Legal reform as a catalyst for social enterprise:

an international social enterprise law & policy report

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With support from:

LexMundi Pro Bono Foundation

About

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Lex Mundi Pro Bono Foundation

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I. Introduction

Achieving rapid, large-scale improvements in social, environmental, and economic outcomes for people and business in all countries around the world is an imperative that requires an "all hands on deck" approach. It is not enough to leave it to governmental and non-governmental organizations to do the hard work of addressing climate change, environmental degradation, and inequalities in health outcomes, education, and social welfare. On the other hand, while many businesses have also taken steps to address these problems, we cannot rely on the goodwill of business interests at large to reform economic systems to promote sustainable growth.

Social enterprises therefore have a vital role to play in bridging this gap. Social enterprises integrate social, environmental, and other impact objectives with traditional business practices and techniques to seek profitable, and therefore self-sustaining, operations while serving the common good. Although social enterprises can be found in all corners of the world, most jurisdictions suffer from a dearth of laws and policies that support them, and in some cases, requirements that may be an actual hindrance to their proliferation.

Accordingly, we have produced this social enterprise law and policy report (this "Report") to identify legal structures and policies that nations can adopt to catalyze the advancement of social enterprises around the world. The recommendations and observations included in this Report have been derived from our review of laws and policies that help social enterprises flourish in 83 jurisdictions around the world, covering every inhabited continent and every major legal structure.[1]

[1] Morrison & Foerster LLP ("M&F" or "we") has reviewed surveys completed by attorneys at 65 prestigious law firms that have volunteered to participate in this project on a pro bono basis. In preparing this Report, we have presumed the accuracy of each survey, without independent verification thereof. For those interested, the individual survey responses from the attorneys can be found online at: lexmundi.com/SocialEnterpriseLawSurveys

Our goal in producing this Report is not to summarize any individual nation's approach to social enterprises. Nor do we intend to prescribe for any individual nation what we believe is the best approach to promote social enterprises. Rather, the goal of this report is to explore a "menu" of tools that legislators and policymakers around the world may seek to implement in their jurisdictions to encourage the formation, and promote the success, of enterprises seeking to "address the global challenges we face, including poverty, inequality, climate change, environmental degradation, peace, and justice."[2]

Social enterprises and the sustainable development goals

Before addressing our key findings, it is necessary to explain how we define "social enterprise." For the purpose of this report, an "enterprise" is any business entity or legal concern, regardless of legal structure. A "social enterprise" is an enterprise, whether structured as a for profit or not-for-profit entity, that, in addition to engaging in a trade or business, endeavors to create a more just and sustainable society in some manner consistent with the United Nations' Sustainable Development Goals ("SDGs"), including by operating their business through a framework that emphasizes environmental, social, and governance ("ESG") factors and that, in so doing, may or must consider the interests of stakeholders other than equity holders.

Of course, these are not definitions without controversy. Not all enterprises are incorporated legal entities, but we refrain from discussing unincorporated associations primarily because they do not generally operate under the purview of the legal regimes that would promote social enterprise generally. Not all social enterprises are formed with the conscious intent to further the SDGs, but the SDGs are broad enough that any true social enterprise should be able to map its environmental or social mission against at least one, if not several, of the 17 SDGs. Some jurisdictions may also have a narrower view of a social enterprise that is much less permissive of profit motive, but adopting such a limiting definition would exclude enterprises incorporated under explicit social enterprise statutes adopted in standards-setting states of the United States of America, such as California or Delaware, as well as of other countries we discuss in this Report.[3]

[2] The United Nations so describes its Sustainable Development Goals.

[3] Most Delaware public benefit corporations or California social purpose corporations would not meet all the criteria used in the UK Cabinet Office's "Social Enterprise: Market Trends," or the following six criteria similar to the definition of "social enterprise" used in "A Report on the Aggregated Activity Size of Social Enterprises in Japan" (May 2015, Cabinet Office of Japan): 1. The enterprise should have mainly social or environmental aims; 2. The main purpose of the business should not be pursuing profit but solving social/environmental issues or making social contributions; 3. The business surpluses should principally be reinvested for the purpose of the business or community rather than being paid to shareholders and owners; 4. It should not pay more than 50% of its profit or surplus to its owners or shareholders; 5. Revenue generated from its business should not be less than 25% of its total revenue; and 6. No more than 75% of its total income should rely on grants and donations.

Figure 1. The 17 United Nations SDGs, adopted in 2015.

1 NO POVERTY

2 ZERO HUNGER

3 GOOD HEALTH AND WELL-BEING

4 QUALITY EDUCATION

5 GENDER EQUALITY

6 CLEAN WATER AND SANITATION

7 AFFORDABLE AND CLEAN ENERGY

8 DECENT WORK AND ECONOMIC GROWTH

9 INDUSTRY, INNOVATION AND INFRASTRUCTURE

10 REDUCED INEQUALITIES

11 SUSTAINABLE CITIES AND COMMUNITIES

12 RESPONSIBLE CONSUMPTION AND PRODUCTION

13 CLIMATE ACTION

14 LIFE BELOW WATER

15 LIFE ON LAND

16 PEACE, JUSTICE AND STRONG INSTITUTIONS

17 PARTNERSHIPS FOR THE GOALS

Infographic available at:
https://en.unesco.org/sustainabledevelopmentgoals

Further, not all jurisdictions recognize a particularly sharp distinction between a social enterprise, as defined in this Report, and any other enterprise. For example, enterprises adopting the most commonly used Japanese for-profit organizational form[4] generally may have any purpose that does not violate public order or morals, and the main purpose of such enterprises can be to contribute to the general public interest and society regardless of profitability. Thus, many companies (if not nearly all companies) in Japan may literally meet our definition of the term "social enterprise."

We do not, however, believe this example renders our definition of social enterprise unusable. Instead, this signals to us that Japan, or countries with corporate structures similar to Japan's, need not focus on creation or amendment of corporate forms to permit social enterprise, but instead may wish to consider other measures to promote achievement of the SDGs through social enterprises.

The unique challenges of, and opportunities for, social enterprises

This Report does not seek to address all of the obstacles to success of social enterprises throughout the world, nor to address all potential laws and policies that may be implemented to promote social enterprise. If we did, the scope of this Report would then simply be too large.

In part, we limit our Report by considering obstacles to success that are unique to social enterprise as distinct from traditional for-profit or non-profit ventures. So, for example, this Report does not address issues with corruption, lack of rule of law, excessive time, expense or red tape associated with forming a legal entity, and other issues that hinder the quick and easy formation and operation of all types of enterprises.[5]

In part, we focus our Report on policies that promote social and public policy objectives but that are designed to benefit social enterprises both specifically (as opposed to all corporations generally) and generally (as opposed to enterprises only pursuing specific goals and objectives). In other words, we do not attempt to summarize the myriad ways in which countries promote specific social objectives, such as affordable housing or reduction in carbon emissions, through targeted tax credits, subsidies, and other programs and that are available to various types of qualifying enterprises.

[4] The Japanese joint stock corporation, or *kabushiki kaisha*, which is also the most commonly used form for social enterprises in Japan.

[5] For more information on legal barriers to enterprise generally, see, for example, Maria Martini, *Reducing Bureaucracy and Corruption Affecting Small and Medium Enterprises*, U4 Expert Answer (2013), https://www.transparency.org/files/content/corruptionqas/380_Reducing_bureaucracy_and_corruption_affecting_small_and_medium_enterprises.pdf

Finally, we limit our recommendations to those that we believe not only are consistent with the general legal and philosophical framework underlying corporate, tax, and other legal regimes around the world, but also those that may actually be adopted by legislators and policymakers actively seeking to, and having some power to, change and implement laws and policies relevant to social enterprise. We would not, for example, recommend reducing reporting requirements for social enterprises structured as non-profits, as compared to the reporting requirements for purely charitable non-profits in the same jurisdiction. Certainly this would make it easier to operate a social enterprise in that jurisdiction, but it would also invite fraud. Indeed, fair and fulsome reporting is a standard quid pro quo for the beneficial tax treatment attendant with the nonprofit form, and the transparency that comes with reporting standards is necessary for donors and regulators to ensure that a nonprofit is in fact working to achieve its public, social, or environmental mission. Nor would we recommend that all social enterprises structured as traditional for-profit entities be fully tax free – that is simply not in the cards in most, if not all, countries.

Key recommendations

Based on our review of laws and policies in place around the world, suggestions from counsel participating in this project, and, of course, our own experience practicing in this space, we have distilled our recommendations for how, from a legal perspective, countries may better help social enterprises flourish to six key strategies:

1 Define social enterprise

Most jurisdictions neither have a definition of “social enterprise” nor have laws, policies, or programs specifically tied to social enterprises. The first step in supporting social enterprises is for governments to define what should constitute a social enterprise in that jurisdiction, based on what policy outcomes that jurisdiction wishes to promote. Countries can then enact various different policies and programs across legal regimes, from corporate law to tax policy to securities law, based on that standard.

❷ Enable fiduciaries to consider stakeholders other than business owners

Many jurisdictions lack clarity when it comes to whether corporate directors, fund managers, and other corporate fiduciaries may consider social and environmental impact alongside financial return to investors.

Without that clarity, many entrepreneurs that seek to form social enterprises are limited to either using non profit forms, putting them at competitive disadvantages to enterprises that can more easily generate profit and take in outside investment, or forming as a for-profit that must value shareholder return above other impact. Further, fund managers must be enabled to consider social and environmental impact in order to facilitate investment in social enterprises by all manner of institutional and other investors.

❸ Provide tax benefits to social enterprises and investors in social enterprises

Most countries we surveyed around the world take the position that for-profit enterprises are taxed one way, and non-profit enterprises are taxed another. Some surveyed countries do provide tax benefits to for-profit enterprises organized as cooperatives or for-profit enterprises that help promote certain economic initiatives, but there is no middle ground for social enterprises that do not wish to organize as a cooperative or limit their operations to investment in specific development areas or projects. There is no need for such a black-and-white approach. For-profit social enterprises should be rewarded for pursuing public good with tax benefits, whether lower tax rates, tax credits, or otherwise.

Similarly, investors that support social enterprises should be rewarded with favorable tax treatment on dividends and other returns on their investment.

❹ Make it easier to invest in social enterprises

It is inherently difficult for social enterprises to fundraise, as there is both a perception and, in many cases, a reality that social enterprises will have lower returns than regular businesses, making them less competitive in the hunt for capital. To counterbalance this difficulty, regulators should focus on removing and minimizing legal obstacles to fundraising, such as limitations on the ability of cooperative ventures to have financial investors and limitations on crowdfunding imposed by securities laws.

❺ Guard against corruption and "greenwashing"

Any changes to tax policy or other laws that provide benefits to social enterprises, or that make it easier to operate as social enterprises, will incentivize businesses to characterize themselves as social enterprises solely for the purpose of achieving the benefits, even without having a true social or environmental mission.

In order to prevent corruption and confirm program eligibility, it is vital that in addition to defining what it means to be a social enterprise, jurisdictions require some form of reporting or certification as to an enterprise's continued compliance with the relevant standards. Furthermore, including meaningful, quantifiable reporting requirements – especially those coupled with independent third-party audit requirements – with respect to achievement of a social enterprise's publicly stated impact goals can help guard against businesses exaggerating their impact through puffery and spin.

6 Be flexible. Allow for scaled application of rules and “opt-in” features

Not all social enterprises should be treated the same. Some may be small start-ups structured as non-profit corporations; others may be large, publicly traded companies with cash assets and annual revenues of tens of millions of dollars or more.

Policies should be flexible enough to consider and apply to many types of social enterprises; moreover, regulators should consider whether certain areas lend themselves well to scaled applications or elective features, in which the more a social enterprise does to demonstrate its commitment to ESG principals and achievement of impact objectives, the more it benefits from favorable treatment under the law (ensuring, of course, that the companies with the greatest resources to prepare impact reports and otherwise justify their impact do not take up the lion’s share of benefits intended for smaller businesses).

The remainder of this report discusses in detail the various ways jurisdictions do and can implement legal structures and policies in line with these recommendations.

II. Corporate form

Despite – or because of – the many traditional alternatives available, in many jurisdictions, social enterprises often find themselves, as far as corporate form is concerned, without a clear home. Across jurisdictions, many social ventures simply default to the non-profit structure, whether because they do not believe they can effectively pursue a social mission given constraints on for-profit companies, because they seek the tax benefit and grant monies only available to non profit enterprises, or due to a belief that social enterprises should only be formed as non profits. Accordingly, a key step legislators and policymakers can take to facilitate the formation of social ventures would be to: (A) amend traditional for-profit structures to facilitate social or environmental mission and other motivations other than profit and equity holder value; and/or (B) create a new for-profit corporate form, or forms, specifically designed for social enterprises.

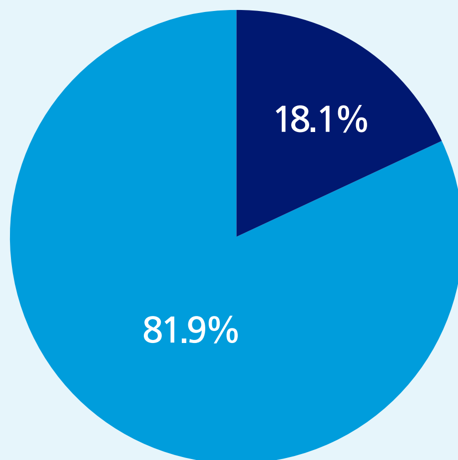
Introduction

Most jurisdictions have one set of corporate forms more traditionally used with enterprises intending to generate profit for shareholders ("for-profits") and one set of corporate forms more traditionally used with enterprises organized to further the public good and whose assets may not be distributed for the enrichment of private individuals ("non-profits").[6] On the for-profit side, we frequently see that corporations and limited liability companies are prevalent in common law jurisdictions, with similar forms used in civil law jurisdictions, such as the German *Gesellschaft mit beschränkter Haftung* ("GmbH"), the Japanese *kabushiki kaisha* ("KK"), or the Francophone *société anonyme* ("S.A."), where a company can pursue any purpose set forth in its Articles of Association as long as such purpose does not violate any law or good manners.

Jurisdictions also tend to have several non-profit corporate forms, which may be very similar or fundamentally different from for-profit enterprise forms, including structures to accommodate tax-exempt charities, tax-exempt foundations, and even entities that operate without a private profit motive but that may not be tax-exempt.

[6] It is important to understand that most non-profit entity types are not prohibited from earning profit, rather, they simply may not distribute those profits to members or other private individuals, and certain excess profits may be subject to taxation. Similarly, most for-profit entities are by no means prohibited from engaging in charitable activity.

Figure 2. International prevalence of distinct social enterprise forms.



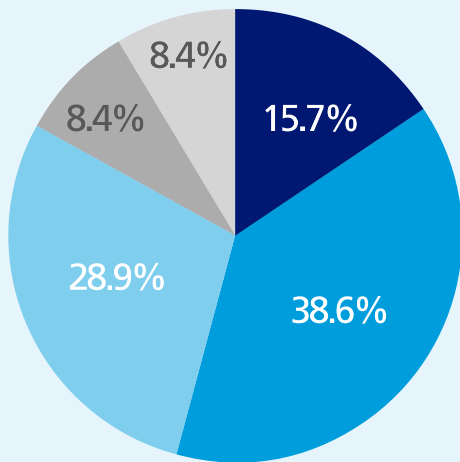
Only about a fifth of jurisdictions surveyed indicated the existence of a special form intended for social enterprises and that is distinct from traditional for-profit and non-profit forms. These special forms are generally either "benefit corporations" (see Seciton II.C.1) or a special form of cooperative corporaton (see Section II.C.2). These results suggest to us that many jurisdictions looking to advance social enterprise can do so in part by creating special forms for social enterprise, though certain jurisdicitons may not need them to the extent that traditional forms already contain built in flexibility (see Figure 3, page 17).

Enabling social and environmental mission in traditional for-profits

Jurisdictions vary in what is permissible for directors or managers of for-profit enterprises to consider in decision making. Based on our survey responses, the spectrum ranges from directors only being able to consider equity holder value to directors being able to consider other factors, such as ESG, in their decision making. In most states within the United States of America, the primary goal of a for-profit corporation is to seek value for equity holders, with boards of directors tasked with pursuing the best interests of the corporation itself and/or its equity holders. Indeed, it is understood by most practitioners that members of Delaware corporate boards of directors may be in breach of fiduciary duties to shareholders for taking actions that would detract from shareholder value as a result of other motivations.

This is simply not the case in many jurisdictions. The Japanese KK generally may have any purpose that does not violate public order or morals, and the main purpose of such enterprises can be to solve social problems regardless of profitability. In Pakistan, corporate directors have a statutory duty to promote the objects of a company not only for the benefit of its shareholders, but also in consideration of the best interests of its employees, the community, and the environment.

Figure 3. Ability of traditional for-profit fiduciaries to consider social or public benefit.



- Shareholder returns and social/public benefit may always be equally considered
- Shareholder returns and social/public benefit may be equally considered if articles allow, secondarily otherwise
- Social/public benefit can only be considered secondarily
- Social/public benefit cannot be considered
- Unknown

While most of the jurisdictions responding to queries on the matter allowed directors, managers, and other fiduciaries of traditional for-profit ventures to consider social or public benefit as well as shareholder value, generally speaking, shareholder value must be the primary consideration, unless corporate documentation contains specific clauses to the contrary. Interestingly, in a few jurisdictions, social and public benefit may always be considered equally with shareholder return; such countries accordingly may do not materially benefit from special corporate forms for social enterprise.

The Egyptian joint stock company and limited liability company, the most common forms of for profit corporations in Egypt, are permitted to consider and prioritize other interests alongside shareholder value.

Many jurisdictions fall somewhere in the middle. For example, in South Korea and the state of Nevada, directors have a fiduciary duty to act in the best interest of the company itself and do not owe a specific duty to the shareholders. While in Nevada, this is nevertheless generally understood to mean that the long-term economic return of the company has primacy, in South Korea, it means directors can or should consider the interest of the company's employees. The law of England and Wales allows directors to consider the long-term consequences of any decision on shareholder value by taking into account the following: fostering the company's business relationship with suppliers and customers, the impact of the company's operations on the community and environment, and the interests of the company's employees. Many practitioners would see these as secondary considerations for directors under Delaware corporations.[7]

[7] Even within England and Wales, the extent to which a board should focus on maximizing shareholder value above these other considerations is of ongoing debate. At least with respect to public companies, there is growing pressure to act in a way that takes into account the interests of a wider group of stakeholders.

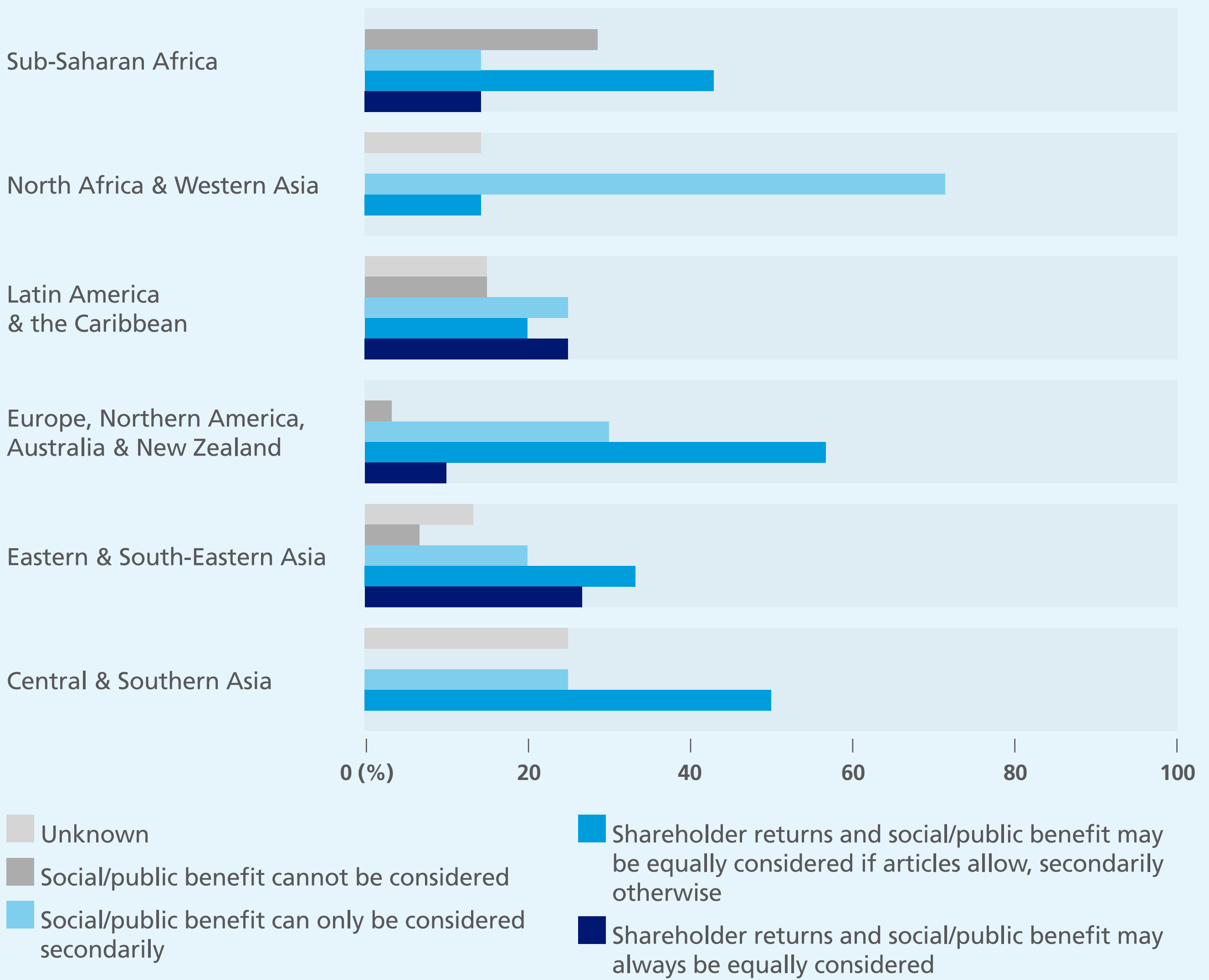
Likewise, in Israel, while maximizing profit to the company's shareholders is primary consideration, directors are also permitted to consider the impact of the company's operations on the general public and the interests of the company's creditors, employees, and other stakeholders. Further, in Israel, a company is permitted to make charitable donations irrespective of business objectives and goals if the company's charter includes a provision to that effect. Similarly, directors and officers of Canadian corporations are required to act honestly and in good faith, with a view to the best interest of the corporation, but Canadian courts have held that when acting with a view to the best interest of a corporation, it may be legitimate and is permitted for directors and officers to consider the interests of shareholders, employees, retirees, pensioners, creditors, consumers, governments, the environment, and the long-term interests of the corporation.

Put simply, the problem with the approach taken in many jurisdictions is that directors may be unable to consider the interests of stakeholders other than shareholders, or they may be unwilling do so for fear of liability for breach of fiduciary duty.

When a corporate form discourages directors from considering all stakeholders, it may be less than ideal for use by social enterprises.

Many countries, including Argentina, Liechtenstein, and Serbia, may thread the needle by providing as a default that directors should be primarily focused on profit maximization and exercising their powers in the best interests of the company and shareholders, but permitting directors to consider other interests, such as environmental or community impact, either to the extent such considerations do not materially detract from shareholder value or to the extent the organizational documents for the company set forth the other interests to be considered. Considering all these approaches, one simple measure countries may take to promote social enterprise and achievement of the SDGs would be to amend their corporate codes governing traditional for-profit enterprises to revise rules governing fiduciary duties of directors and managers to permit, or even require, their consideration of factors other than just financial returns and of stakeholders other than just shareholders, either generally or to the extent a special mission or interests are specified in a company's shareholder approved organizational documents.

Figure 4. Regional ability of traditional for-profit fiduciaries to consider social or public benefit



Encouragingly, no region appears to be particularly behind the curve when considering the ability of directors, managers, and other fiduciaries to consider social or public benefit. Notably, regions outside of Central & Southern Asia and Northern Africa & Western Asia do have some countries that allow directors to consider social and public benefit equally with shareholder return. Surveyed countries in Northern Africa and Western Asia, however, generally only allow social and public benefit to be of secondary concern to director decision making, suggesting that countries in that region may easily be able to make their legal regimes more friendly to social enterprise by either creating new corporate forms for social enterprise where none exist or allowing for social and public benefits to be equally considered if organizational documents specifically allow for this, particularly as countries in those regions do not, as of the date of our surveys, have such forms (see Figure 5, page 21).

Adoption of novel corporate forms and designations

While it might be simple from a conceptual perspective to expand the permitted mission and associated fiduciary duties of a country's traditional for-profit forms, this could effect a major change to the way that country's corporate laws have historically operated. Further, corporate forms like the Japanese KK that may allow for consideration of factors other than profit and shareholder return may not generally require such consideration, much less prioritization of SDGs.[8] Accordingly, legislators could instead consider adopting new corporate forms that are specifically tailored for social enterprises and that mandate consideration of interests other than shareholder value.

One potential hurdle to adopting a new corporate form that is specifically tailored for social enterprises may be the need to convince legislators, practitioners, and social entrepreneurs that not all social enterprises should be formed as non-profit or charitable organizations. Several practitioners we surveyed in producing this Report stated in firm terms that the appropriate enterprise form for a social enterprise must be a non-profit form, or otherwise suggested that a special enterprise form was not necessary.

It is our belief, however, that due to limitations on non profit and charitable organizations, such as restrictions on disposition of assets and distributions, those forms may not be attractive or appropriate enterprise forms for social enterprises hoping to scale and attract outside equity investors or even focus on a double, or triple, bottom line.[9]

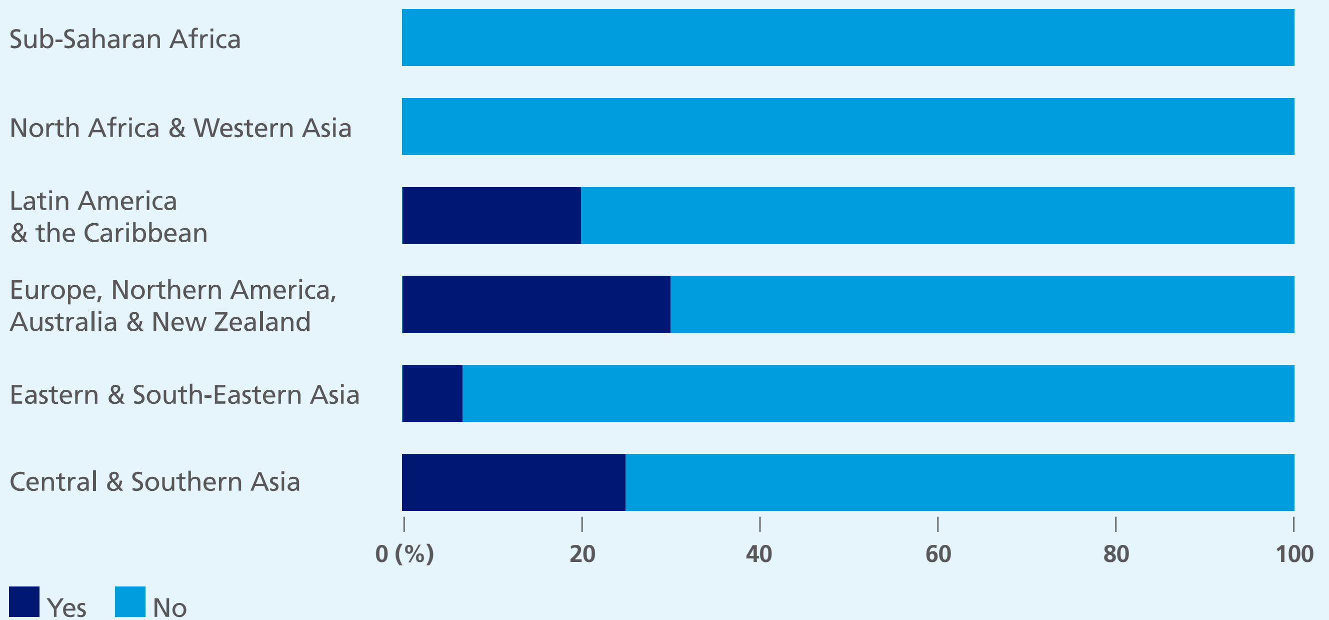
i. "Benefit" Corporate Structures

If a jurisdiction wishes to create a corporate form that is specifically tailored for social enterprises, they could choose to model it on enterprise forms found in the United States (for example, California benefit corporations or social purpose corporations, and Delaware public benefit corporations or public benefit limited liability companies), England and Wales (for example, community interest companies and community benefit industrial and provident societies), Canada (for example, British Columbia's Community Contribution Company), or Columbia (for example, sociedades comerciales de Beneficio e Interés Colectivo, or "BIC Companies").

[8] We note that in certain circumstances like bankruptcy or hostile takeovers, it is arguable that interests of employees of a Japanese KK be taken into account, but that is not a general requirement, even if many Japanese boards of directors may do so anyway.

[9] In industry parlance, a "double bottom line" measures not only the enterprise's financial performance, but also its performance in terms of positive social impact, whereas a "triple bottom line" further measures how environmentally responsible the enterprise has been.

Figure 5. Prevalence special social enterprise forms.



Breakdown of jurisdictions that allow for the creation of a corporate form specifically tailored to social enterprises and distinct from either the traditional for-profit or non-profit entity forms, by region. Note that Europe, Central & Southern Asia, and Latin America are leaders in allowing for such specifically tailored formations. However, there may be reasons that Eastern and South-Eastern Asian countries register lower in this regard: for example, the Republic of Korea already has special certifications for public benefit corporations, even they do not have an altogether separate form of entity for such corporations, and Japan allows directors of traditional corporations to consider public and social benefit equally with shareholder return in all cases, which reduces the need for separate and distinct social enterprise forms.

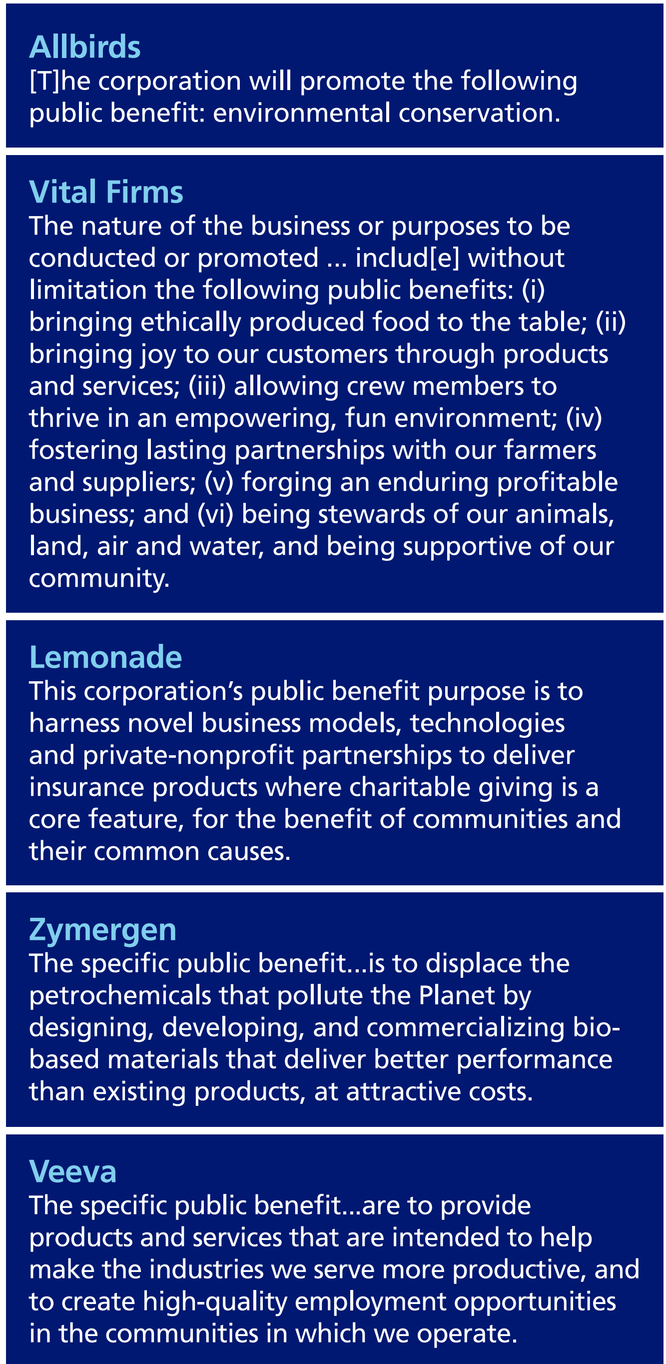
In adopting such a special, for-profit entity form, which, for purposes of this Report, we will refer to as "Benefit Corporations," we recommend that jurisdictions build upon the existing for-profit enterprise organization forms, rather than starting with completely new forms. This helps ensure that a well understood body of law applies to the new entity form and that it is clear where the new entity falls in the jurisdiction's overall legal framework, minimizing gaps and uncertainty.[10]

[10] By way of example, in the United States of America, we generally promote the Delaware public benefit corporation form or the California social purpose corporation form, which are based on the general corporation forms for Delaware and California, respectively, and which are materially different from the "benefit corporation" model statute promoted by B Labs and adopted in other U.S. states, but which statute operates as a stand-alone distinct form existing local corporate law. For more information on B Labs, see Section VI.C.

The requirement, or ability, to pursue a social purpose is the baseline for what a Benefit Corporation should provide for. A Benefit Corporation should commit, in its organizational documents or shareholder's agreement, to operate in pursuit of a public mission or social purpose. The laws stipulating the Benefit Corporation could provide for a general statement of public mission or focus on ESG matters or could require that the social enterprise specify a more tailored and specific public mission or social purpose in its organizational documents.

Parallel to the general requirement that enterprises keep financial books and records that can be made available to shareholders, Benefit Corporations may also have additional reporting requirements with respect to achievement of social mission. Issues related to reporting are discussed further below in Section VI, but regulations could include a requirement for Benefit Corporations to produce reports annually, every other year, or even every third year, on the ways in which the social enterprise pursued a general, or specific, public benefit during the covered period and the extent to which general public benefit was created. In Delaware, for example, public benefit corporations are required to provide their shareholders an impact report every other year, but may elect to do so annually instead.

Figure 6. Exemplar PBC Mission Statements.



Mission Statements found in the formation documents of selected publicly traded PBCs. As of September 9, 2021, there are 13 publicly traded PBCs.

Such a requirement helps assure that the Benefit Corporations are actively pursuing their social purpose or operating in such a way as to pursue general public benefit, rather than using the special enterprise form to illegitimately obtain additional benefits or reputational advantage.

In addition to mandatory or voluntary reporting, a Benefit Corporation form could contain so-called "asset lock" or "mission lock" provisions, which either allow or require that a portion of an enterprise's profits be retained to pursue the public mission or social purpose rather than being distributed to shareholders, or that upon dissolution or sale of the business, a portion of the assets or sale proceeds be distributed to other entities or organizations pursuing the social purpose (rather than all going to the shareholders). Asset lock terms apply to Benefit Corporations in several jurisdictions we surveyed. For example, enterprises incorporated under a Benefit Corporation form in England and Wales, and social enterprises incorporated under the Community Interest Company form in Northern Ireland, are subject to a 35% dividend cap to shareholders, outside of which distributions of assets outside of the enterprise may only be made in limited circumstances, including sale of assets at market value, transfer of assets to another asset-locked body, or transfers of assets that otherwise benefit the community. Similarly, under the Czech Republic's social cooperative (sociální družstvo) form, enterprises are prohibited from paying dividends to members in excess of one-third of disposable profits.

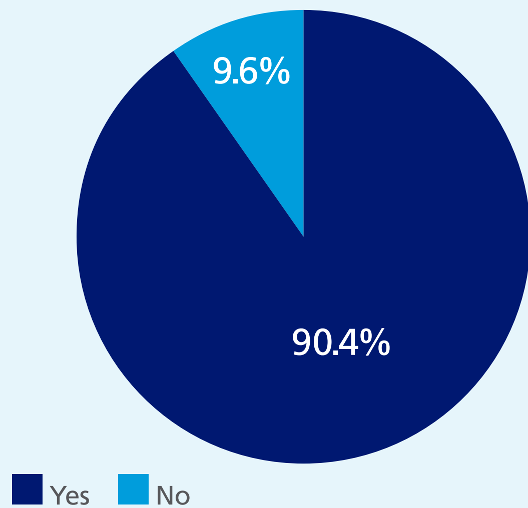
A jurisdiction could also provide that enterprises that utilize the Benefit Corporation form and adopt some or all of the optional add-on features could receive special benefits, such as lower tax rates or preferential access to government credit, grants, and other programs. For example, in Colombia, enterprises that voluntarily adopt the status of a BIC Company receive preferential access to credit lines offered by the national government, preferential rates for registration of trademarks and tradenames, and certain income tax benefits.[11] These add-on benefits could also be provided on a sliding scale. For example, a Benefit Corporation that adopted certain optional provisions could get access to government funding at a preferred rate, while an enterprise that adopted more of these optional provisions could also get a tax deduction (or vice versa).

[11] In Colombia, profits distributed as shares to BIC Company employees will be treated as non-income and "occasional profit" for income tax purposes. This treatment is limited to up to 10% of the profits that are effectively distributed to the company's employees either during the year they are generated or the following year.

ii. Cooperative corporations

Countries may also consider expanding the use of, or creating, a cooperative enterprise form. A "cooperative" is generally understood to be a farm, small business, or other organization that is owned and run jointly by its members (typically the workers and/or customers), who share in the profits or benefits. Approximately 90% of the countries we surveyed, including countries on every inhabited continent, allow for social enterprises to form as cooperatives. In most countries, cooperatives are neither new nor designed specifically for social enterprises, but by being worker or customer-controlled and managed, there is a greater alignment of investor interests with that of the business' stakeholders, which is helpful for keeping the social enterprises' mission locked. Further, cooperatives in many of these countries are provided tax benefits and potentially increased access to government and philanthropic funding.

Figure 7. Percentage of jurisdictions with cooperatives



Cooperatives are widely used entity structures. Jurisdictions that do not permit formation of cooperatives are in a small minority, and policy makers in such jurisdictions are strongly recommended to consider whether adopting this form, which can allow for greater stakeholder-shareholder alignment, may be conducive to progress in achieving the SDGs.

Social enterprises that are seeking significant outside investment or rapid growth, or which may not initially have a large membership group, may not find forming as a cooperative a particularly attractive option.

Since the level of financial investment in these entities does not determine control, it can be difficult to attract outside capital. Additionally, in some countries, there are membership limitations when forming a cooperative,[12] while in others, cooperatives face additional taxes or fees.[13]

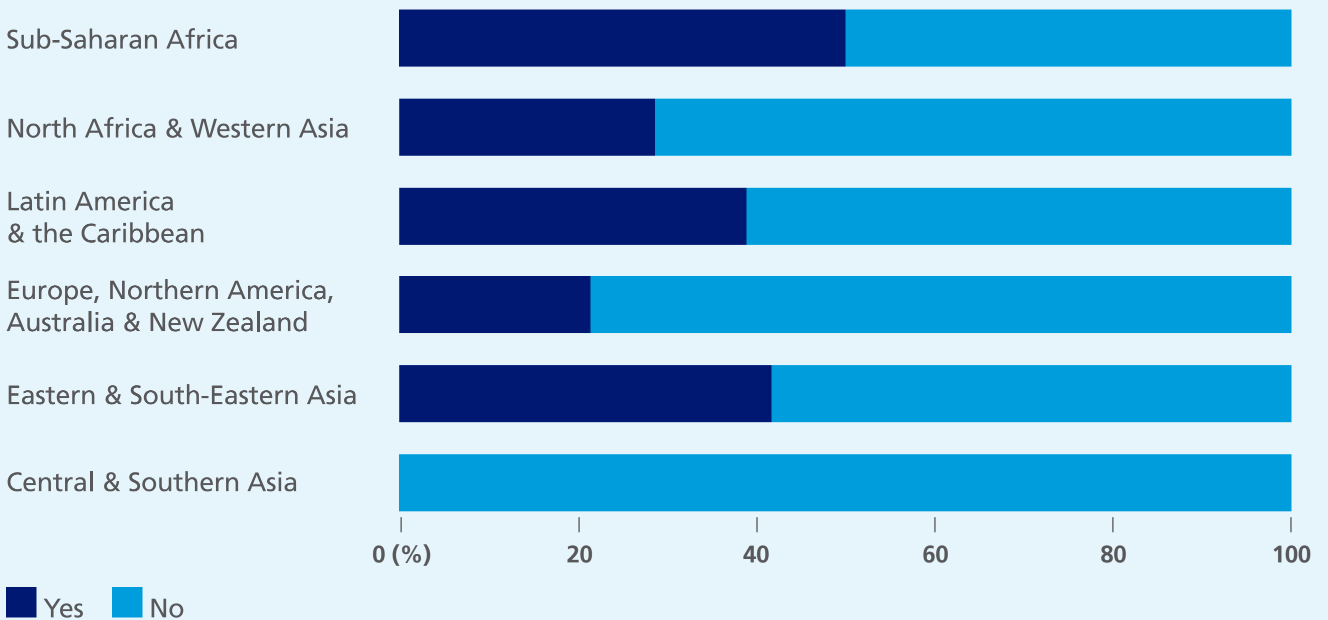
[12] For example, in Pakistan, a producer or housing Cooperative Society must have at least 50 members, while other Cooperative Societies must have at least 30 members, and the members must live in the same town or village (or in the same group of villages within a 15 kilometer radius from the registered office of the society). In addition, the federal securities laws of the United States of America limit the practicability of forming a cooperative with members resident in more than one state.

[13] In Honduras, cooperatives must pay an annual fee equal to 15% of their gross surplus as an additional tax.

To make the cooperative form more attractive generally in jurisdictions that already have them, regulators may consider amending requirements that discourage social enterprises from forming as a cooperative. For example, to address the issue of under capitalization, the Italian legislature passed a law permitting participation of financial shareholders in cooperatives, but in order to safeguard the principle of "one person, one vote," financial shareholders are limited to one-third of the voting rights.

On the other hand, jurisdictions without a cooperative enterprise form should strongly consider adoption of such a form, particularly if they have neither a Benefit Corporation form nor permit the management of a standard enterprise to consider factors beyond shareholder return.

Figure 8. Prevalence of special tax benefits for cooperative enterprises.



One way to make the cooperative form more attractive is to provide tax benefits for social enterprises that form as cooperatives. Most jurisdictions do not afford cooperative entities special tax benefits compared to regular corporate structures. Readers from jurisdictions that do not provide these benefits may wish to look to other countries in their region that do – or to countires in other regions – for guidance as to potential ways to implement tax incentives for the formation of social enterprises in cooperative form. For other advantages of providing tax incentives to social enterprises, see Section III. Tax, page 27.

iii. Social enterprise designations

As an alternative to adopting a distinct corporate form, a jurisdiction may create a social enterprise designation as an "add-on" to existing corporate forms. For example, in South Korea, enterprises can be government-certified as "social enterprises" if they limit their business activities to achieving certain specified objectives, such as providing social services or job opportunities to vulnerable social groups, have a decision-making structure that involves stakeholders, and reinvest or dispose at least two-thirds of their profits for social objectives. Being certified as a social enterprise in South Korea allows an enterprise to receive tax benefits, discussed further in Section III below, and access to preferred contracts, expanded funding channels, and business management programs that are specifically targeted at social enterprises. In Malaysia, the Social Enterprise Accreditation ("SE.A") is a national certification that recognizes legitimate social enterprises. Once certified, the social enterprises are listed on a public registry that enables customers and investors to access further information about them, they receive access to additional funding and support from the government, and they have access to a network of Malaysia's leading social enterprises, with events, networking, and other opportunities to collaborate.

Italy and the Czech Republic have similar certifications or designations for social enterprises that meet certain requirements, such as inclusion of employees and other stakeholders in decision making and a commitment to a public purpose.

Note that this would not be dissimilar to certifications and designations many jurisdictions already have in place to achieve more targeted policy objectives. For example, Mauritius has implemented a certification program, for developers of residential properties that conduct a social impact assessment and set up a social fund to provide for social amenities, community development, and other facilities to the neighborhood based on community needs identified in the assessment. In Lithuania, a special designation exists for enterprises with the specific purpose of promoting the reintegration of people whose work capacity is reduced due to disability and that submit appropriate annual materials and reports on how the enterprise plans to achieve impact and how profits and state assistance have been used to further the social enterprise's goals. Generally speaking, enterprises that met these special certifications will benefit from some kind of government grants, subsidies, tax breaks, or other financial support. In this case, the policy recommendation would be not just to implement such certifications in a targeted manner for specific policy objectives, but to adopt a certification or designation, with attendant benefits, for social enterprises more broadly.[14]

[14] This section discusses state certifications of social enterprise status or designation. For a discussion of third-party certifications as to impact, see Section V.C below.

III. Tax

In most jurisdictions, only enterprises that are organized as non-profits and subject to ongoing obligations are eligible for tax benefits. In order to encourage the formation of social enterprises and help support their growth, jurisdictions may wish to consider offering limited tax benefits to *for-profit* social enterprises as well, provided they satisfy relevant reporting and other qualifying criteria that are aligned with a country's social policies. Further, to encourage investments in such qualifying social enterprises, jurisdictions may also consider offering preferential tax treatment for investors in such enterprises.

Introduction

Potential tax benefits applicable to social enterprises include reducing or eliminating tax on social enterprises, providing tax credits for social enterprises, making contributions to social enterprises tax deductible in certain cases, and lowering tax on financial returns from investment in social enterprises, among other options. None of these mechanisms need be "all or nothing," but can apply in a scaled manner based on the size of a social enterprise or level of commitment to certain social or public purposes.

Processes and reporting for non-profits to qualify for and continue receiving tax benefits are often time consuming and restricting, and many social enterprises incorporated as non-profits voice a desire to reduce or eliminate such requirements.

It is important to note, however, that these difficulties are "a feature, not a bug": without robust qualification and reporting processes to receive tax benefits, businesses that do not have true social purposes and are not meeting standards would illegitimately receive these benefits and competitive advantage – corruption and fraud would be inevitable. Accordingly, jurisdictions may even wish to appoint a dedicated agency or task force within their tax authorities to grant and administer any tax benefits to social enterprises, whether incorporated as for-profits or non-profits, and to audit eligible social enterprises to ensure compliance and prevent potential abuse.

Allow tax benefits to for-profits

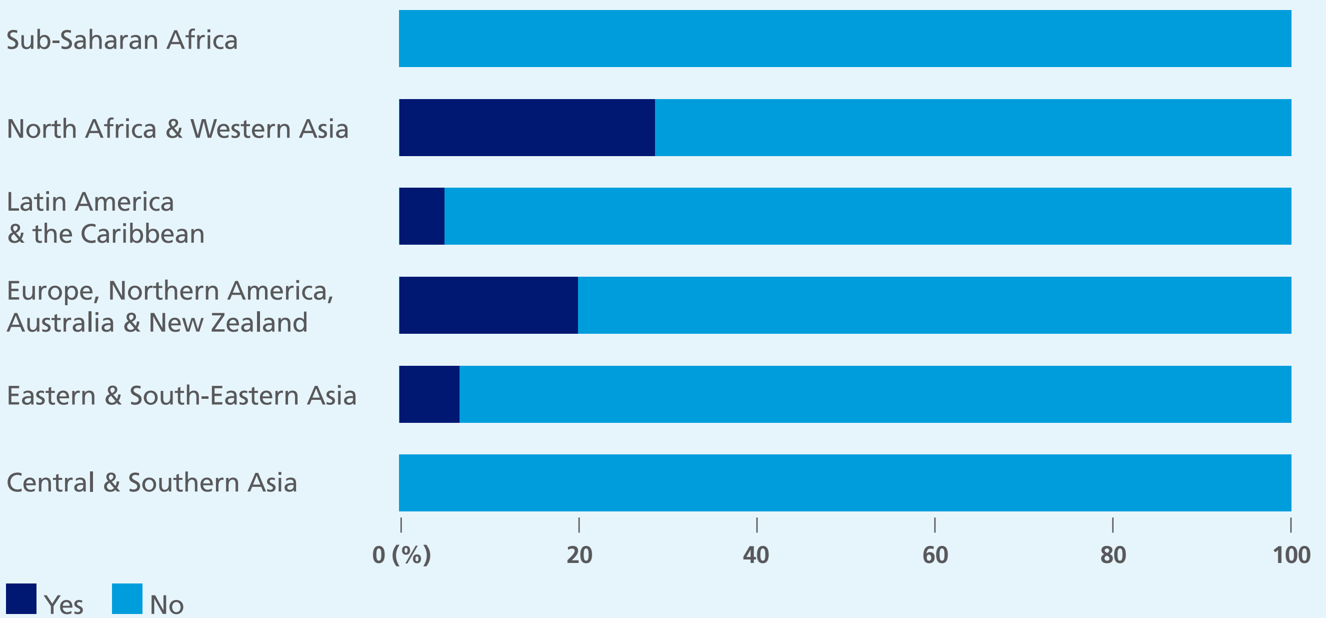
Most countries we surveyed do not have specific tax regimes for social enterprises. Social enterprises generally must choose between being organized as either:

(1) for-profit enterprises, in which case they can pursue profits but would be subject to full taxation like any other private business enterprise; or (2) non-profits, in which case they are generally prohibited from generating profits, but can qualify for various tax benefits, such as an exemption from income taxes, enhanced tax deductions for qualifying expenses, and the ability to receive donations tax-free while allowing donors limited tax deductions. As a result, social enterprises in such countries have generally opted to be non-profits.

The existing dichotomy between taxable for-profits and non-taxable non-profits unnecessarily distorts the operations of social enterprises.

Instead, policymakers should consider offering tax benefits to social enterprises based on their business model and activities, some of which could apply to social enterprises organized as for-profits, and some of which could apply to those organized as non-profits.[15]

Figure 9. Prevalence of tax benefits for for-profit social enterprises



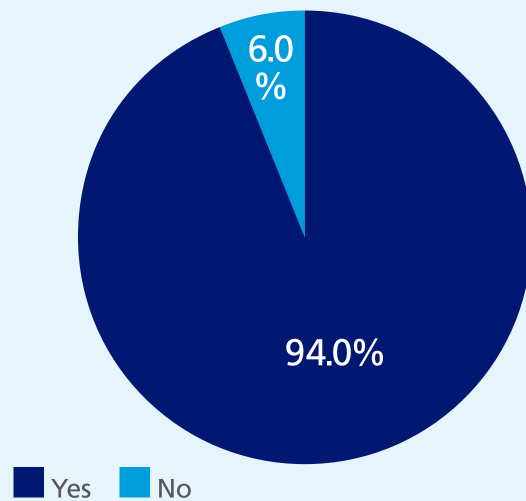
Very few countries provide specific tax benefits to social enterprises incorporated as for-profit enterprises, and no region in the world is particularly advanced in this regard. As such, this provides an area of growth for many jurisdictions.

[15] We note that many jurisdictions of course do leverage their tax codes to promote specific activities in the public interest, whether through tax credits, allowances or deductions for applicable activities. However, this approach tends to be piecemeal and "top down," rather than proscribing broad swaths of activity that may allow a qualifying business to have more general preferential tax treatment.

In either case, preferential tax treatment could be conditional on the social enterprise meeting qualifying criteria, such as performing specific business activities and incurring specified expenditures that are in line with social policies. For example, with respect to for-profit social enterprises, in South Korea, social enterprises can obtain tax exemptions/benefits if they meet various requirements qualifying them as so-called "public service companies." Such companies enjoy tax exemption on their non-profit-making activities, but can also enjoy lower taxes (e.g., income tax, property tax) on their profit-making activities in some circumstances.

With respect to non-profit social enterprises, organizations could be allowed to generate revenues from profit-making activities that are exempt from taxation below a certain threshold, as is the case in Serbia. To reduce the cash flow burden on social enterprises, jurisdictions could also exempt social enterprises from consumption-type taxes.[16] For example in Italy, value-added tax, or VAT, is not imposed on social-health services and advertising services rendered to non-profit organizations, and such organizations are, under certain conditions, also exempt from municipal property taxes on property that is exclusively used for non-commercial activities. Jurisdictions may also consider offering similar tax exemptions to reduce the advertising and other operating costs of qualifying social enterprises.

Figure 10. Prevalence of social enterprises as non-profit corporations



Nearly every jurisdiction surveyed allowed social enterprises to form as a non-profit entity. Some jurisdictions, however, offer different tax benefits based upon the non-profits chosen organizational form or area of operation (such as by electing to be a publicly utility or limiting operational activities to avoid lobbying). Policymakers could offer additional benefits to social enterprises who organize as non-profits, on top of the more blanket or indirect tax benefits provided to all non-profits.

To address concerns that tax benefits could confer an unfair advantage on social enterprises vis-à-vis their non-social enterprise counterparts, policymakers can limit the amount of such benefits in various ways. For example, countries could offer tax benefits only to "small-size" social enterprises whose market capitalization or annual revenues do not exceed prescribed amounts, or tax benefits could be limited to the first few start-up years of a social enterprise.

[16] Such as taxes on the purchase of a good or service.

Reduce or eliminate taxes on social enterprise

Most, if not all, jurisdictions already use tax incentives to promote specific industrial policies. For example, countries as diverse as Singapore, Egypt, and the United States of America offer tax incentives to corporations if they carry out projects in certain locations or in certain priority investment sectors. Besides granting preferential tax status to approved social enterprises, countries can also consider granting specific tax incentives to all businesses as long as such businesses pursue activities in specific areas that are aligned with SDGs, such as investing in clean energy and education, or if such businesses officially qualify as social enterprises.

Tax incentives can be offered in the form of: (1) reductions or exemptions from tax; (2) enhanced tax deductions or credits for qualifying expenditure; and (3) enhanced capital allowances for investing in qualifying equipment, infrastructure, or know-how. Policymakers should, however, be aware that each type of tax benefit achieves slightly different policy objectives. For example, a reduced corporate income tax generally increases the amount of after tax profits that a business would have. This has the broad advantage of increasing shareholder value and thus attracting investments, but would also have the disadvantage of giving that business an unfair advantage over other market participants.

Offering enhanced deductions and allowances may offer a more targeted approach by encouraging spending in certain areas, but such tax benefits may favor businesses operating in certain industries (e.g., R&D and manufacturing) over others (e.g., finance or service oriented industries). It is beyond the scope of this Report to comment on the merits of each type of tax benefit that can be offered, but policymakers should be aware of these market-distorting effects in formulating any tax incentives for businesses.

Tax benefits for donating to and investing in social enterprises

To encourage donations to certain charitable non-profits, many jurisdictions provide donors with income tax deductions based on their donations to such non-profits; these deductions are subject to varying limitations. For example, in Japan, a corporate donor's deductions are capped based on its annual taxable income and paid-in capital, and no deductions are allowed for donations made to related parties. Besides allowing deductions to donors, donees are also generally exempt from paying income tax on the donations, provided strict conditions are met. In Malaysia, in order for a non-profit to enjoy tax exemption on the donations they receive, the non-profit must be in operation for at least two years and must provide services or benefits to Malaysians only.

Policymakers can consider implementing similar tax deductions and tax exemptions for donations to designated "high-priority" for-profit social enterprises, provided that such social enterprises comply with reporting and accountability processes similar to those undertaken by charitable non-profits. In addition, to mitigate the unfair advantage such social enterprises would have over their private sector counterparts (as such social enterprises would be receiving donations tax-free), policymakers can impose limitations on how the donation proceeds can be used. For example, rules could provide that social enterprises may only use the donated proceeds to fund activities that are oriented toward the enterprises' social mission, otherwise such enterprises would have to pay full income tax on such donations and no deductions would be allowed to their donors.

We also recommend that policymakers encourage other forms of capital flow into social enterprises, specifically through equity and debt investments. Policymakers can do so by reducing taxes on returns from financial investments in social enterprises, as has been done in Italy.[17] For example, countries can impose lower withholding tax rates on dividends and interest paid by a social enterprise to its shareholders' and lenders.

Countries could also allow investors a tax deduction on the capital they have contributed into a social enterprise. Such lower rates and deductions could be made conditional on the social enterprise, or its shareholders meeting prescribed conditions, such as requiring a certain percentage of an enterprise's profits to be reinvested instead of being distributed to investors each year, and requiring investors to maintain their investments for a minimum period.[18] Such measures are similar to the tax incentives that some countries offer to foreign investors to encourage foreign direct investments.

Simplify tax process

Any preferential tax treatment that is afforded to social enterprises should be accompanied by a stringent and robust application process to guard against abuse. Most countries we surveyed have such processes for evaluating applications by non-profits for tax-exempt treatment, although the timelines for said process vary greatly between countries, from a few weeks to years. Policymakers should consider simplifying and expediting the application process for any preferential tax regime offered to social enterprises, as a lengthy and complicated process would discourage uptake and defeat the purposes of such regime.

[17] In Italy, there are certain tax exemptions that apply to investors investing in non-profit limited companies or partnerships that pursue certain public benefits and qualify as "social enterprises." Investors are also allowed tax deductions on a portion of the capital that they have invested into such qualifying entities if they maintain their investments for five years.

[18] For example, in Liechtenstein, in order for certain for-profit corporate entities that pursue public benefits to be exempt from income tax, they have to introduce profit caps towards their investors.

For example, in one surveyed jurisdiction, there are specific tax exemptions available for social enterprises, but the process for obtaining those exemptions is so complex that many social enterprises do not understand what is required and so never start the process. While it is understandable that in order to receive tax exemptions, diligence must be completed and certain conditions must be met, the process should not be so complex and/or time consuming that social enterprises are discouraged from doing it.

Alternatively, policymakers could offer an expedited application process that would result in fewer tax benefits. For example, a jurisdiction could provide a shorter application form with faster review for enterprises that are applying for tax benefits during a prescribed number of “start up” years, or that are applying for a one-time tax credit. A more robust application process can be reserved for enterprises that wish to obtain an exemption from income taxes entirely. This simplified application process could operate in tandem with the regular application process, and enterprises could apply for limited tax benefits while they await approval of their application for full tax benefits.

Reporting

To ensure accountability under any preferential tax regime, social enterprises incorporated as for-profit entities should be required to demonstrate that their activities are aligned with the goals of the relevant tax regime, for instance, through annual reporting requirements that, for organizations of a certain size, receive independent review or audit. Such reporting requirements are not dissimilar to the reporting rules that are already in place for charities and non-profits, which are generally subject to robust monitoring, potential tax audits by the relevant authorities and mandatory annual third-party audits for larger organizations.

Reporting generally involves providing information about the activities undertaken by the entity during the reporting period and the level of reporting that is required often correlates to the size of entity. So, for example, in Italy, social enterprises that are so-called “third sector” entities (i.e., operating in specific sectors such as health services, environmental safeguarding, scientific research, or humanitarian aid) with revenues greater than €1 million per year must publish and file their social report with the national register of the third sector, in addition to publication on their website.

In the Czech Republic, large public-interest enterprises (with >500 employees) must include in their annual report, or in a separate report, non-financial information on environmental and social matters, respect for human rights and efforts against corruption and bribery. In Slovakia, all registered social enterprises are required to prepare annual reports assessing the achievement of the positive social impact listed in its formation documents.

In addition, social enterprises that fail to satisfy the requisite reporting requirements should be subject to fines, penalties, or clawbacks on the tax benefits. For example, if a social enterprise has claimed a 0% tax rate on income for a particular year but fails to substantiate such claims through adequate reporting, it should be subject to a clawback for the unpaid taxes, with interest.

IV. Funding

One of the primary difficulties facing enterprises is the lack of funding. This is exacerbated for social enterprises, where as a result of perception or business reality, many traditional private funding sources are wary of investment. Indeed, while many social enterprises can be just as attractive to investors focused solely on financial returns, some types of social enterprise require "concessionary" capital to achieve their goals.[19]

Introduction

The current sources of funding for social enterprises consist mainly of private investments, with limited government funding and grants available in some jurisdictions. Many jurisdictions surveyed had grants and funding available for small businesses and non-profits generally, but very few had dedicated grants or funding targeted at social enterprises. To stimulate the growth of social enterprises, policymakers should adopt policies that encourage private investment in social enterprises. Jurisdictions should also provide government funding sources to provide social enterprises an alternative to private funding.

ESG considerations in investing

ESG can be a useful tool in evaluating potential investment risks and opportunities. Studies have shown that investors incorporating ESG in their investment analysis are rewarded with higher rates of return.[20] However, despite the benefits of an ESG framework in an investment analysis, very few of the jurisdictions surveyed had mandatory requirements for investor classes to consider ESG factors in their investment decisions. Given social enterprises are likely to be perceived favorably when viewed from an ESG perspective, we believe it is important for policymakers to consider promotion of ESG factors in investment decisions by fund managers in order to help support the development of social enterprises more broadly.

[19] "Concessionary capital" refers to investments that sacrifice the potential for some financial returns – for example, by providing early-stage investment in riskier businesses, agreeing to below market investment terms, or agreeing to equity or debt positions that sit junior to other, non-concessionary investors – in order to help a social enterprise secure financing and entice other investors to follow suit.

[20] *See, e.g.,* Morgan Stanley Institute for Sustainable Investing, *Sustainable Funds Outperform Peers in 2020 During Coronavirus* (Feb. 24, 2021), https://www.morganstanley.com/ideas/esg-funds-outperform-peers-coronavirus; Gunnar Friede, Timo Busch & Alexander Bassen (2015) ESG and financial performance: aggregated evidence from more than 2000 empirical studies, Journal of Sustainable Finance & Investment, 5:4, 210-233, DOI: 10.1080/20430795.2015.1118917, https://doi.org/10.1080/20430795.2015.1118917; NYU Stern Center for Sustainable Business, *ESG and Financial Performance*, https://www.stern.nyu.edu/experience-stern/about/departments-centers-initiatives/centers-of-research/center-sustainable-business/research/research-initiatives/esg-and-financial-performance

i. Promote ESG consideration in investment decisions

It is generally understood that the primary objective of an investment is to maximize long term returns for its investors. This is particularly true for some of the world's largest investment platforms, pension funds, which are intended to provide for the retirement security of workers. Accordingly, most regulated investment funds, including pension funds, are subject to rules that obligate their managers, or fiduciaries, to choose investments consistent with this intent. This raises the important question of where ESG and the SDGs can fit into this framework, as opening up pension fund capital for social enterprises could provide the necessary financing to assist in their growth and proliferation.

From a theoretical perspective, ESG may play into investing in two primary ways. First, ESG may be a useful tool in evaluating potential risks and opportunities that could materially impact the potential to achieve strong financial returns. In recognition of this, EU Regulation 2019/2088 requires managers of funds to develop policies on the integration of sustainability risks into their investment processes. Second, ESG may be a driver behind "impact investing," in which investment strategies are based on an investor's specific priorities with respect to various factors often relevant to the SDGs. These investments may emphasize impact over returns ("impact first"), emphasize returns over impact ("return first"), or evaluate impact and returns equally.

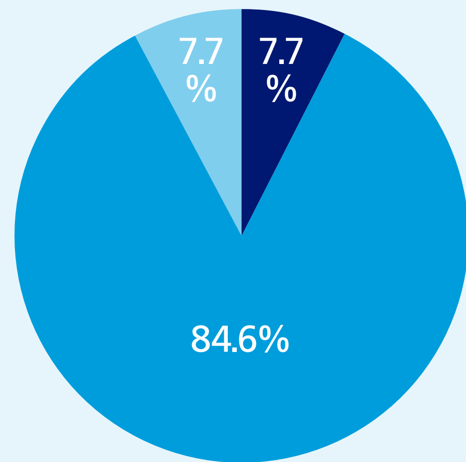
From a practical perspective, investors, both impact funds and "traditional" return first funds, can have ESG considerations play a role throughout the entire investment process - from initial deal selection and diligence, to negotiated information and reporting rights, and, finally, the investor's management of, and interaction with, the investor's portfolio companies.

The state of the law worldwide is not very advanced in considering either theoretical approach to ESG in investing. No surveyed jurisdiction had a direct requirement, whether mandatory or otherwise, for all investor classes to consider ESG factors when making investment decisions. However, most jurisdictions surveyed allowed for ESG to be considered, either equally or secondarily with return on investment. In some countries, such as Honduras and Japan, the regulators acknowledge and encourage investors to consider ESG factors when making investments, but there are no negative consequences for investors if they choose not to do so. In Iceland and the Netherlands, pension funds are required to establish ethical standards in their investments. Mexico has also recently passed a law that will become operational in 2022 requiring pension fund investment companies to consider ESG in their investments.

In other jurisdictions, such as Bangladesh, Luxembourg or Turkey, certain investment funds would be required to consider ESG, but only to the extent that they had elected to do so in their organizational documents.[21]

In other jurisdictions, the legal regime may actively discourage investors from prioritizing ESG in investments, or at least may be less than clear on the issue. For example, the United States Department of Labor has issued a final rule that prevents pension plan managers from investing based on ESG if the investment strategy would "subordinate return or increase risk for the purpose of non-financial objectives," although they would allow pension fund fiduciaries to consider ESG as part of their framework for assessing an investment's potential risk and return profile. However, as of March 2021, the U.S. Department of Labor issued a statement that they would not enforce the final rule or pursue enforcement actions against any plan fiduciary based on a failure to comply with the rule, until further guidance is published.[22]

Figure 11. Ability of regulated funds to balance ESG with ROI



- Investment funds must consider ESG in their investment decisions
- Investors may consider ESG in their investment decisions
- Investors may not consider ESG at all in their investment decisions

Only a few jurisdictions surveyed affirmatively require managers of certain classes of regulated pension or investment funds to consider ESG in their investments alongside return on investment. On the other hand, most jurisdictions surveyed allow for pension fund managers to consider public or social benefits alongside returns on investments when making investment decisions. We strongly encourage policymakers in the minority of jurisdictions that do not permit fund managers to consider public or social benefits, or where the law is unclear, to reconsider approach in this area.

[21] In Bangladesh, the fund manager for "impact funds", a subset "alternative investment funds", is required to disclose material risks, which must include ESG risks, and how they are managed at the fund and portfolio company levels in the annual report of the fund. In Turkey, whether investment funds must consider ESG is governed by their bylaws. Certain funds, such as sustainability pension funds generally require ESG consideration in their bylaws.

[22] As of October 2021, the United States Department of Labor issued proposed regulations that would reverse the earlier rule and permit employer-sponsored pension plan fiduciaries to consider ESG factors when they make investment decisions. The proposed regulation would not allow fiduciaries to sacrifice investment returns or take on additional investment risk in pursuit of non-financial public benefits; however, it expressly permits consideration of the financial risks and impacts associated with climate change and other ESG factors. The proposed rule also permits consideration of climate or ESG benefits as a tie-breaker in making investment decisions.

Governments should strongly consider encouraging, or at least explicitly permitting, pension fund managers to consider ESG considerations when making investment decisions. Further, consideration of ESG should not be discouraged if consistent with driving return.

We believe that fund managers should have the ability to leverage all tools at their disposal to achieve their objectives. Accordingly, governments should strongly consider encouraging, or at least explicitly permitting, pension fund managers to consider ESG considerations when making investment decisions. Further, consideration of ESG should not be discouraged if consistent with driving return. Thus, governments should consider clarifying in their guidance the distinctions between "impact first" and "return first" impact investing, and expressly permitting the latter, perhaps coupling such permission with the requirement to publicly disclose the particular ESG focus and to report on results.

ii. Educating the market

Despite evidence that investment firms focused on ESG factors tend to outperform the market, the belief persists that a focus on ESG negatively affects return.

For example, in Japan, many respondents to a Bank of Japan report published in July 2020 cited that it is difficult to see the relationship between ESG factors and monetary returns. Additionally, they also noted the risk that impact investments might be affected by various uncertainties concerning politics, science and technology, climate change, etc.

Governments seeking to promote ESG consideration in investment decisions may first wish to dedicate resources to educating the market on the benefits of focusing, or at least including, such considerations. For example, some countries, including Egypt and South Korea, have published guides and stewardship codes to educate investors on the tangible and financial benefits of incorporating ESG considerations in investment strategies. These types of publications could potentially dispel the myth that profit maximization and ESG considerations are mutually exclusive.

Countries looking to support the development of social enterprises may also consider creating new financial instruments focused on ESG factors that address specific needs within their jurisdiction. Possible financial instruments include green bonds and social impact bonds. These bonds encourage the creation of social enterprises by allowing companies to raise funds for ESG related activities and require that some portion of such funds be used for sustainability or social impact purposes, as applicable.

Guidelines for such bonds may be outlined in a guidebook or framework like the Argentine Securities Exchange Commission's "Guidelines for the Issuance of Social Negotiable Securities, Green and Sustainable" or the Malaysian Securities Commission's Sustainable Responsible Investment Sukuk framework. Holding competitions in which social enterprises may vie for grants may be helpful in educating the market on the existence of social enterprises and the benefits of including ESG considerations in investment strategies. In some jurisdictions, such as Malaysia, various grant making organizations hold competitions for social enterprises to receive grants.[23] These government-sponsored competitions bring awareness to the market and provide funding to social enterprises, which, as discussed in this report, may struggle to access financing.

Government grants & funding

Grant making is of particular importance for social enterprises, both because traditional investment monies may not be available for the reasons discussed earlier in this section, and because governments are often funding programs to achieve the SDGs. Thus, one way to help support social enterprises is to make grants more available and easier to obtain.

Many jurisdictions surveyed had grants and funding available for small businesses and non-profits generally, but few jurisdictions had dedicated grants and funding for social enterprises specifically. Poland, for example, created social enterprise support centers which distribute funds from the European Social Fund in the form of subsidies and loans to promote social enterprise job creation. Singapore, through a collaboration between the public and private sectors, created the Centre for Social Enterprise, raiSE, which offers grants to support new and existing social enterprises that are beginning or expanding operations.

A number of jurisdictions also had funding programs available to enterprises in specific industries (such as agriculture or healthcare). In order to help social enterprises grow and scale, jurisdictions could consider adopting grant and funding programs that are intended to benefit social enterprises specifically, rather than small businesses generally. In jurisdictions with funding limitations, officials could work to create a centralized database, such as that available from the United Kingdom,[24] or search tool, such as that available in Japan,[25] that social enterprises could use to research whether there are any government funding programs available to them based on their size or the industry in which they operate.

[23] Including, for example, the AirAsia Foundation, the British Council & Arthur Guinness Fund's Entrepreneurs for Good, the myHarapan Social Business Challenge and the Agensi Inovasi Malaysia's Berdubi Berganda Challenge.

[24] In early 2021, there were 173 loan schemes and grants located on the United Kingdom government websites.

[25] Japan has a number of government funding programs that are available through various government ministries such as the Ministry of Education, Culture, Sports, Science and Technology, the Ministry of the Environment, and the Ministry of Economy, Trade and Industry. A social enterprise can research whether there are any suitable government funding programs by using a search tool on the Cabinet Office website that is available at https://www.npo-homepage.go.jp/policy-portal/

A centralized database or search tool would also help social enterprises navigate funding programs in countries where there are a number of government grants or funding programs that are aimed at enterprises using a specific enterprise form or operating in a specific industry.

Securities regulation & crowdfunding

Securities regulations serve to protect the interests of non-sophisticated investors by imposing requirements, obligations, and thresholds for the security issuers. However, strict securities regulations may also hinder the ability of social enterprises to raise funds from the public. As a result, jurisdictions should consider whether their securities regulations serve as excessive obstacles for social enterprises to access necessary funding, whether new laws concerning crowdfunding go far enough in enabling access, and whether different standards should be applied to fundraising by social enterprises.

Crowdfunding was originally touted as a potential breakthrough in the ability of smaller enterprises to get funding. However, many jurisdictions that have adopted such statutes, like the United States of America, Malaysia, and South Korea, limiting how much a project (including a social enterprise) may receive from crowdfunding.

On the one hand, lifting caps on crowdfunding for social enterprises would be an effective way to increase the funds available for social enterprises. On the other, it may expose investors, who may not have the requisite experience to adequately assess the risks of the investment, to losses that they are unable to bear. Jurisdictions may therefore wish to consider easing such limits solely for certain "qualified" social enterprises, whatever those qualifications may be – for example, having financial success (which would reduce concerns over protecting investors) or having a substantial reported impact certified by a third party.

Other securities regulations may adversely impact social enterprises more indirectly by imposing requirements on the crowdfunding process. Japan, Liechtenstein, and Germany all impose licensing requirements on crowdfunding, thus making it difficult, if not impossible, for a social enterprise to meet such requirements on its own. In turn, such platforms may have onerous reporting requirements (such as in Japan), which are disproportionately burdensome for social enterprises.

V. Publicly traded social enterprises

While most social enterprises are not public companies, some are. While these companies may not need the support of the policies and programs discussed elsewhere in this report, they are important to consider not just because they may be eligible for such benefits, but because their ability to influence and set standards will impact smaller social enterprises.

Introduction

Public companies, generally speaking, are enterprises with wide shareholder bases and revenues, assets or prospects of sufficient magnitude to support market capitalizations ranging from the tens of millions to hundreds of billions of dollars. Their securities usually trade on public exchanges, and they are usually also required to regularly disclose certain business and financial information to their shareholders if not the public at large.

Public companies tend to be regulated both by government agencies and stock exchanges or other securities regulators. For example, in the United States of America, public companies must adhere to rules set by the Securities Exchange Commission, a government agency, and those established by the public exchanges that facilitate securities trading, typically either New York Stock Exchange or the NASDAQ Stock Market LLC. Exchanges are themselves often quasi governmental organizations, or are regulated by government agencies.

As of the date of this Report, thirteen public companies traded on the U.S. national stock exchanges are incorporated as Delaware public benefit corporations (see Section II.C.1), including nine operating companies that commenced their initial public offerings as Delaware public benefit corporations, one that filed for a direct listing as a public benefit corporation, one that converted to the novel form after submitting a proposal for and receiving shareholder approval, and even one special purpose acquisition company. All but one of these companies completed their initial public offering or conversion within 15 months of the date of this Report. We expect to see this trend continue, as investors become more familiar with the new corporate form, as pressures related to ESG mount and as companies formed after the adoption of the new form in 2013 begin to grow large enough to support an initial public offering.

Of course thirteen is a small number compared to the thousands of public companies in the United States of America alone. Yet, it is not just the thirteen Delaware public benefit corporations that are focusing on ESG and impact.

Indeed, investors are increasingly demanding reliable information on climate change and other ESG-related issues upon which to make educated investment and voting decisions. Financial institutions responsible for $150 trillion of assets have voiced support for the recommendations of the Task Force on Climate-Related Financial Disclosure calling for climate-related financial disclosures by companies for investors, lenders, and other stakeholders.[26] In addition, investors with approximately $100 trillion of assets under management have signed on to the United Nations-backed Principles for Responsible Investment whereby they have committed to incorporating ESG criteria into their investment analyses.[27] Many companies have responded to this call for information on climate change and other ESG-related issues by voluntarily providing such disclosures in their public securities filings.

While the majority of this Report focuses on issues that are relevant to smaller scale social enterprises, it is important to consider issues related to publicly companies for several reasons. Smaller scale social enterprises may eventually grow large enough to become publicly traded themselves, and we believe it is important to foster the long-term success of all social enterprises, particularly ones whose potential for impact will only scale with the growth in their operations.

In addition, policies applicable to and programs available to social enterprises generally may also be available for publicly traded social enterprises, and it bears consideration whether public companies should be treated any differently. Further, public companies, whether or not social enterprises, will likely have the resources to set the standard for disclosure and best practices related to any such policies and programs, which will impact smaller scale social enterprises.

Standards setting

The joint role stock exchanges and government agencies play in regulating public companies can be used to promote the implementation ESG-related standards through several approaches. For example, regulators can simply mandate standards applicable to public companies – in other words, a public company must take certain actions or adhere to certain standards that do not apply to their private counterparts. Alternatively, regulators can impose a "comply or explain" framework, in which actions or standards are not mandatory, but companies must explain why they have chosen not to implement them.

[26] *See, e.g.,* Timothy Massad, *The SEC Needs to Catch Up on Sustainability*, BLOOMBERG (Jan. 27, 2021), https://www.bloomberg.com/opinion/articles/2021-01-27/sec-s-gensler-must-decide-on-new-esg-disclosure-rules; TCFD, *Recommendations of the Task Force on Climate-Related Financial Disclosures: Final Report* (June 2017), https://assets.bbhub.io/company/sites/60/2020/10/FINAL-2017-TCFD-Report-11052018.pdf

[26] *See,* Mark S. Bergman, ESG Disclosures: *Frameworks and Standards Developed by Intergovernmental and Non-Governmental Organizations*, HARV. L. SCH. F. ON CORP. GOVERNANCE AND FIN. REG. (Sept. 21, 2020), https://corpgov.law.harvard.edu/2020/09/21/esg-disclosures-frameworks-and-standards-developed-by-intergovernmental-and-non-governmental-organizations/

Either approach, however, presents difficult questions. Should securities regulators be in the business of telling public companies how they should operate? Should standards apply differently as between public companies that are social enterprises or incorporated under Benefit forms, compared to other public companies? If so, would this not burden publicly traded social enterprises compared to their non-social enterprise counterparts? If not, is it an overreach to impose value-based requirements on public companies generally?

We do not propose to answer these questions here. Instead, we suggest that regulators seeking to promote social enterprises and the achievement of the SDGs through regulation of public companies focus on disclosure standards.

Disclosure requirements

Much, if not most, regulation of public companies comes through disclosure requirements. Public companies make regular, publicly accessible filings with regulators containing material information regarding a company, its business, its results of operations, its governance, and other factors, in order to permit investors to make decisions regarding investing in a company's shares and voting at shareholder meetings. The disclosures in these and other filings and elsewhere, including on a company's website, can be mandated by regulators or can be disclosed voluntarily by the company.

It has long been the policy of regulators to promote good corporate behavior by requiring disclosure not just of financial information, but other information that investors find material. For example, the U.S. securities laws require disclosures regarding human capital management, executive compensation, and CEO-to-average employee pay ratios in order to promote better behavior by public companies relevant to the social and governance prongs of the ESG framework, and disclosure regarding mine safety and health to encourage companies to be more mindful of factors relevant to the environmental and social prongs of the ESG framework.

ESG-related disclosure increases investor and competitor visibility into such activities and offers financing and competitive advantages to companies that perform better from an ESG perspective. Thus, some regulators are now more directly encouraging ESG-related progress through ESG-related disclosures. The Pakistani government, for example, requires all public companies to provide descriptive as well as financial disclosures related to corporate social responsibility.

To comply with this requirement, public companies in Pakistan must disclose ESG related factors relevant to their business, including environmental protection measures taken, community investment activities, and corporate spending on disadvantaged groups.

Also, in Morocco, companies listed on the Casablanca stock exchange must include an ESG section in their annual report, detailing its strategy and specific steps implemented to achieve ESG goals.

ESG requirements are also required under EU Regulations: insurance companies, companies with undertakings designated by law as being of the public interest and public limited liability companies with an average of over 500 employees per year must submit a non-financial declaration addressing the effects of the company's activities on the environment (including addressing climate-related risks and opportunities) and on employees and society. They must also disclose their observance of human rights and anti-corruption and anti-bribery measures. Finally, they must relate these non-financial performance indicators to the information disclosed in the financial statements.[28]

In addition to, or instead of, mandating ESG-related disclosures from public companies, regulators can require ESG-related disclosures by asset managers.

In March 2021, in a bid to fight "greenwashing"[29] and to promote investment in sustainable business, the EU Commission introduced a Sustainable Finance Disclosure Regulation targeted at "financial market participants" ("FMPs"), which include managers of mutual funds, pensions, and other investment products. Broadly, the regulation requires covered FMPs to make disclosures regarding ESG impact at both the product level and the entity level. FMPs that consider the "principal adverse effects" of their investment products must report how they consider such effects, while FMPs that do not consider the ESG impact of their investment products must also disclose this information.

Instead of imposing mandatory disclosures, other regulators are publishing guidance promoting voluntary disclosure on certain matters. For example, in Japan, publication of the Tokyo Stock Exchange's "ESG Information Disclosure Practice Handbook" resulted in an increase in ESG-related disclosure and an improvement in descriptiveness and specificity of the disclosed information. The Egyptian Exchange saw a similar result following publication of its ESG guide.

[28] *See* European Union (Disclosure of Non-Financial and Diversity Information by certain large undertakings and groups) Regulations 2017, S.I. No. 360 of 2017.

[29] "Greenwashing" refers to the use of marketing claims or statements that deceive or mislead consumers as to the environmental benefits or attributes of a product or service, or, more broadly, as to an enterprise's environmental practices as a whole.

In addition, we note that staff of the U.S. Securities and Exchange Commission on March 15, 2021 issued a request for public input on climate change and ESG-related disclosures for public companies as that agency considers potential changes to the law, and many constituencies have submitted responses, including the Sustainable Accounting Standards Board ("SASB"), which advocates for universal climate and ESG reporting standards for public companies around the world, and our law firm, in which we recommend that regulators take a measured approach to adopting rules and issuing guidance around climate and ESG disclosures that is built upon and consistent with existing securities law frameworks.[30]

We direct you to Section VI of this Report for further discussion regarding what ESG related reporting and disclosure standards may be advisable specifically.

Other benefits for publicly traded social enterprises

The other sections of this Report discuss in detail policies and programs that can be implemented to promote social enterprise generally. In adopting any such measures, regulators should consider, on a case-by-case basis, whether they should be available to publicly traded social enterprises. If they do, it will be all the more important to establish standards by which a company can qualify for the benefits—to have not only a clear definition of what counts as an eligible social enterprise, but also reporting requirements to ensure that a company continues to satisfy substantive requirements for the beneficial treatment. If not, it will be all too easy for public companies that are not truly concerned with impact, ESG, the SDGs, and similar factors to take advantage of programs not intended for their benefit, to the detriment of actual social enterprises and the integrity of any social enterprise-focused reforms.

[30] *See* SASB SEC Climate Letter, dated May 19, 2021, https://www.sasb.org/wp-content/uploads/2021/05/SASB_SEC_Climate_Letter_2021-05-19_FINAL.pdf, and Morrison & Foerster's SEC Climate Letter, dated June 11, 2021, https://www.sec.gov/comments/climate-disclosure/cll12-8911364-244302.pdf

VI. Impact reporting & third-party certifications

Impact reporting is the process by which social enterprises measure and record the impact they are having on society or the environment. While impact reporting can be a difficult, time consuming and costly process, the value it provides is unquestionable. Robust reporting procedures enable social enterprises to monitor their impact, which in turn enables them to set ambitious goals and improve their impact year over year. Reporting is also a valuable resource for investors and donors in social enterprises.

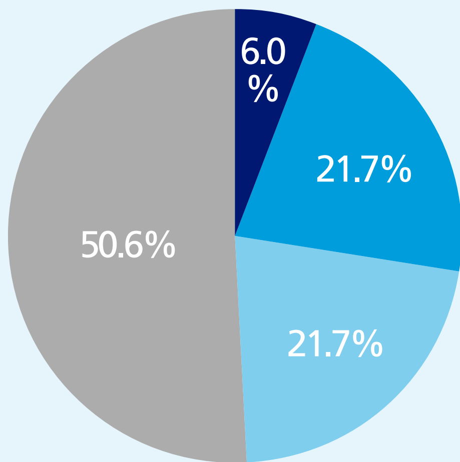
Introduction

With respect to private or public social enterprises and for-profit or non-profit social enterprises, investors and donors need to be able to monitor how their capital is being utilized and to confirm the impact it is having. Furthermore, reporting – especially reporting coupled with independent third-party audit – is fundamental to preventing "greenwashing," the process by which corporations exaggerate their impact through puffery and spin. With the vast increase in focus on ESG topics, particularly in recent years, concerns around greenwashing have also increased. In order to verify the accuracy of statements and claims made by social enterprises with respect to their impact, accurate reporting is critical.

Unlike with financial reporting, where businesses around the world may apply International Financial Reporting Standards ("IFRS") and may be certified by independent accounting firms registered with and regulated by government agencies, there are no generic impact reporting standards that can be consistently applied across different markets or jurisdictions, and no certifying agencies that are consistently regulated around the world. Not surprisingly, then, impact reporting and certification for social enterprises varies hugely, from those countries where there are no ESG-or impact-focused reporting requirements at all for social enterprises, regardless of what form they take, to those where ESG and impact reporting requirements are tied to the corporate form chosen (that is, whether they incorporate as Benefit corporations or non-profit), to those where are ESG reporting requirements apply only for large enterprises, such as Norway.[31]

[31] In Norway, large enterprises are required to present their policy on the integration of considerations relating to human rights, employee rights, social matters, the external environment and corruption prevention in their business strategy, daily operations, and stakeholder relations. Further, the large enterprises must also explain how this policy is reflected in their actions and provide an assessment of what has been achieved and expected future achievements. Finally, enterprises listed on the Oslo Stock Exchange and Euronext Expand are required to report on the foregoing issues.

Figure 12. Prevalance of mandatory ESG/impact reporting requirements



- Yes, for all social enterprises
- Only for publicly listed companies or companies meeting a certain size requirement
- Only for social enterprises formed using specific enterprise forms
- No mandatory ESG or other impact reporting requirements

Given few jurisdictions have a clear definition of "social enterprise," it is not surprising that only four jurisdictions surveyed had mandatory ESG reporting requirements for all social enterprises. However, many jurisdictions do have mandatory ESG reporting requirements either for publicly listed companies or for companies incorporated under specific social enterprise forms (see Section VI.B). Interestingly, not all jurisdictions that may have special corporate enterprise forms may wish to require specific ESG reporting under them, as some jurisdictions may choose to allow flexibility in how shareholders of such enterprises monitor performance.

Impact reporting

The question of what form of impact reporting should be required for social enterprises, or even enterprises generally, is complex, with many differing points of view, even when the agreed goal is to promote social enterprise.

The first concern is whether reporting should be mandated at all, for social enterprises or generally, and if so, in what form. One approach is to focus on social enterprises or companies adopting a social enterprise form specifically. Interestingly, in the United States of America, California's benefit corporation ("BC") and Delaware's public benefit corporation ("PBC") provide examples of similar, but different stances on this point. In California, the BC must publish an annual report that assesses an enterprise's performance against an independent third-party standard selected by the board of directors of the BC. In Delaware, the PBC is not required to access its performance against a third-party standard, but must publish a report every three years that provides the shareholder's with a statement of the enterprise's overall social and environmental performance and of the best interests of those materially affected by the enterprise's conduct.

Another approach is to focus on businesses generally, but only require reporting for the larger businesses. For example, in Malaysia, all companies listed in the Main Market, the Malaysian market place for companies to list their shares for trading, are required to include a sustainability statement when submitting their annual reports. This sustainability statement is a narrative statement of the company's management on material economic, environment, social risks, and opportunities. It allows investors who are interested in ESG considerations to understand more about how a company is addressing these concerns. A sustainability statement is something that could easily be incorporated into a country's existing reporting standards for social enterprises and also for corporations generally.

While impact reporting is important for transparency and confirmation that the social enterprises are pursuing a public mission, it is also important for the impact reports to be credible and have comparable data. Consistent with many public commentators on the issue, many survey respondents noted that this can be best achieved if there are uniform standards to assess the performance of social enterprises, whether they are for-profit or non-profit.

It is important to ensure that reporting requirements be tailored to the type of social enterprise and should be scalable depending on the enterprise's size and revenue.

To that end, the Global Impact Investing Network ("GIIN") has developed Impact Reporting and Investing Standards ("IRIS") which are intended to help standardize the process of measuring and reporting impact with a set of generally accepted performance metrics. Incorporating these standards into the reporting requirements for social enterprises could be one way to access a more global investor base.

Whatever approach is taken, we believe it is important to ensure that reporting requirements be tailored to the type of social enterprise and should be scalable depending on the enterprise's size and revenue. The publicly traded company reporting requirements noted above and also discussed in Section V.C would clearly be onerous if imposed on small companies with fewer resources. Unfortunately, no jurisdictions surveyed had impact reporting requirements for all social enterprises that varied depending on the enterprise's size and revenue.

Third-party impact certification

In addition to standardized impact reporting, certifications of impact can also be an extremely important tool to provide credibility to social enterprises. Some countries have set up national certification schemes specifically for social enterprises. The credibility provided by certification can allow social enterprises access to greater resources and capital.[32]

Perhaps the most famous certification for social enterprises is the B Corporation Certification. This certification is now being used globally (including the United States, the UK, Italy, and Ecuador) and is provided by B Labs, a non-profit organization, for those organizations which meet B Labs' standards of verified social and environmental performance, public transparency and legal accountability to balance profit and purpose.[33] There are currently over 3,500 B Corporations across more than 50 countries globally. To become a B Corporation, the enterprise must take and pass an impact assessment, incorporate certain provisions in its charter and governance documents (although this requirement of the license agreement is often waived), comply with ongoing reporting requirements and pay certain fees to license the "B Corp" mark.

While the promotion of the B Corporation standard around the world is a good start, B Labs' lack of independent (or in many cases any) required audit function with respect to ESG standards or impact may exacerbates the risk of "greenwashing" as companies evaluate themselves and pay for the privilege of being a "B Corporation". Further, while this is a useful certification for for-profit organizations, in many countries social enterprises must be incorporated as non-profits. A similar certification (with third-party audit requirement) applicable to non-profits could be extremely useful.

As with impact reports, the value derived from certifications is enhanced when they are uniform and comparable. Also as with impact reporting requirements, certification standards should be flexible and scalable depending on an enterprise's size and revenues. Unfortunately, the current certification schemes, based on the survey responses, are largely one-size-fits-all, which we fear may disproportionately burden small and mid-sized enterprises. Without flexibility, social enterprises without sufficient resources to achieve and maintain certification may be unable to derive the benefits from their social enterprise status, regardless of their positive impact.

[32] This section discusses third-party certifications as to impact. For a discussion of state certifications of social enterprise status or designation, see Section II.C.3 above.
[33] https://bcorporation.uk/about-b-corps

VII. Governmental infrastructure

Although many jurisdictions have governmental infrastructure and programs tailored specifically to, and reserved for, small and medium-sized enterprises ("SME"), few jurisdictions have such programs and infrastructure tailored specifically for social enterprises. Some social enterprises may be eligible to take advantage of the programs and administrations created for SMEs, but other social enterprises will not qualify. Additionally, social enterprises may have needs that can be better served by an organization or program designed specifically for them, rather than one SMEs generally.

Government agencies

Only four of the surveyed jurisdictions, New Zealand; Lebanon; Singapore; and Thailand, reported having a dedicated administrations or organizations for social enterprises. The government of New Zealand partnered with the Akina Foundation in forming The Impact Initiative, which focusses on "building the overall conditions for a thriving Social Enterprise sector in Aotearoa, New Zealand." The Initiative focuses on capacity building, impact, finance and legal barriers, and social procurement to help Social Enterprises thrive. To date, the Initiative has been effective in identifying key areas where New Zealand's legal landscape needs to adjust to better account for social enterprises. With the key areas now identified, the Initiative's next phase is creating the changes that would help social enterprises thrive, based on the research they conducted.

Singapore's Centre for Social Enterprise offers advisory services, programs, training, resources, and grants to new and existing social enterprises. In Thailand, the Office of Social Enterprise Promotion issues registration and certification to, and also advises, trains, and promotes, social enterprises.

While few surveyed jurisdictions may have social enterprise-specific administrations, many have administrations for SMEs. For example, the Small Business Administration in the United States of America is a cabinet-level federal agency dedicated to small businesses and provides counseling, capital, and contracting expertise. In Japan, there is also the Small and Medium Enterprise Agency, an external bureau of the Ministry of Economy, Trade, and Industry. Malaysia has the SME Corporation Malaysia, which serves as the central coordinating agency under the Ministry of Entrepreneur Development and Cooperatives.

This finding is important for two reasons. First, many social enterprises may take advantage of SME administration programs. Second, SME administrators may present a model for how social enterprise administrators could be established.

The roles and responsibilities of these government agencies differ from country to country. Japan's Small and Medium Enterprise Agency plays a more active role in helping SMEs. It actively promotes the potential of small enterprises, supports the starting up of small businesses, advises on startup preparation, assists business innovation in financing, handling taxes and cultivating markets, and provides financial support in the event of natural disasters or pandemic outbreaks. At the same time, SME Corporation Malaysia coordinates the implementation of development programs for SMEs and runs financing programs to help startups raise funds. Slovenia has business incubators, entrepreneurial accelerators, and technology parks where new enterprises, co-founded and co-financed by the state, can develop. Angola runs an incubator for small and medium business enterprises that provides economic stimulus, as well as technological and managerial support, in an effort to increase businesses' stability and borrowing capabilities. Funding assistance to SMEs is a common theme across the initiatives to help SMEs.

For most countries, social enterprises are served, supervised, and regulated by a patchwork of government agencies, or no agencies at all, making it more difficult for social enterprises to navigate and obtain the support they need. We believe a single government agency or state sponsored organization, modeled after an SME agency and charged with supervising and providing support for social enterprises, could enable social enterprises to easily find the assistance, and information they need without using their limited resources to navigate a bureaucratic web.

Non-financial resources for social enterprises

Similar to the status-quo-related to government agencies dedicated to social enterprises, many countries have government initiatives and resources that target SMEs, which many social enterprises would be eligible to take advantage of, but fewer have dedicated resources that specifically target social enterprises. However, governments can play a strong role in providing non-financial resources and support to social enterprises.

For example, the Czech Republic launched a government project, Social Entrepreneurship Support, which will operate until November 2021. The main objective of this project is to offer a network of consultant and traineeships to build relevant experience and know-how and promote the creation of social enterprises.

The Social Entrepreneurship Support seeks to accomplish this objective by connecting social enterprises with "Local Consultants." These local consultants are experts with experience working with social enterprises. They will, in turn, share their knowledge with up and coming social enterprises in the Czech Republic. South Korea also has dedicated programs for social enterprises, which provide consultations and operational support for qualified social enterprises on issues related to business, tax, labor, accounting, and employee training. Another objective of these resources is to help social enterprises access financial incentives such as tax exemptions and social insurance premium assistance.[34] In addition, the Ontario government in Canada has created various initiatives to support social entrepreneurs, educators, and impact investors.

These are all positive models to emulate, though jurisdictions are likely to have numerous examples of similar non-financial resources for SMEs within their own borders, including programs providing counseling and consultation, training and education, tax advice, facilitation of networking and collaboration among SMEs, and promotion of SMEs in general.

While these programs may be helpful to and relevant for social enterprises, there is additional value to create resources specifically dedicated to social enterprises, which face unique issues different from other SMEs.

Regulatory sandboxes

A "Regulatory Sandbox" is a framework set up by a regulator to allow small-scale, live testing of business and technological innovations by private enterprises in a controlled environment under the regulator's supervision without the need to fully comply with costly, complex, and often confusing legal requirements that would otherwise pose barriers to entry. For example, Japan has a framework of a regulatory sandbox to support the development of innovative technologies and business models that are difficult to implement due to existing regulatory restrictions and that relate to financial services, healthcare, mobility and transportation. Under the framework, a business operator that has obtained an approval from the competent authority can experiment under certain condition, without the full impact of applicable domestic Japanese laws and regulations.

[34] *See* Doh, Soogwan, 2020, "Social Entrepreneurship and Regional Economic Development: The Case of Social Enterprise in South Korea" *Sustainability* 12, no. 21: 8843. https://doi.org/10.3390/su12218843; Jeong, Bokgyo, (2017), "South Korea: Government Directed Social Enterprise Development: Toward a New Asian Social Enterprise Country Model," Kerlin, J.A. (Ed.) *Shaping Social Enterprise*, Emerald Publishing Limited, Bingley, pp. 49-77. https://doi.org/10.1108/978-1-78714-250-320171003

None of the survey respondents reported having a Regulatory Sandbox specifically tailored for social enterprises. Regulators may wish to consider implementing regulatory sandboxes uniquely tailored to social enterprises to address the many unique challenges these enterprises face with respect to funding, labor, and the like.

For example, one of the greatest difficulties social enterprises face is in fundraising. There are inherent difficulties in fundraising due to many investors perceiving social enterprises as less lucrative opportunities than their conventional business counterparts. This difficulty is exacerbated by what may be a patchwork of regulations around fundraising, including limitations under corporate law, federal and provincial securities laws, and tax policies that prevent social enterprises from effectively raising capital from the general public. Thus, a Regulatory Sandbox around crowdfunding, whether generally or for social enterprises specifically, could be highly valuable.

Pakistan provides such a model. As crowdfunding is not yet legal in Pakistan, the Securities & Exchange Commission of Pakistan granted approval to a technology-based crowdfunding platform to commence live testing and experimentation under its Regulatory Sandbox initiative.

Under the initiative, the applicant is allowed to operate in a controlled environment for a period of up to six months and if the initiative is successful, a legal framework for crowd funding platforms may be developed in Pakistan.

We note that one potential hurdle in using Regulatory Sandboxes as a policy tool is the amount of financial and human resources associated with establishing, supporting, and enforcing the framework for the Regulatory Sandbox. When adopting a framework for a Regulatory Sandbox, legislators should carefully evaluate feasibility and demand, adopt specific and clear entry conditions/criteria for participation, and decide on the scope of support to be provided to participants. Further, legislators could consider easing entry requirements, simplifying the application process and/or cost of application for social enterprises participating in general Regulatory Sandboxes to encourage social enterprises to participate.

VIII. Catalyzing change by defining the solution

One factor that seems to consistently stifle the ability to promote social enterprise and implement any of the many policies or programs discussed in this Report is that in many countries, there is no clear definition of what a social enterprise *is*.

If achieving the SDGs by 2030 is the central problem faced by the world right now, and social enterprises are a key solution, progress must begin by defining the solution.
There is value in keeping this definition broad. As discussed in our Report, many jurisdictions that limit their conception of social enterprises to only non-profit entities ignore a vast number of for-profit entities that are helping to achieve positive social and environmental goals. There is also value in keeping this definition narrow. Having a definition that is too broad enables greenwashing and for businesses that do not focus on ESG and impact to unduly derive competitive benefit and take up resources that could be put to better use elsewhere.

Policy makers have myriad tools at their disposal to promote social enterprise. They can create new corporate forms, they can adopt more flexible tax policies, they can promote private investment, they can facilitate fundraising, they can provide support services, they can reward and promote good behaviors, and they can require ESG and impact-related disclosures.
But the first step for policy makers seeking to develop a more comprehensive framework to catalyze growth in social enterprises will be to confirm what enterprises should benefit from their support.

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