. Called the Community Interest Company (CIC), it closely resembles conventional company law forms, but has additional 'community interest' requirements and an asset lock. It is overseen by a 'light-touch' regulator, with whom all CICs must file an annual community interest report. Since 2005, almost 10,000 CICs have been registered. Although this is a substantial number, it still represents a minority of social enterprises in the UK, the majority of social entrepreneurs choosing more traditional legal forms including conventional for-profit businesses and entities that can be registered as charities.

CICs can be established as a Company Limited by Guarantee, a Company Limited by Shares or a Public Limited Company. The most common form of CIC is a Company Limited by Guarantee, which does not allow any level of private ownership or profit distribution. The Company Limited by Shares is of particular interest to the Working Group, as this allows for the limited distribution of profits and there has been considerable learning from experience with this form of CIC since 2005. In the words of the CIC Regulator:

"Offering a shares model for enterprises with a social purpose was a bold and imaginative step when it was set up and I intend to ensure that it continues to offer a great opportunity to entrepreneurs who

want to use it to grow their business for maximum community and social benefit.”¹⁸

Since it was first introduced, the restrictions on the distribution of profits by a CIC Company Limited by Shares have been formally reviewed twice by the CIC Regulator. These reviews have both resulted in changes that have relaxed the restrictions on the distribution of dividends. The CIC Regulator describes the rationale for this as follows:

“Access to investment however remains an issue and I continue to hear that there are some potential barriers to investment. This is not new, concerns had been voiced previously and in 2009 I undertook a review of the caps on investment. This consultation ... concluded that the caps were unduly complicated and restrictive. The results were persuasive but because of the relative newness of the model I decided to proceed with caution. I made a number of small but important changes; raising the dividend and interest caps and making the process simpler by removing the reference to the Bank of England base rate.

In my time as Regulator, I have been struck by the fact that the percentage of CICs that have adopted the limited by shares model has changed little over the last 8 years and remains under 25%. The changes I introduced in 2010 did not result in increased take-up which is disappointing and supports the view that there are still issues with the model.”

The CIC Regulator undertook a further consultation during 2013, which resulted in a decision to further relax the limit on profit distribution. Currently, the CIC limited by share has a two-part cap on the distribution of profits. The so-called ‘dividend cap’ will be removed, leaving just an aggregate cap that limits total dividend payments to 35% of profits. This will give CICs much greater discretion to reward investors, while still ensuring that a large majority of profits are retained and used for the social purpose. The recommended changes are scheduled for introduction in late 2014.

Once the dividend cap has been removed, there will no longer be a link between dividends payable and the initial value of shares. This should allow shares in successful CICs to appreciate. Currently, there is little incentive for investors to buy shares at anything more than their initial face value, as future dividends are restricted to 20% of that initial value. So returns to investors are severely limited and there is no secondary market in CIC shares.

C.12 NEW DEDICATED FORMS FOR SOCIAL ENTERPRISE (CANADA)¹⁹

Theme: Using legal form to embed social mission

Social enterprises in Canada can adopt a range of forms, from enterprising non-profits and charities, to co-operatives and social-purpose for-profit businesses – including over 100 registered B Corporations. There is also a new hybrid corporate form for social enterprises in British Columbia – the Community Contribution Company (C3). Nova Scotia has similarly passed Community Interest Company (CIC) legislation; however, the regulations are still in development. Ontario has launched a consultation process on a potential hybrid corporate form.

British Columbia’s Community Contribution Company (C3) was introduced in July 2013. It is modelled on the UK Community Interest Company, and has a legally enforced social purpose. The majority of the profits must be used for community purposes or transferred to a qualified entity. There is a cap on dividends payable to investors of 40% of annual profits and an asset lock upon dissolution (at least 60% of assets must be directed to qualified entities). Like in the UK, there is a requirement for annual reporting on community contributions, but unlike in the UK, there is no official verification of reports and no regulator.

Industry Canada is also consulting on the possible introduction of a purpose-built hybrid corporate form for social enterprises at the national level, which is seen as desirable for consistency. According to the MaRS Centre for Impact Investing, “a hybrid corporate form introduced at the national level could respond to the needs of a sub-set of social enterprises that are seeking to raise share capital, while locking in a social purpose to ensure its longevity, and providing assurances to customers and investors who are driven by social impact considerations. This could have significant impact on the growth of social enterprise activity in Canada.” However, MaRS emphasises that a new, national legislative form, while beneficial, is currently less of a priority for the sector as a whole than reforms that allow non-profits and charities greater freedom to engage in revenue-generating activities.

¹⁸ Department for Business, Innovation and Skills (2013) Changes to the Dividend and Interest Caps for Community Interest Companies. Available at <https://www.gov.uk/government/news/changes-to-the-dividend-and-interest-caps>

¹⁹ This example draws heavily on analysis by the MaRS Centre for Impact Investing, in particular its submission to Industry Canada’s consultation on the Canada Business Corporations Act in relation to the incorporation structure for socially responsible enterprises. <http://impactinvesting.marsdd.com/>

C.13 SOCIÉTÉ À OBJET SOCIAL ETENDU (FRANCE)

Theme: Using legal form to embed social mission

Academics and practitioners have proposed a new corporate form in France, similar to the US Benefit Corporation. Labelled the Extended Purpose Corporation, or Société à Objet social Etendu (SOSE), the concept has attracted significant attention at the national level.

The proposal aims at revitalizing and extending the notion of “corporate purpose²⁰”, which used to be defined to get a governmental authorization before 1867. Today, the corporate purpose has lost its significance and is narrowly interpreted as the financial purpose. But the for-profit business can pursue a much broader and more innovative purpose. Crucially, the SOSE would allow for the creation of a new Board to evaluate the management of this wider purpose. It would do this as follows:

- Any corporation, whether a social enterprise or conventional for-profit corporation, would have the option of embedding in its articles an extended (social or environmental) purpose.
- It would only be possible to revise the extended purpose by a super-majority (two-thirds or three-quarters). This offers a “safe harbour” for officers and directors to develop ambitious impact-oriented strategies.
- Accountability and transparency regarding the extended purpose would be secured through a second, purpose-oriented Board. This would be composed of experts and committed parties and the Board of Directors would be bound to take into account its reports. It would evaluate the corporate strategy regarding its extended corporate purpose and assess performance against it.

The second Board would play the role undertaken by external auditors (in the case of Benefit Corporations) or by the sole Board (in the case of Flexible Purpose Corporations).

C.14 SOCIAL RETURN ON INVESTMENT (SROI) NETWORK (GLOBAL)

Theme: Transparency and impact reporting

The SROI Network is an international membership organisation with members in over 40 countries. The board includes representatives of national affiliated

networks including Japan, Hong Kong, Australia, Netherlands and Sweden. SROI is a principle-based framework for accounting for the wider impact of an organisation’s work. The inevitable judgements on what is included and excluded from that account mean that an assurance process is required and one of SROI’s seven principles is to have appropriate verification of a social account, depending on audience and purpose.

One of the Network’s services is assurance (www.thesroinetwork.org/sroi-analysis/assurance) of reports for compliance with the SROI principles:

1. Involve stakeholders
2. Understand what changes
3. Value the things that matter
4. Only include what is material
5. Do not over claim
6. Be transparent
7. Verify the result

Assurance is also the way in which an organisation can be held to account by its stakeholders, who, as beneficiaries, may have no other way of ensuring that what is being reported on includes the information they would expect to receive. Assurance contributes to credibility of claims, increased reliability and security and confidence. Running a team of thirty experienced assessors drawn from an international community of SROI Accredited Practitioners, the Network uses criteria to test for adherence to its principles.

Assurance is provided at different levels. The first is a principles only based approach and the second involves the assurance of data and evidence. The Network is about to launch an online self-assessment tool for organisations to assess their approach against these principles. The Network is also involved in verification of software designed to assist in the impact reporting process.

C.15 BIG VENTURE CHALLENGE (UK)

Theme: Attracting commercial investors

Big Venture Challenge (www.unltd.org.uk/bvc) is an accelerator programme for growth-oriented social ventures, supported by the Big Lottery Fund and delivered by UnLtd and partners. First run in 2012, it takes a cohort of social ventures through a year-long

²⁰ In French, «objet social» can be both interpreted as «social purpose» and «corporate purpose» (the legal term for corporation in French is «société»).

programme of investment-readiness and other support, helping them to refine their business models and networks and introducing them to potential investors. When investment is secured, UnLtd also provides a co-investment in the form of a grant, part of which is repayable based on performance. The package effectively de-risks the investment and enhances the investibility of the venture.

Over half of the social ventures in the programme have for-profit legal forms. These ventures are required to consider how they can lock in their social mission, although the programme is not prescriptive regarding how this is done.

Of the 2012 cohort, just over half of the ventures attracted investors, with an average deal size of £158,000. One year on, those that secured investment had increased the number of beneficiaries by 162%, compared with 25% for those that had not. Of the 2013 cohort, two-thirds secured investment from a total of 75 angel investors, with an average deal size of £253,000. The programme shows how it is possible to draw commercially-motivated investors into the profit-with-purpose sector at the angel stage.

Research commissioned by UnLtd has found that entrepreneurs opt for a profit-with-purpose model for the following reasons:

- Simplicity
- Access to a full range of finance, including equity
- Flexibility
- Familiarity
- Allows for financial return while embedding social mission
- Allows the entrepreneur to retain control
- Enables shared ownership with investors
- Demonstrates the principle that social impact and profit can co-exist.

C.16 FINANSOL (FRANCE)

Theme: Investment fiduciaries

France has stimulated the social impact investment market through tax advantages for solidarity investments funds and a '90/10' rule, which obliges corporate employee pension fund managers to offer savers a choice of investing in funds which invest 5-10% of their capital in the 'solidarity

economy'. This has channelled the savings of over a million individuals into investment in the solidarity economy. Total investment in the French solidarity economy amounts to approximately one billion Euro, including bank saving products, corporate employee plans and investment funds.

In response to this policy support, Finansol (www.finansol.org) was established as an industry-led market mechanism that identifies which investment funds qualify as solidarity financing vehicles. It takes the form of a label. It is overseen by the Finansol Association, which seeks to promote, defend and analyse solidarity finance. The label is granted by an independent committee of twelve members, who have expertise in social finance. In 2013, the Finansol label was awarded to its 132nd recipient.

The primary criteria for the label are:

- **Solidarity:** If the investment is made through a mutual fund or a life insurance policy, 5-10% of the fund's assets must be invested in social businesses. The remaining assets must respect environment, social and governance criteria. In the case of solidarity savings accounts or term accounts, at least 25% of the interest payments must be granted on an annual basis to a non-governmental organisation.
- **Transparency:** A correspondent is made available to give investors all the necessary information they might request. This person is in touch with the Finansol team on a regular basis.

The label has secondary criteria, including management fees, volume objectives and promoter support. Financial return on investment is not a criterion.

Finansol also defines which investee enterprises qualify for investment from Finansol-labelled funds. The Finansol label is used as a marketing tool by potential investees. It is offered as private accreditation alongside the government-managed 'solidarity' accreditation, which relates to eligibility for investment through the 90/10 pension funds. The main difference between the two is that the Finansol criteria is more specifically related to the potential investees' mission, whereas the government label is partly based on legal form, and for example is awarded to any co-operative, irrespective of its mission. Forthcoming legislation is expected to amend the government label to be more focused on mission.

ANNEX D: METHODOLOGY AND MEMBERSHIP

The Mission Alignment Working Group (the Working Group) was one of four working groups formed by the Social Impact Investment Taskforce established under the UK's presidency of the G8.

The Working Group met in person on three occasions (21 January 2014, 20 March 2014, and 2 May 2014). A variety of written materials were circulated to the Working Group between meetings, and the Working Group was twice solicited for written comments on drafts of the Recommendations.

The Working Group also received feedback and inputs from National Advisory Boards, other Working Groups, and many other experts and practitioners from across the world, for which we are indebted.

The members of the Working Group are listed below:

Name	Organization	Position	Country
Cliff Prior <i>Chair</i>	UnLtd	CEO	UK
William H. Clark, Jr. <i>Reporter</i>	Drinker Biddle & Reath LLP	Partner	USA
Ben Allen	Oomph	Founder	UK
Ingo Ballschmieter	Bertelsmann Foundation	Advisor to the Executive Board	Germany
Olivier de Guerre	PhiTrust	Chairman	France
Lucy Fergusson	Linklaters	Partner	UK
Mark Florman	Fortitude Partners	Chairman	UK
Pamela Hartigan	Skoll Centre for Social Entrepreneurship	Director	UK
Peter Holbrook	Social Enterprise UK	CEO	UK
Ken Ito	Asian Venture Philanthropy Network	Japan Advisor	Japan
Andrew Kasoy	B Lab	Co-founder	USA
Stephen Lloyd	Bates Wells & Braithwaite	Partner	UK
James Perry	Panahpur	CEO	UK
Fried Roggen	S12 Fund	Fund Manager	Belgium
Blanche Segrestin	Mines ParisTech	Professor	France
Johannes Weber	Social Venture Fund	Managing Partner	Germany
Simon Willis	Young Foundation	CEO	UK

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- Sir Ronald Cohen, Chair of the Social Impact Investment Taskforce established under the UK's presidency of the G8
- Tom Fox, Policy Lead, UnLtd
- Rebecca Thomas, Office of Sir Ronald Cohen

