BALANCING PURPOSE AND PROFIT

Legal mechanisms to lock in social mission for *"profit with purpose"* businesses across the G8

Addendum: Review of legal and policy developments since 2014

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PAOLA BAROMETRO	Associate	Italy
ALEXANDRA E. CAMBOURIS	Senior Associate	United States
ANDREA CASINI	Summer Associate	Italy
SYDNEY DOMORAUD-OPERI	Counsel	France
SIRA FRANZINI	Attorney Trainee	Italy
KANE HUANG	Senior Associate	Japan
YUKO INUI	Senior Associate	Japan
RENE KATHAWALA	Pro Bono Counsel	Overall Coordination, including Canada
DARIA LOSHKAREVA	Career Associate	Russia
GIOVANNI LEONI	Associate	Italy
WILHELM NOLTING-HAUFF	Partner	Germany
DOMINIC O'BRIEN	Partner	United Kingdom
MARKUS PIONTEK	Associate	Germany
DOMINIC SEDGHI	Senior Professional Support Lawyer	United Kingdom
ALEXANDER SHCHAVELEV	Associate	Germany
STEFAN SCHULTES-SCHNITZLEIN	Partner	Germany
GABRIELLE VIVIER	Associate	France

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DISCLAIMER

The contents of this Guide are for information purposes and to provide an overview only. This Guide does not provide legal information on how to and whether to choose a particular corporate form in each of the eight jurisdictions discussed. The Guide also does not purport to discuss all corporate forms available in each jurisdiction, though those it does discuss are current as at June 2016 only. Although we hope and believe the Guide will be helpful as background material, we cannot warrant that it is accurate or complete, particularly as circumstances change after publication. Moreover, the Guide is general in nature and may not apply to particular factual or legal circumstances. This Guide is intended to convey only general information, therefore it may not be applicable in all situations and should not be relied or acted upon as legal advice. This Guide does not constitute legal advice and should not be relied on as such. Readers seeking to act upon any of the information contained in this Guide are urged to seek individual advice from legal counsel in relation to their specific circumstances.

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EXECUTIVE SUMMARY

Many countries are introducing legal innovations at the intersection of business and social impact. This is an exciting and fast-moving space, and it can be hard to keep up with the latest developments.

In December 2014, UnLtd, the Foundation for Social Entrepreneurs, worked with the international law firm Orrick, Herrington & Sutcliffe LLP to produce a report titled "Balancing Purpose With Profit." The report, published by the Thomson Reuters Foundation, fed into the deliberations of the Mission Alignment Working Group of the Social Impact Investment Taskforce established under the United Kingdom's Presidency of the G8. It was published in the context of the Taskforce's recommendation that all governments should "provide appropriate legal forms or provisions for entrepreneurs and investors who wish to secure social mission into the future."

Orrick's analysis set out the legal and regulatory systems of the G8 countries with respect to businesses whose primary purpose is to deliver social impact, which retain flexibility to distribute some or all of their profits – otherwise known as "profit-with-purpose businesses" ("PPBs"). Our research paper identified the corporate structures that can be used by PPBs in each G8 country, the market mechanisms that could help these impact-driven businesses lock in or demonstrate social purpose and key areas for legal reform in each G8 country.

Now, 18 months later, we publish this update on the development of corporate structures for PPBs. We have observed significant innovations in Canada, France, Italy, the United Kingdom and the United States. The development of legal and other structures that make PPBs more attractive is a powerful confirmation of the reality in our civil society that not every investor or shareholder subscriber is motivated solely by profit. Millions of business owners around the world seek to do more than simply maximize financial return. Their primary purposes include improving the environment, eradicating poverty and developing communities. In the classic model, these social purposes had to be pursued as a charity or nonprofit corporation. This is no longer the case, and the G8 countries are continuing to develop legal regimes that allow businesses to have a primary mission of having a positive social and environmental impact while gaining access to investment capital that can deliver that impact in unprecedented scale and scope.

The significant developments since the publication of our original report can be summarized as follows:

- Canada: At least one province is actively reviewing the creation of a new corporate form in line with the key characteristics of PPBs, and the province British Columbia, with one of the strongest PPB regimes, introduced Social Impact Purchasing Guidelines;

- France: More than 30 different implementing measures were adopted in connection with the legal framework available to businesses with limited profit-distribution, the "enterprises of the social and solidarity economy" ("SSE"), which included provisions that allow for-profit companies to obtain the SSE designation and give greater access to public funding for SSEs. In addition, organizations such as B-Lab have entered the French market to provide a certification system

for PPBs. In the first year alone, more than 30 companies have been certified by B Lab;

- Italy: Parliament passed the 2016 Financial Law that created the benefit company ("*Società Benefit*") in the Italian corporate law; a new regulation was passed on the "innovative startup with social purposes"; and bill n. 1870, reforming the Voluntary Sector, or Third Sector, and, specifically, amending the existing regulations governing social enterprises, was approved by the Parliament on the 25th May 2016;

- United Kingdom: The Government has launched a Review on Mission-Led Business, which will examine the potential of PPBs and produce recommendations for further development of this sector. The Government has also introduced various refinements to the existing legal framework. For example, as part of its 2015 budget, the Government announced a new Social Venture Capital Trust to encourage investment in companies that invest in social enterprises; and

- United States: Six jurisdictions passed legislation authorizing the creation of PPBs, including public benefit corporations and L3Cs; the Internal Revenue Service clarified rules applicable to private foundations that may help to facilitate further investments in PPBs; and there were at least two very significant market transactions involving PPBs, with one going public and the other issuing a public offering, all receiving considerable market attention.

The attached reports provide more detail on the developments in these countries. It should be noted that despite the lack of significant reform in Germany, Japan and Russia, there are still signs that social enterprise and social business activity in those jurisdictions is only increasing. We have been in touch with social enterprise clients in those jurisdictions who are working to solve significant social and/or environmental issues there.

CANADA

CANADA

1. Introduction

Since publication of the first report, Canada has continued to foster an enabling environment for profit-with-purpose businesses ("PPBs"). While only one province has introduced and implemented a corporate form for PPBs, recent initiatives have helped to bolster their financial sustainability and organizational visibility. These efforts include the introduction of social procurement and social finance policies, along with the provision of capacity building and advisory services. These initiatives may serve to accelerate PPB formation in Canada, where both the federal and provincial governments continue to prioritize the development of the social economy.

2. Legislative and Regulatory Developments

The Canadian provinces of British Columbia and Nova Scotia have introduced specific corporate forms for profit-with-purpose businesses (PPBs), namely the Community Contribution Company (C3) and Community Interest Company (CIC). British Columbia's C3 Act has not been amended since it was added in the 2011-12 parliament.[1] Nova Scotia's CIC Act, introduced in November 2012 and amended in November 2014,[2] is still not in force due to the absence of approved regulations to implement the corporate form.

No other Canadian province has amended or enacted provincial legislation pursuant to a legally recognized PPB structure. However, businesses throughout Canada can avail themselves of British Columbia's C3 legislation. In Canada, an entity can incorporate in a province and register to conduct business in another. If a business were to incorporate as a C3 in British Columbia, it would be required to adhere to the Act's regulatory requirements, even if registered and operating elsewhere. As of May 2015, fewer than thirty C3s have incorporated under the Act, while at least one has adopted the strategy of incorporating in British Columbia in order to operate as a C3 in a different province.

The Government of Canada has not introduced rules to facilitate the incorporation of a PPB structure at the federal level. In November 2015, ministerial mandate letters to the Minister of Families, Children and Social Development, the Minister of National Revenue and the Minister of Employment, Workforce Development and Labour included the directive to "develop a Social Innovation and Social Finance strategy." However, the mandate letters do not describe specific action items regarding the strategy.

3. Other Developments to Promote PPBs in Canada

Ontario is the only province actively reviewing the creation of a new corporate form in line with the key characteristics of PPBs. As part of Social Enterprise Strategy for Ontario, the Ministry of Consumer Services formed a Social Enterprise Panel in January 2014 to "explore introducing legislation to enable the creation of new 'hybrid' corporations (e.g., for-profit corporations that are dedicated to a social purpose, and required to re-invest a portion of

[1] British Columbia "Point in Time" Act Content, Business Corporations Act, [sbc 2002] Chapter 57, *available at* http://www.bclaws.ca/civix/document/id/consol22/consol22/02057_pit.
[2] Government Restructuring (2014) Act: Chapter 34 of the Acts of 2014, available at http://nslegislature.ca/legc/bills/62nd_2nd/3rd_read/b005.htm#text.

profits into that social purpose)." [3] In May 2014, the Social Enterprise Panel released a set of recommendations that included a call for public input. Public submissions were due in May 2015.

Five Canadian provinces have implemented social enterprise strategies: Newfoundland and Labrador, Québec, Ontario, Manitoba and Nova Scotia. Of the five provinces, only two, Manitoba[4] and Newfoundland and Labrador[5], introduced social enterprise strategies since December 2014. Unlike Ontario, neither of the new initiatives specifically references the introduction of a new corporate form or seeks to confer PPBs with legal or fiscal definition through alternative channels. However, in Canada, where a "social enterprise" is not a legally recognized business structure, provincial social enterprise strategies encompass an array of initiatives that may improve the environment for PPB formation and development, including social procurement policies.

In March 2015, British Columbia introduced Social Impact Purchasing Guidelines. The guidelines include two channels for implementation: "purchasing goods or services from a social enterprise or socially conscious business," and "incorporating social value in solicitation documents." The guidelines are inclusive with regard to legal form, specifically recognizing both C3s and "traditional for-profit business" in addition to charitable organizations. While other provinces and municipalities have introduced social procurement policies, this policy is directly applicable due its implementation in a province with a specific corporate form for PPBs.

[3] Dual Purpose Corporate Structure Legislation: Stakeholder Engagement Report, available at http://www.ontariocanada.com/registry/showAttachment.do?postingId=17642&attachmentId=26891.
[4] Manitoba Social Enterprise Strategy: A Strategy for Creating Jobs through Social Enterprise, available at https://ccednet-rcdec.ca/sites/ccednet-rcdec.ca/files/ccednet/pdfs/mb_social_enterprise_strategy_2015.pdf.
[5] Government of Newfoundland and Labrador, Office of the Premier, available at http://www.exec.gov.nl.ca/exec/cabinet/ministers/pdf/Minister_Mitchelmore_Mandate.pdf.

FRANCE

FRANCE

1. Introduction

Since publication of the report (the "Report") on profit-with-purpose businesses ("PPBs") in France, more than 30 different implementing measures were adopted in 2015 to clarify the social and solidarity economy ("SSE") law. Specifically, the Government specified the requirements for obtaining recognition as either an "enterprise of the social and solidarity economy" (the "SSE Enterprise") or "solidarity enterprise of social utility." This legislative activity provides further support to the growing social sector in France.

2. Amendments to the SSE Law

As mentioned in the Report, associations, foundations, cooperatives and mutual companies are considered de facto SSE enterprises. For-profit commercial companies can obtain the SSE enterprise designation provided that certain conditions are respected[6] and expressly incorporated within the articles of association. The implementing measures for the SSE law provide for (i) the specific stipulations that must be included in their articles of association[7], (ii) the additional information that must be provided at the time of registration;[8] and (iii) the conditions upon which for-profit SSE enterprises may proceed with a capital reduction for reasons other than losses.[9]

The designation of a "solidarity enterprise of social utility" has also been clarified through publication of the specific requirements to be met in order to receive such designation.[10]

Two points should be emphasized. First, regarding third parties' right to enforce social purpose, the SSE Law creates regional chambers of the social and solidarity economy, which have standing to take legal action to enforce the articles of association of SSE enterprises and, through them, their legal obligations. Second, it appears that the legal obligations applicable to SSE enterprises regarding profit distribution limitations, governance and capital reductions are more restrictive than those being applied to companies not benefiting from the above mentioned legal label. Therefore, one should understand that using such labels involves specific constraints relevant to PPBs.

3. Other Notable Developments Further Fostering PPBs in France

SSE enterprises now benefit from financing and tax advantages such as (i) specific funding from Bpifrance, the public investment bank (e.g., Social and Solidarity Loan, from 10 to 50,000 €) and more than 60 different socially-committed financial institutions (*financement solidaire*); (ii) specific funding from local authorities (e.g. subsidies granted through calls for proposals for project funding); and (iii) specific public procurements (e.g., local authorities and public entities whose annual public procurements are worth at least 100 million € pretax

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[6] Already mentioned in the first version of the Report (see paragraph 5.2 of the France Report).

[7] Décret n°2015-858 du 13 juillet 2015 relatif aux statuts des sociétés commerciales ayant la qualité d'entreprises de l'économie sociale et solidaire.

[8] Décret n°2015-1219 du 1er octobre 2015 relatif à l'inscription des personnes morales de droit privé ayant la qualité d'entreprises de l'économie sociale et solidaire.

[9] Décret n°2015-760 du 24 juin 2015 pris pour l'application de l'article 1er alinéa 15 de la loi n°2014-856 du 31 juillet 2014 relative à l'économie sociale et solidaire.

[10] Décret n°2015-719 du 23 juin 2015 relatif à l'agrément « entreprise solidaire d'utilité sociale » régi par l'article L. 3332-17-1 du code du travail.

value in aggregate) must adopt a socially responsible public procurements policy.[11] In addition, since publication of the Report, the Government passed a law granting funding to pay for a full-time employee for SSE enterprises in ten different regions.[12] However, investing into a SSE enterprise does not grant any specific tax benefit.

"Solidarity enterprises of social utility" have access to the aforementioned advantages, plus (i) additional specific funding from Bpifrance; (ii) additional specific funding from local authorities; and (iii) funding from solidarity employee savings funds. In addition, investors in "solidarity enterprises of social utility" may claim tax benefits such as income tax (18% tax credit) or solidarity tax on wealth reductions (50% tax credit).

Overall, there is a strong case for affirming that the SSE Enterprise sector is attracting increasing interest in France. The appropriate legal framework is developing progressively, as shown by the aforementioned implementing measures of the SSE Law. The government will publish (hopefully by the end of 2016) a guide of good practices provided by the SSE Law to further clarify the SSE Law with respect to SSE enterprises. However, in the meantime, some major legal uncertainties still exist, such as the definition of "stakeholders," "democratic governance" and "social utility."[13] The same is also true for (i) the binding status of the just mentioned guide of good practices or (ii) to the interpretation to be given to the principle according to which profits must be principally dedicated to the development and maintenance of the activities of the SSE Enterprise. Therefore, entrepreneurs will have to bear in mind those different elements when conducting the cost-benefit analysis prior to applying for the "SSE enterprise" or "enterprise of social utility" designation. With respect to investors, they must be aware that, under the SSE law, there is no limit on the return on investment in the event of a sale of shares. Nevertheless, the majority of profits of a SSE enterprise must be used for the social purpose (at least 50%), which is an extra constraint in comparison to companies that do not use these designations.

There was another notable development to spur the further growth of PPBs in France in 2015, when the B-corp label was officially launched. More than 30 companies are already certified and many more are becoming B-corps. Other designations that promote PPB businesses include the "Lucie" label for CSR/environmental companies, the "ENR" *(Entreprise Numérique Responsable*) for responsible digital companies, the ISO certification, and the "new economy company movement" ("MENE") launched in 2015 with the publication of the "MENE charter" (*Mouvement des Entreprises de la Nouvelle Économie).*

[11] Décret n°2015-90 du 28 janvier 2015 fixant le montant prévu à l'article 13 de la loi n°2014-856 du 31 juillet 2014 relative à l'économie sociale et solidaire.
[12] Loi n° 2016-231 du 29 février 2016 d'expérimentation territoriale visant à résorber le chômage de longue durée publiée au Journal Officiel du 1er mars 2016.
[13] These are the criteria a company using the SSE Law labels has to comply with. Please *see* paragraph 5.2 of the France section of the Report.

ITALY

ITALY

1. Introduction

At the time when our initial report was published (the "2014 Report"), Italian law did not provide for a specific legal form designed for pursuing a profit-with-purpose business ("PPB"). Entities seeking to be a PPB could incorporate (and may still incorporate under the current law) as an ordinary for-profit legal entity pursuant to the Italian Civil Code, and commit as a secondary purpose to accomplish a social and/or environmental benefit, thus opting to acquire the status of "social enterprises" ("*impresa sociale*") under Law no. 118 of 13th June 2005 and implementing measures (above all, Legislative Decree no. 155 of 24th March 2006, the "Decree"). The Decree provides for a legal qualification of "social enterprise" that applies to both non-profit (*i.e.*, associations, foundations) and profit-driven (*i.e.*, partnerships, joint-stock companies, limited liability companies, partnerships limited by shares, cooperative companies and consortia) legal entities. In order to qualify as a social enterprise, those legal entities that are naturally profit-driven such as companies have to give up their ability to share the profits amongst the owners/shareholders and are subject to a number of restrictions, thereby converting into non-profit entities.

Since the publication of the 2014 Report, there have been three significant changes in the Italian legal framework applicable to PPBs:

- bill no. 1870 on the reform of the Voluntary Sector (commonly called Third Sector or "*Terzo Settore*") was approved by the Italian Parliament on the 25th May 2016, which includes amendments to the regulation on social enterprises;
- the new regulation on the "innovative startup with social purposes"; and
- the introduction of the "Benefit Company" into the Italian legal framework by the 2016 Financial Law.[14]

Some minor changes in the corporate tax rates and VAT rates have also been introduced for all companies by the 2016 Financial Law, which will also have an impact on the tax treatment of companies pursuing social purposes.

Below is a detailed analysis of these significant developments for PPBs under Italian law.

2. Amendments to Regulation on Social Enterprises

2.1 Bill No. 1870 and the Reform of the "Third Sector"

As already explained in our 2014 Report, the social enterprise regime outlined by the Decree has proven to be unattractive, mainly due to i) the absence of tax, economic or other support policies adopted by the Italian Government; ii) the existence of barriers to access investments; iii) a slow implementation of the Decree by local administrations; and iv) the circumstance that the Decree has not repealed existing provisions of law, which apply to different kinds of non-profit entities, thereby creating an uneven legal framework for this sector.

[14] This is the Italian Budget Law. Law no. 208 of 28th December 2015 *Disposizioni per la formazione del bilancio annuale e pluriennale dello Stato* (*Legge di stabilità 2016*), entered into force on 1st January 2016.

In order to address the pitfalls of the current legal framework for social enterprises, an amendment to the Decree was proposed by the Democratic Party on 22nd August 2014 and included in Bill no. 2617 (now no. 1870). The Bill was passed by the Chamber of Deputies on 9th April 2015 and by the Senate on 30th March 2016, and the final text was approved on 25th May after a long and sometimes complex discussion by both Houses of the Italian Parliament.

Bill no. 1870 has the form of a law (so-called "enabling law" or "*legge delega*") that will give the Government the authority to legislate by executive order ("*decreto legge*") within the limits provided by the enabling law. Most specifically, Prime Minister Matteo Renzi's government has been mandated by the parliament ("delegated") to carry out the reform of the so-called Third Sector, which should also include a revision of the legal regime of social enterprises.

Due to its delegating nature, this Bill only provides for guiding principles and criteria with regards to the upcoming reform. The Italian Government shall now adopt the legislative decrees that will actually affect the current legal framework.[15]

2.2 Bill No. 1870 Overview

The principles and criteria that shall lead the exercise of the Government's legislative power in the review and reorganization of the regulation on social enterprise are the following:

- **Legal qualification of the social enterprise** - the social enterprise is defined as a private organization pursuing – together with all entities of the Third Sector – the common good and aiming at enhancing the level of active citizenship, social protection and cohesion, promoting the participation, the inclusion and the full development of each person, and enhancing the potential for growth and the employment.[16] In pursuing those goals, social enterprises shall i) act primarily through the company profits (meaning that other sources of financing might be acceptable); ii) adopt responsible and transparent management systems; and iii) foster the full engagement of employees and other stakeholders.[17]

- **Sectors of social activities** – social enterprises shall choose those sectors where they may operate among those activities of "general interest" typically pursued by entities of the Third Sector, as individualized by the delegated law itself pursuant to Section 4, para. 1 of the Bill.[18] The list of such activities of "general interest" shall include activities individualized i) through criteria that take into account certain standard of social interest and ii) on the basis of the sectors already provided for by the Decree and by the law regulating the tax regime of the so-called Non-Profit Organizations of Social Utility (i.e. ONLUS), Legislative Decree of 4th December 1997, no. 460.[19] Furthermore, the list should be periodically updated and integrated through decrees of the Prime Minister based on proposals from the Minister of Labor and Social Policies.[20]

- **Social cooperatives** - social cooperatives and their consortiums shall automatically

[15] Since the Senate approved the Bill with amendments, based on applicable law, a second approval by the Chamber is necessary.
[16] Sections 1, para. 1 and 4, para. 1, lett. a) of Bill no. 1870.
[17] Section 6, para. 1, lett. a) of Bill no. 1870.
[18] Section 6, para. 1, lett. b) of Bill no. 1870.
[19] Please see paragraph 6.1 of the 2014 Report.
[20] Section 4, para. 1, lett. b) of Bill no. 1870.

qualify as social enterprises.[21]

- **Distribution of profits** - forms of remuneration of share capital shall be allowed, ensuring the prevailing allocation of profits to the achievement of social objectives. Such forms of remuneration shall be subject to certain conditions and in any case shall comply with the restrictions established for cooperatives "with a prevalence of mutual aid."[22] A prohibition against the distribution of surplus operating funds shall be maintained for those entities for which the law already provides, even if they are qualified as social enterprise.[23]

- **Financial Statements** – organizations operating a social enterprise shall have the obligation to draft their financial statements pursuant to Section 2423 of the Italian Civil Code, if compatible.[24]

- **Transparency** - the provision of specific obligations for transparency and limits on the remuneration of corporate officers and governing bodies.[25] Please note that the transparency requirement applies to every entity that is part of the Third Sector.

- **Redefinition of the categories of disadvantaged workers** –categories of disadvantaged workers to be employed within social enterprises shall be redefined, taking into account the "new forms of social exclusion" and the principles of equal opportunities as set forth by the national and European legal framework currently in force and including a gradual shift of benefits aimed at favoring the most disadvantaged categories.[26] Please note that the relevant categories of disadvantaged workers were specified by EC Regulation no. 800/2008.

- **Entities as member of administrative bodies** –private companies or public entities shall be allowed to be appointed as a member of corporate bodies of the social enterprises, without prejudice to the prohibition of assuming a position of control.[27]

- **Coordination with non-profit sector regulation** – the Bill asks for a reorganization and more accurate coordination of the legal framework on social enterprises with the rules concerning business activities carried out by non-profit organizations.[28]

- **Auditors** – one or more auditors shall be nominated by the articles of association and shall be in charge of monitoring the compliance i) with the law and the bylaws of the company, ii) the principles of sound administration and iii) the adequacy of the company's organizational and administrative structure and accounting systems.[29]

- Section 9 of the Bill sets forth the principles and the guiding criteria that the Government should conform to while introducing financial support measures in favor of (all) "Third Sector" entities. The following criteria specifically concern social enterprises:

[21] Section 6, para. 1, lett. c) of Bill no. 1870.
[22] Please refer to the 2014 Report, page 11 for the definition of cooperative companies with a prevalence of mutual aid and relevant distribution restrictions.
[23] Section 6, para. 1 lett. d) of Bill no. 1870.
[24] Section 6, para. 1 lett. e) of Bill no. 1870.
[25] Section 6, para. 1 lett. f) of Bill no. 1870.
[26] Section 6, para. 1 lett. g) of Bill no. 1870.
[27] Section 6, para. 1 lett. h) of Bill no. 1870.
[28] Section 6, para. 1 lett. i) of Bill no. 1870.
[29] Section 6, para. 1 lett. f) of Bill no. 1870.

a) the introduction of forms of access to raising venture capital through web portals;[30] and
b) tax relief measures to encourage capital investments.[31]

Moreover, the law provides economic support measures in favor of entities of the Third Sector and actions aimed to reorder and to harmonize the tax system and to offer different forms of advantageous taxation.

3. Innovative Startup with a Social Purpose

With Law Decree no. 18th October 2012, no. 179, converted into Law no. 221 of 17th December 2012 (the "Startup Law"), the Italian government enacted a specific regulation on "innovative startups" aimed at boosting innovation through the creation and development of this new legal form of company.[32]

Sections 25 to 32 of the law provide for specific measures aimed at promoting the creation and development of startups in Italy. Several incentives as well as exceptions to the general rules applicable to enterprises are provided by the Startup Law to stimulate investments in innovative startups.

More specifically, the Startup Law introduced tax incentives for corporate and private investments in startups.[33] These incentives apply both in case of direct investments in startups and in case of indirect investments through other companies investing predominantly in startups. The main provisions are the following:

a) personal income taxpayers investing directly or indirectly in innovative startups may benefit from a tax credit ("*detrazione*") equal to 19% of the amount invested up to a maximum of Euro 500,000;

b) corporate income taxpayers investing directly or indirectly may benefit from a tax allowance ("*deduzione*") equal to 20% of the amount invested in the innovative startup's share capital, up to a maximum of Euro 1.8 million;[34] and

c) the main condition for the grant of the above tax incentives is that the investor maintains an amount at least equal to the tax incentive in the innovative startup for at least two years.[35]

In order to benefit from support measures, a startup must fulfill a number of requirements, including:

a) it shall have been established for no longer than 48 months;
b) it shall reside or be subject to taxation in Italy;
c) it shall have no turnover or shall have a turnover not exceeding Euro 5 million;
d) it shall not distribute profits;
e) its core business shall consist of innovative goods or services of high technological value;
f) it shall not originate from a merger, demerger or divestment process;

[30] Section 9, para. 1 lett. f), no. 1 of Bill no. 1870.
[31] Section 9, para.1 lett. f), no. 2 of Bill no. 1870.
[32] Law no. 221 of 17th December 2012 on "Further urgent measures for Italy's economic growth", commonly known as "Decreto Crescita bis."
[33] Section 29 of the Startup Law. The tax incentives were implemented by Ministerial Decree of 30th January 2014 in relation to fiscal years 2013, 2014 and 2015. They were extended to 2016 with Ministerial Decree of 19th February 2016.
[34] Section 29 of the Startup Law.
[35] Ministerial Decree 30th January 2014.

g) it shall meet specific requirements concerning its employees, namely:
   - either 15% of its costs shall be related to R&D; or
   - at least one-third of the team shall be made up of people who either hold a PhD or are PhD candidates at an Italian or foreign university or have conducted research for at least three years or at least two-thirds of the team shall be made up of people holding a Master's degree; or
   - it shall be the owner or the licensee of a patent or a registered software.

In January 2015, the Italian government regulated the new form of "innovative startup with a social purpose" by means of Circular 3677/C (the "Circular").[36]

The new "innovative startup with a social purpose" is a company that fulfills all of the requirements that apply to ordinary startups but operates in specific sectors that have a considerable social value according to the Italian legislator. Such sectors match those provided for by the legislation on social enterprises, including social inclusion, providing support against the marginalization of disabled persons, environmental protection, etc. (please see paragraph 2.1 of the 2014 Report).

The Circular introduced a new procedure – based on the accountability of the social impact, on transparency and widespread control of information – for the recognition of innovative startups with a social purpose. Such procedure requires companies wishing to register as innovative startups with a social purpose to file a "self-certification" where they:

1) represent that they operate in one of more sectors listed in Section 2, para. 1 of the Decree;
2) indicate the sectors where they operate;
3) represent that they pursue an interest of general benefit; and
4) undertake to give evidence of their social impact by means of drafting the so-called "Document of description of social impact" ("*Documento di descrizione di impatto sociale*"). Such document should demonstrate the social impact of the startup, meaning the long-term benefits that it is supposed to have and changes that it is supposed to bring in the (local) community, in terms of knowledge, attitudes, status, life conditions and values.

Innovative startups for social purpose are subject to the same legal exemption as regular startups, but they are granted a more favorable tax regime, namely:

i. personal income taxpayers investing directly or indirectly in innovative startups may benefit from a tax credit ("*detrazione*") equal to 25% (as opposed to 19% for regular startups) of the amount invested; and
ii. corporate income taxpayers investing directly or indirectly may benefit from a tax allowance ("*deduzione*") equal to 27 % (as opposed to 20% for regular startups) of the amount invested.[37]

4. The New Italian Benefit Corporation

With the approval of the 2016 Financial Law, the Italian legislator introduced the Benefit Corporation into the Italian legal framework, thus making Italy the first country to enact such corporate form outside the United States.

[36] Circular 3677/C issued by the Ministry of Economic Development on 20th of January 2015.
[37] Section 29 of the Startup Law.

Benefit corporations are the first PPB form introduced by the Italian legislator. They are for-profit companies that at the same time pursue "one or more purposes of common benefit and act in a responsibly, sustainable and transparent manner towards persons, communities, territories and environment, social and cultural commons and activities, entities and associations as well as all other stakeholders"[38] (e.g., employees, customers, suppliers, lenders, creditors, Public Administration and civil society).

Based on the 2016 Financial Law, companies that seek to pursue a social purpose with the aim of sharing profits shall adopt one of the typical forms provided for by Section 2249 of the Italian Civil Code (which was described in the 2014 report) and apply to register as "benefit companies." In order to qualify as a benefit corporation, such companies shall undergo a certification process to meet standards of social and environmental performance, accountability and transparency.

The 2016 Financial Law has set forth the following rules for Italian benefit corporations:

1. the social purposes of the benefit corporations shall be specifically indicated in the corporate activity ("*oggetto sociale"*).[39] An existing company may apply to register as a Benefit Corporation after amending its deed of incorporation or its bylaws by including in the Company's corporate activity the new general social purposes;

2. the company's management shall aim at balancing the pursuit of profits, the interests of its shareholders and those of its stakeholders;[40]

3. benefit corporations shall identify the person or the persons (i.e., directors) entrusted with functions and tasks aimed at pursuing the common benefit goals;[41]

4. sanctions provided for by the Italian Civil Code in relation to directors' liability shall apply to the directors of a benefit company in the event of failure to fulfill their obligations under points 2 and 3 above;[42]

5. an annual report shall be attached to the annual financial statements of the benefit corporation. Such report shall describe the achievement of common benefit goals and shall include:

    - the description of goals, methods and actions implemented by the management for the pursuit of the social purpose and any circumstances that may have prevented or delayed such achievement;

    - an impact assessment;

    - description of the new goals that the company intends to pursue in the following year.[43]

[38] Section 1, para. 376 of the 2016 Financial Law.
[39] Section 1, para. 379 of the 2016 Financial Law.
[40] Section 1, para. 380 of the 2016 Financial Law.
[41] Section 1, para. 380 of the 2016 Financial Law.
[42] Section 1, para. 381 of the 2016 Financial Law.
[43] Section 1, para. 381 of the 2016 Financial Law.

In the event that a benefit corporation breaches its obligation to pursue social goals, it shall be subject to sanctions provided by the regulation on misleading advertising[44] and by the Italian Consumer Code.[45]

5. Tax Changes

With reference to the current legal framework on tax treatment of companies as described in the 2014 Report, the 2016 Financial law has provided for the following changes:

- the corporate tax rate switches from 27,50% to 24% with effect from the tax period following the period underway, on December 31, 2016.[46] Therefore the rate of the withholding on profits paid out to companies and entities subject to an income corporate tax in a EU member state as well as in another state party to the EEA Agreement, included in the white list, is amended;

- social cooperatives are subject to VAT with a 5% tax rate for social, healthcare, educational and welfare services rendered to special categories of disadvantaged persons.[47]

[44] Legislative Decree no. 145 of 2nd August 2007, Implementing Section 14 of Directive 2005/29/EC amending Directive 84/450/EEC on misleading advertising.
[45] Legislative Decree no. 206 of 6th September 2005, Consumer Code.
[46] Section 1, para. 61 of the 2016 Financial Law.
[47] Section 1, para. 960 of the 2016 Financial Law.

UNITED KINGDOM

UNITED KINGDOM

1. Introduction

The most significant development in the United Kingdom for profit-with-purpose businesses ("PPBs") since issuance of the Report (the "Report") relates to the Government's decision to conduct a new review to unlock the potential of PPBs. This review is potentially very significant for PPBs and how they are treated in law and policy, even though recommendations are not expected to issue until Autumn 2016.

2. Government Review of PPBs

In March 2016, the Minister for Civil Society launched a Review on Mission-Led Business, which aims to substantially increase the economic and social impact of PPBs in the UK economy.[48] The press release that the Government issued in connection with this review noted the following: "It is estimated that there are as many as 195,000 of these businesses in the UK, employing 1.6 million people. In 2012 these businesses were estimated to turn over £120 billion a year. They are adopting new solutions to longstanding social issues like aged care, dementia and unemployment. The review, led by the Cabinet Office, will examine how this emerging sector can be supported to double in size over the next decade, delivering greater economic and social benefits. The review will shortly issue a Call for Input and report by the end of 2016. This trend is being driven by the millennial generation who increasingly demand an increased focus on social purpose in who they work for, how they consume and where they invest."[49]

As part of this process, the Government seeks to know more about why businesses might adopt PPB corporate forms, how these businesses will grow over time, the challenges they might face and how to address them. The Government's particular focus is on those who run mission-led and mainstream businesses, as well as those who invest in, advise and fund businesses that combine profit and social impact. The Government's review will likely result in significant positive treatment of PPBs in both law and policy, with the review to be completed by Autumn 2016.[50]

3. Other Notable Developments for PPBs

On 6 April 2016, the new UK Ownership and Control Transparency Regime relating to Persons with Significant Control ("PSC") came into force. From this date, companies registered in the UK must (unless they are exempt from the regime) investigate and record details of persons who have "significant control" over them. Significant control is met by satisfying on of five specific criteria. These are based on share ownership, voting rights, board control, other significant influence or control and control through a trust or partnership. The PSC regime may be of significant relevance for PPBs.

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[48] *See* Press Release from UK government, available at https://www.gov.uk/government/news/new-review-launches-to-unlock-potential-of-mission-led-businesses.
[49] *Id.*
[50] See UK Government's Call For Evidence, available at https://www.gov.uk/government/consultations/mission-led-business-review-call-for-evidence.

The Social Investment Tax Relief Act has been enacted. It amends the UK tax regime to provide income tax relief at 30% for investments in qualifying social enterprises and certain related reliefs and exemptions from capital gains tax. The Government is in the process of applying for state aid exemption to allow the maximum eligible investment to be increased substantially.

Finally, in its 2015 Budget, the UK Government announced a new Social Venture Capital Trust scheme to encourage investment in companies that invest in social organisations. Investors in a Social VCT will be eligible for income tax relief at 30% of the value of their investment. The regime is not yet enacted in the UK.

UNITED STATES

UNITED STATES

1. Introduction

The legal framework for profit-with-purpose businesses (“PPBs”) in the United States continues to develop, with five additional states and Puerto Rico passing benefit corporation legislation since our last report.[51] Puerto Rico also recently enacted a law to permit companies to organise as low-profit limited liability companies (“L3Cs").[52] Other important legislative developments include amendments to the relevant social enterprise legislation in two key states—Delaware and California. The US Internal Revenue Service ("IRS") has also clarified some of the rules applicable to private foundations that may help to facilitate investments in profit-with-purpose businesses and/or profit-with-purpose businesses organising as L3Cs.

While the movement for legal changes to accommodate profit-with-purpose businesses continues to progress, perhaps the more important developments occurred in the marketplace rather than the statehouse. In 2015, Etsy, Inc., a "certified B Corporation" (a "B Corp") certified by B Lab went public, and Laureate Education, Inc. converted to a Delaware public benefit corporation ("PBC") as part of the company's planned initial public offering ("IPO").[53]

These IPOs have put profit-with-purpose businesses in the spotlight and will test market appetite for equity investments with a triple bottom line. They have also drawn attention to some of the important questions that surround the viability of profit-with-purpose businesses. For example, is having a social mission compatible with the expectations of traditional shareholders? Do new legal forms reflect a company's substantive commitment to a social mission or a more superficial desire for the reputational enhancement that a commitment to a social mission may provide?

2. LEGISLATIVE AND REGULATORY DEVELOPMENTS

2.1 New Statutes for Profit-With-Purpose Businesses

State legislatures have continued to debate and legislate new legal forms for profit-with-purpose businesses. Of the four forms discussed in our last report—the benefit corporation, FPC, special purpose corporation and L3C—the benefit corporation has predominated. 30 states plus the District of Columbia and Puerto Rico now have some form of benefit corporation law. By contrast, L3C legislation has stagnated; only eight states authorise L3Cs and Puerto Rico became the only jurisdiction to enact L3C legislation since 2011.[54] Benefit corporations are also proving to be more popular among founders. Recent estimates indicate that there are over 2100 active benefit corporations in the United States as compared with 1300 L3Cs.[55]

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[51] **Idaho**: Ida. Code § 30-2001 *et seq*.; **Indiana:** Ind. Code § 23-1.3-1-1, *et seq.* **Montana**: Mont. Code Ann. § 35-1-1401 *et seq*; **New Hampshire**: N.H. Rev. Stat. § 293-C:1, *et seq*.; **Tennessee:** Tenn. Code Ann. § 48-28-101, *et seq.*

[52] Puerto Rico amendment to General Corporation Law Act 233-2016; http://www.mcvpr.com/media/publication/437_New%20Types%20of%20Entities.pdf.

[53] Laureate Education's IPO had not completed as of the date of this report.

[54] *See* Elizabeth K. Babson & Robert T. Esposito, Drinker Biddle Client Alert, *The Year in Social Enterprise: 2015 Legislative and Policy Review*, (Feb. 4, 2016) http://www.drinkerbiddle.com/resources/publications/2016/the-year-in-social-enterprise-2015-legislative-and-policy-review.

[55] *See* Ellen Berrey, How Many Benefit Corporations Are There? (May 5, 2015) http://ssrn.com/abstract=2602781 (calculating the number of active benefit corporations in the United States as of April 2015 at 2144); and interSector Partners, L3C,

Of the six jurisdictions that have adopted benefit corporation legislation since the last report, most, with the exception of Tennessee and Puerto Rico, have followed the model benefit corporation law ("MBCL").[56] By contrast, Tennessee and Puerto Rico pursued hybrid approaches, combining elements of the MBCL and the Delaware public benefit corporation statute.[57]

2.2 Amendments to Existing Laws

The new legal forms for profit-with-purpose businesses continue to be refined, even in those states where benefit corporation legislation has already been adopted. Delaware and California have both recently amended legislation governing new corporate forms in important ways.

In October 2014, California amended its "flexible purpose corporation" statute to rename FPCs "social purpose corporations" ("SPCs") and "strengthen the corporation's commitment to its special purpose."[58] In addition to the name change, the amendments to the FPC statute included the following:

- Mandatory consideration of the social purpose: The directors of an SPC are now required to consider all relevant factors in discharging their duties, including the corporation's mission as set forth in its articles.[59] Previously, directors of an FPC had greater flexibility to consider (or not) the mission of the corporation.

- Dissenters' Rights: Dissenters' rights were expanded to include conversions from an SPC to another business entity as well as most mergers involving an SPC in which the SPC does not survive.[60] The FPC statute afforded limited dissenters' rights to shareholders in connection with a change in the special purpose of the FPC or certain conversions or mergers with non-FPCs.

- Supermajority Voting Rights: The SPC law also imposes a mandatory supermajority approval threshold (2/3 of each outstanding class of voting stock) on certain shareholder votes, including the conversion into or out of an SPC,[61] and certain reorganisations involving share consideration.[62] Previously, a corporation could override the supermajority vote requirement for conversions in its articles.

- Reporting: The SPC law eliminated the ability to opt out of the requirement to produce an annual report with a special purpose MD&A section for corporations with fewer than 100 shareholders.[63]

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http://www.intersectorl3c.com/l3c_tally.html (calculating the number of L3Cs as of January 16, 2016, at 1324 (excluding L3Cs formed under the laws of the Oglala Sioux and Navajo tribes, but included those formed under the laws of North Carolina whose L3C statute was subsequently repealed) (last visited Mar. 22, 2016).

[56] Elizabeth K. Babson & Robert T. Esposito, Drinker Biddle Client Alert, *The Year in Social Enterprise: 2015 Legislative and Policy Review*, (Feb. 4, 2016) http://www.drinkerbiddle.com/resources/publications/2016/the-year-in-social-enterprise-2015-legislative-and-policy-review.

[57] *Id.*

[58] California SB 1301 p. 6 http://www.leginfo.ca.gov/pub/13-14/bill/sen/sb_1301-1350/sb_1301_cfa_20140621_181747_asm_comm.html.

[59] *See* Cal. Corp. Code § 2700(c).

[60] *See* Cal. Corp. Code §§ 3200-3201.

[61] Cal. Corp Code §§ 3301-3302.

[62] Cal. Corp Code § 3401(d).

[63] *See* Jeremy Chen, *What is a California Special Purpose Corporation?* http://jeremychenlaw.com/what-is-a-california-social-purpose-corporation/ (last visited Mar. 22, 2016).

By contrast, the amendment to Delaware's "public benefit corporation" ("PBC") statute had the opposite effect: relaxing certain of the rules applicable to PBCs. These include:

- Conversion: The approval threshold to convert into or out of a PBC was lowered from 90% of all classes of stock to 66 2/3% of the outstanding shares of each class of voting stock.

- Dissenters' Rights: The Delaware law generally provides for dissenters' rights in connection with the conversion into or out of a PBC and in connection with a merger with a non-PBC entity. As a result of the amendment, Dissenters' rights are no longer available for shareholders of PBCs whose stock has a liquid market, and, in connection with a merger, if the consideration received is either cash or shares for which there is also a liquid market.

2.3 Taxation of Private Foundations

The Internal Revenue Code ("IRC") generally imposes an excise tax on investments made by private foundations if the investment jeopardises its ability to carry out its mission(s).[64] The IRC exempts from this excise tax investments that further the mission of the private foundation and where no significant purpose of the investment is the production of income or appreciation of property,[65] so a private foundation may not have been able to rely on this exemption to invest in a profit-with-purpose business.

In September 2015, the IRS issued guidance to private foundations regarding the sorts of investments that could trigger an excise tax under the US Internal Revenue Code ("IRC") by clarifying the extent to which an investment would be considered a "jeopardizing investment" for purposes of determining whether it would trigger the excise tax.[66] It is now clear that managers of private foundations who do not select investments purely on the basis of financial metrics but also consider the foundation's mission in selecting investments (so-called "Mission-Related Investments" or "MRIs") are not making jeopardising investments if they exercise ordinary care and prudence in doing so. "For example, a private foundation will not be subject to tax under section 4944 if foundation managers who have exercised ordinary business care and prudence make an investment that furthers the foundation's charitable purposes at an expected rate of return that is less than what the foundation might obtain from an investment that is unrelated to its charitable purposes."[67]

While some private foundation managers have been making MRIs without the benefit of formal guidance[68], this clarification may help promote investment in profit-with-purpose businesses and may make it easier for such businesses to raise capital from the foundation community. Encouragingly, it also suggests that the traditional view of profit and purpose as antagonists may be eroding.

3. Significant Transactions

The last 12 months have also seen interesting developments in the IPO market for profit-with-purpose businesses. In April 2015, Etsy, the online marketplace for vintage and

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[64] IRC §4944(a)(1).
[65] *See* IRC §4944(c).
[66] *See* IRS Notice 2015-62 https://www.irs.gov/pub/irs-drop/n-15-62.pdf.
[67] *Id.*
[68] *See* Celia Roady & Matthew R. Elkin, *IRS Provides Guidance on Mission-Realted Investments by Private Foundations*, (Sept. 29, 2015) https://www.morganlewis.com/pubs/irs-provides-guidance-on-mission-related-investments-by-private-foundations.

handmade goods, went public as B Corp, but did not convert from a traditional corporation into a benefit corporation. Then in October, a private-equity backed network of for-profit colleges and universities, Laureate Education, converted to a Delaware PBC in connection with a planned IPO. It is unclear at the publication of this update how, and whether, either Etsy or Laureate Education will impact the behaviour of PPBs that seek to take advantage of traditional capital market transactions.

4. Conclusion

Despite these developments, profit-with-purpose companies nonetheless remain largely untested. There have not yet been any court rulings interpreting any of the various statutes governing profit-with-purpose entities and M&A activity has been limited. As more companies adopt these forms, however, questions that remain about the legal and commercial viability of these forms will hopefully be answered. Regardless of success of the new legal forms, these changes suggest that corporate law is moving beyond a binary view of the corporate mandate as either profits or purpose to a recognition that profits and purpose can coexist and possibly enhance one another.