COMMENTS BY THE EUROPEAN CENTER FOR NOT-FOR-PROFIT LAW TO DRAFT LAW AMENDMENTS ON SOCIAL ENTERPRISES IN MOLDOVA

The European Center for Not-for-Profit Law (ECNL)[1] is pleased to have an opportunity to provide its comments to the Moldovan draft Law Amendments on Social Enterprises, version as of January 29, 2016 (hereinafter: "*Draft Law Amendments*"). We would like to commend the work of the Social Enterprise Platform that developed the Draft Law Amendments in a highly participatory manner.

The comments provided in the present document are based on European best practices, with special regard to the examples of France, Italy, Lithuania, Slovenia and Spain. The document does not intend to be exhaustive, but rather to highlight priority issues.

The comments are divided into two parts:

1) General comments that highlight the European best practices and the main, conceptual issues; and
2) Detailed comments and recommendations on how to further improve the Draft Law Amendments.

The comments were prepared within the Moldova Partnerships for Sustainable Civil Society Program (MPSCS) implemented by FHI 360 and ECNL.[2] ECNL remains committed to provide further support to local stakeholders in the process of developing a legal framework for social entrepreneurship. For additional information on the European regulatory models for social entrepreneurship, the drafters may also consult ECNL's *Comparative analysis of the Regulatory Framework for Social Enterprises.*

I. GENERAL COMMENTS

Social enterprises combine the tools and strategies of a business with social values and goals. Their increasing economic and social value was endorsed by various international and European bodies and organizations. At the EU level, the European Commission launched a project called *Social Business Initiative* to support the creation of social enterprises. The initiative is organized around 3 main objectives:

1) ***Make it easier for social enterprises to obtain funding***
2) ***Increase the visibility of social entrepreneurship***
3) ***Make the legal environment friendlier for social enterprises***

The efforts of the European Commission were endorsed also by the European Economic and Social Committee ("EESC"). In its Communication No. (2011) 682 the EESC[3] *"considers that social enterprises should be supported by virtue of the key role that they can play as drivers of social innovation, both*

[1] The European Center for Not-for-Profit Law (ECNL) is a leading European resource and research center in the field of policies and laws affecting civil society. Its mission is to promote an enabling legal and fiscal environment for civil society in Europe and beyond. ECNL has demonstrated deep commitment to empower civil society organizations and ensure their sustainability. ECNL staff has more than 10 years of experience in promoting CSO law reform in the following regions: Western Europe and European Union; new EU member states; Newly Independent States (Armenia, Azerbaijan, Georgia, Moldova, Ukraine); Western Balkans and Turkey.

[2] These comments were made possible by the generous support of the American people through the United States Agency for International Development (USAID). The contents are the responsibility of the authors and do not necessarily reflect the views of USAID or the United States Government.

[3] Available at: http://www.eesc.europa.eu/?i=portal.en.int-opinions.20965.

because they introduce new methods for providing services and measures aimed at improving people's quality of life, and because they promote the creation of new products to satisfy society's new needs." In addition, the EESC emphasizes that "*a favorable economic and regulatory environment is essential for the promotion of social enterprises."*

In August, 2014, the Republic of Moldova concluded an Association Agreement with the European Union and the European Atomic Energy Community and their Member States.[4] Article 63 of this Agreement provides an obligation for the parties to implement strategies for the small medium enterprise ("SME") development, based on the principles of the Small Business Act for Europe.[5] The Small Business Act recognizes "social economy" organizations as special category of SMEs that include non-profit associations, foundations, co-operatives, mutual societies and similar legal forms. The Act under point 3.4. further emphasizes that: *"In order to respond to the particular needs of these undertakings, the Commission announced in the Single Market Act a number of actions that will provide a level playing field. These actions would address issues related to cooperatives, foundations and mutuals on the one hand and enterprises pursuing social objectives on the other."*

The scope and content of the social entrepreneurship regulation depends on the objective of the regulation and target group it aims to promote. If the law aims to recognize and encourage the growth of social entrepreneurship as such, it is essential to make sure the definition and criteria are not overly narrow. Also, such regulation should provide very simple and straightforward rules to start up and build a social enterprise.

In light of the European good practices in regulation of social entrepreneurship, we **welcome the following positive aspects and developments of the Draft Law Amendments:**

- The Draft Law Amendments for the first time establish a legal framework for social entrepreneurship in Moldova;
- The Draft Law Amendments recognize two types of social enterprises: general ones pursing social goals and integration social enterprises;
- The Draft Law Amendments provide tax and other benefits for organizations engaged in social entrepreneurship.

We would also like to suggest following issues for further discussion:

- The Draft Law Amendments define a relatively narrow scope of social entrepreneurship: they limit the possibility for CSOs without a public utility status and businesses/corporations established by individuals, CSOs without a public utility status to carry out social entrepreneurship activities under the Draft Law Amendments;
- The list of social entrepreneurship activities is narrow and does not recognize other socially useful activities;
- The procedure for granting social enterprise status may limit the expansion of social entrepreneurship.

[4] Available at: http://eeas.europa.eu/delegations/moldova/documents/eu_moldova/eu_-_moldova_association_ageement.pdf
[5] Available at: http://eur-lex.europa.eu/legal-content/EN/ALL/?uri=celex:52011DC0078

II. SPECIFIC COMMENTS AND RECOMMENDATIONS

- **SCOPE OF ELIGIBLE ORGANIZATIONS TO CARRY OUT SOCIAL ENTREPRENEURSHIP**

Issue: According to the Article I. point 1[1] of the Draft Law Amendments, social entrepreneurship is carried out either by a public utility civic association and foundation or a business company and cooperative founded by them. This regulation limits the possibility of CSOs without a public utility status and businesses/corporations established by individuals, CSOs without a public utility status and companies to carry out social entrepreneurship activities under the Draft Law Amendments.

Discussion: Article I. point 1[1] of the Draft Law Amendments defines social entrepreneurship as "*the entrepreneurial activity carried out by a* ***social enterprise, by a public utility civic association or foundation*** *in view of reaching social or community objectives such as strengthening economic and social cohesion at the level of social communities, employment, and developing social services."* The point 2[1] further defines the social enterprise as "***a business company or cooperative, founded by a civic association or foundation having the public utility status***." Based on this regulation, the scope of eligible organizations that may conduct social entrepreneurship activities under the draft Law amendments is limited to associations and foundations with public utility status and business companies and cooperative founded by CSOs with public utility status.

Social entrepreneurship is generally based on the principle of combining the social purpose with entrepreneurial spirit in the organization, while the legal form of social enterprises has a secondary nature. In many European countries**, organizations with a variety of legal forms may carry out social entrepreneurship activities**. Besides associations and foundations with public utility status, **other nonprofit legal forms**, such as centers (e.g. Poland, Spain) and institutes (e.g. Czech Republic, Slovenia), may engage in social entrepreneurship.

Organizations without a public benefit, public utility or charity status in countries where such distinct status exists may operate as social enterprises, too. While in many countries public utility organizations can obtain social enterprise status (Slovenia, Spain, Italy) we are not aware of any country where public utility status would be a precondition to become a social enterprise. These are two different concepts that may overlap but do not substitute each other.

Mixed or for-profit organizations are typically allowed to carry out social entrepreneurship activities, too, provided they abide by special social, economic and governance criteria. These include, for example, cooperatives and share companies, **regardless of the founding individual and/or legal entity**. Cooperatives/social cooperatives exist, for example, in Croatia, Slovenia, Italy, Poland and Spain. Share companies can be social enterprises, for example, in France, Lithuania, Slovenia and Sweden.

The Draft Law Amendments also limit **individuals that are not yet institutionalized** to engage in social entrepreneurship. For example, if a group of individuals decides to carry out social entrepreneurship activities in accordance with these Draft Law Amendments, they would have to either:

1. Found an association or foundation and get a public utility status; or
2. Found an association or foundation, get the public utility status, found a business company or cooperative and get a social enterprise status.

In addition, if a group of individuals wants to found an integration social enterprise, they will have to always choose the second option as the Draft Law Amendments allow only business companies and

cooperatives to operate as integration social enterprises. This seems to be a long procedure that does not necessarily encourage the creation of new social enterprises.

Recommendation: We recommend the drafters to expand the scope of eligible organizations to all non-profit legal forms, including those that do not have public utility status. This applies also to the integration social enterprises. In addition, we recommend to allow all individuals and legal entities to found business companies and cooperatives carrying out social entrepreneurship activities.

- **LIST OF ALLOWED ACTIVITIES**

Issue: The Draft Law Amendments in Article I. point 1[2] define a relatively narrow scope of social entrepreneurship activities.

Discussion: The Article I. point 1[2] lists following activities to represent social entrepreneurship activities:

1) *"Promotion of active measures for stimulating the employment of persons from the disfavored categories of the population;*
2) *Creation of job and employment, on a priority basis, of persons from the disfavored categories of the population;*
3) *Provision and development of social services;*
4) *Promotion of environment protection activities at the level of local communities."*

While this scope recognizes the most typical activities of social enterprises, it may not follow new trends and provide enough flexibility for innovative social entrepreneurs. There are many activities that are socially useful but do not fall within any of the above categories. For example, promotion and sale of the fair trade products, which may have a strong social and economic impact, would not qualify as a social entrepreneurship activity. Similarly, an initiative to organize small cultural events at a local level would not be considered as a social entrepreneurship either, despite of the social value they may have for the community.

In many European Union countries, the scope of activities goes beyond the social service provision or social and economic integration of disadvantaged. Social enterprises engage in a broad range of areas provided they strengthen the social and economic cohesion. In addition to activities included in the Draft Law Amendments, following ones are recognized in other European countries:

- ***Public services***, e.g. maintenance of public spaces, transport services;
- ***Culture and national heritage,*** e.g. culture, technical culture and preservation of cultural, technical and natural heritage, enhancement of cultural heritage;
- ***Land-based industries and the environment,*** e.g. promoting the use of renewable energy and green economy, reducing emissions and waste, recycling, renewable energy;
- ***Other social and community services,*** e.g. counselling, youth outreach, micro finance, temporary housing for homeless;
- ***Education,*** e.g. University and post-graduate education, extra- school education or the prevention of early school leaving and the school and educational success, research*;*
- ***Tourism, sport and recreational activities***; e.g. social tourism;
- ***Practising solidarity with developing countries***, e.g. promoting fair trade.

European practices show that there are various policy solutions on how the activity areas of social enterprises can be regulated. As an example:

1. <u>The law may regulate the list of areas through an enumerative list:</u>

For example, the Legislative Decree of 24 March 2006, n. 155 in **Italy**[6] provides in Article 2 following list of areas: *a) social assistance; b) health care; c) social care; d) education and training; e) protection of the environment and the ecosystem; f) enhancement of cultural heritage; g) social tourism; h) university and post-graduate education; i) research and provision of cultural services; l) Extra-school education, for the prevention of early school leaving and the school and educational success; m) instrumental services to social enterprises.*

In addition, the following paragraph provides an exception for the integration social enterprises. It stipulates that "*regardless of the exercise of business activities in the areas referred to in paragraph 1, organizations may acquire the status of a social enterprise if they operate a business for the labour insertion of individuals who have: a) disadvantaged workers b) disabled workers.*"[7]

The Law on Social Entrepreneurship in **Slovenia**, Official Gazette of RS, no. 20/2011[8] lists the following areas of activity (Article 5): *a) Social security; b) Family protection; c) Protection of persons with disabilities; d)Science, research, education and upbringing; d) Providing and organizing youth work; e) Protection and promotion of health, f) Ensuring social inclusion, promotion of employment and vocational training for persons who are unemployed or threatened by unemployment; g) The provision of employment to persons referred to in Article 6 of this Law, including the activity of the work of such workers to other employers; h) Organic food production; i) Conservation, management and protection of the environment and animal welfare, j) Promoting the use of renewable energy sources and the development of green economy; k) Tourism for persons to whom life conditions prevent or hinder access to tourist services, in a way that respects the values of sustainability, accessibility and solidarity (social tourism) l) fair trade and trade in services and products from the activities of social entrepreneurship; m) Culture, technical culture and preservation of cultural, technical and natural heritage; n) Amateur sport and physical culture, whose purpose is recreation and socialization; o) Rescue and protection; p) Encouraging the development of local communities; q) Support services for social enterprises.*

Similarily as in Italy, Slovenian Law on Social Entrepreneurship provides an exception from the list of activities for the social enterprises employing the most disadvantaged groups in the labour market pursuant to Commission Regulation (EC) No 800/2008 of 6 August 2008.

2. <u>The law may provide a general definition and regulate the scope of activities that cannot be carried out by social enterprises:</u>

For example, the **Lithuanian** Decree No. 1501 of 29 November 2004[9] on the approval of a List of non-supported activities of the social enterprises defines the following activities as non-supported:
1. Tobacco Growing; 2. Hunting, trapping and related service activities; 3. Mining and quarrying; 4. Manufacture of beverages, with the exception of non-alcoholic beverage; mineral waters and other bottled water; 5. Tobacco products; 6. Manufacture of coke and refined petroleum products; 7. Other basic organic chemicals; 8. Processing of nuclear fuel; 9. Ships and floating structures; 10. Various types

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[6] Available at: http://www.camera.it/parlam/leggi/deleghe/06155dl.htm.
[7] **Disadvantaged workers** as defined in Article 2, first paragraph 1, letter f) , i), ix) and x) of Regulation (EC) No. 2204/2002 of 5 December 2002 on the application of Articles 87 and 88 of the EC Treaty to State aid for employment; **disabled workers** under Article 2, first paragraph 1, letter g) of the Regulation (EC) No. 2204/2002.
[8] Available at: http://www.mddsz.gov.si/fileadmin/mddsz.gov.si/pageuploads/dokumenti__pdf/zaposlovanje/Act_SE_rev_clear.pdf.
[9] Available at: https://www.e-tar.lt/portal/lt/legalAct/83cdeaf0a7f311e5be7fbe3f919a1ebe.

of ship repair and maintenance; 11. Aircraft and aerospace repair and maintenance; 12 cranes and other construction equipment, which cannot be attributed specifically to the construction field, with operator renting; 13. Wholesale and retail trade; repair of motor vehicles and motorcycles with the exception of motor vehicle maintenance and repair and retail sale of second-hand goods in stores; 14. Transportation and storage with the exception of the postal and courier (courier) activity; 15. Beverage serving activities; 16. Programming and broadcasting; 17. Telecommunications; 18. Financial and insurance activities; 19. Real estate activities; 20. Legal activities; 21. Rental and leasing; 22. Security and investigation activities; 23. Public administration and defense; compulsory social security; 24. Gambling and betting activities; 25. Other service activities with the exception of computers and personal and household goods; other personal service activities; 26. The extra-territorial organizations and bodies.

All the other activities outside of this list may be carried out by social enterprises.

Recommendation: We would recommend the drafters to expand the list of social entrepreneurship activities. If the drafters prefer the policy solution No. 1, they may want to consider including to the list, for example: (1) preservation of cultural, technical and national heritage, (2) extra- school education, (3) public services and maintenance of public spaces, (4) tourism and sport with the recreation and socialization purpose and (5) practicing solidarity with developing countries. In addition, the drafters may want to consider defining the environmental protection in a broader sense and do not limit it to the local level. For example, they may define it as a protection of the environment, ecosystem and animal welfare.

- **CONCEPT OF SOCIAL ENTREPRENEURSHIP**

Issue: The Draft Law Amendments do not provide enough clarity when defining the concept of social entrepreneurship.

Discussion: Social enterprises may be nonprofit organizations that apply business models to accomplish their mission as well as business organizations that aim to achieve a significant social impact besides generating profit. In many European countries as well as at the EU level, the term "social enterprise" refers to all organizations engaged in social entrepreneurship activities, regardless of their legal form. According to the Article I. point 2^1 of the Draft Law Amendments, **the term "social enterprise" refers solely to business companies and cooperatives that are founded by public utility associations and foundations.** In other words, according to this amendment to the Law on Entrepreneurship and Enterprises, the public utility associations and foundations are not social enterprises per se. We recognize that Article II. point 6 provides that *"the public utility civic association that carries out social entrepreneurship is assimilated to a social enterprise or an insertion social enterprise, as applicable, if it meets the conditions set out in para. (4) or para.(5)"*. However, it is not clear from this provision whether they will become social enterprises as per definition in the Article I. point 2^1 of the Draft Law Amendments. Hence, **it does not help to provide a clear picture of the scope of organizations that are social enterprises under the Draft Law Amendments**. Also, the fact that criteria for social enterprises are included in the Law on Associations, while the definition is in the Law on Entrepreneurship and Enterprises may create challenging situations in practice. It would be useful to incorporate both the definition and the criteria to the same regulation.

One of the added value of the social enterprise regulation is **an easier identification of organizations operating as social enterprises.** This is particularly relevant in case the state provides direct and indirect benefits for social enterprises. The current wording of the Draft Law Amendments may create confusion, in particular to distinguish the public utility associations and foundations that carry out social entrepreneurship from those that do not.

In addition, Article II. point 5 regulates the requirements for the integration social enterprises. Letter a) of this Article stipulates that an integration social enterprise shall: "*Permanently have at least 30% of staff hired from the disfavored categories of the population, so that the cumulated working time of such staff represents at least 30% of the total working time of all members of the staff*". As we understood, the definition is provided in the Law on Social Welfare No. 547 of 25 December, 2003. However, for the sake of clarity, we suggest to include the definition also to the Draft Law Amendments or at least give a specific reference to the Social Welfare Law. As described above, such reference included both Slovenian and Italian social enterprise regulations.

Recommendation: The drafters may want to review the terminology used in the Draft Law Amendments and: (1) consider naming all organizations that carry out social entrepreneurship activities "social enterprises"; (2) include definition and qualification criteria for social enterprises to one legal act; (3) provide/refer to a definition of disfavored groups.

- **QUALIFICATION CRITERIA FOR CARRYING OUT SOCIAL ENTREPRENEURSHIP**

Issue: The Draft Law Amendments provide the same qualification requirements for all types of organizations, which puts some of them into a disadvantaged position.

Discussion: Article II. point 4 and 5 of the Draft Law Amendments provide qualification requirements for the social enterprises. According to the point 6 of the same Article, public utility civic associations and foundations carrying out social entrepreneurship are assimilated to social enterprises **provided they meet the same conditions as business companies and cooperatives**. We understand the intention of drafters to introduce a comprehensive approach towards social entrepreneurship and apply the same criteria for all types of organizations. However**, having equal conditions for all legal forms may actually put some of them into a disadvantaged position.** According to the Article II. point 4 of the Draft Law Amendments one of the criteria for social enterprises is that "*at least 50% of their income comes from entrepreneurship activities.*" While it is evident that business companies and cooperatives generate income mainly from entrepreneurship activities, it may be complicated for CSOs and particularly for those with public utility status to meet this criteria. On the other hand, all nonprofit organizations have to meet the requirement to "*reinvest 90% of their profit into reaching the objectives of the areas expressly stipulated in their constituent acts.*" Hence, having such criteria for CSOs carrying social entrepreneurship is redundant.

Recommendation: The drafters may want to revise the criteria for social enterprises and apply them in accordance with a legal form in question.

- **PROCEDURE FOR GRANTING SOCIAL ENTERPRISE STATUS**

Issue: Article I. point 2[1] refers to the legislation on civic associations and foundations for the procedure on granting the status of social enterprise. The rules for this procedure are, however, unclear and the whole process may be much simpler to provide legal predictability to the applicants.

Discussion: Article I. point 21 and Article II. regulate the procedure for granting the social enterprise status and qualification requirements. The Draft Law Amendments include some general provisions, however, they do not provide clear guidance on which documents an applicant has to submit to prove that the qualification requirements were met. We understand that there will a bylaw adopted to further regulate this procedure, however, as a matter of good practice **the law provides at least a list of documents that the applicant has to submit.** The regulation should take into account that also newly established organizations may apply for the status and accommodate the list of documents to this situation. For example, according to the Law on Social Entrepreneurship in Slovenia, the articles of

association shall prove that the applicant complies with the qualification requirements for a status. The registration authority should verify that the memorandum or the articles of an association of a non-profit legal entity includes all the obligatory qualification requirements for social enterprise. These are, for example, equitable management of the social enterprise, principles of participatory governance and utilization of the assets after its dissolution (Article 12 of the Law on Social Entrepreneurship). In addition, according to Article 24 of this Law, the application shall also include:

- *"a decision by the founders or competent body of a non-profit legal entity to operate as a social enterprise;*
- *the names, personal registration numbers, nationality and permanent or temporary addresses of all authorized representatives and the scope of powers for societies;*
- *evidence of the potential sum for the commencement of the operation or the value of the society's assets."*

According to Article II. Point 7 of the Draft Law Amendments, **social enterprise status is granted for a definite period** of 5 years. This may be challenging because of two reasons: (1) the public utility status for associations and foundations is granted only for a 3-years period and the loss of such status by a founding organization may have an impact on a social enterprise status, too; (2) there is a risk that a social enterprise will have to interrupt or terminate its operation because of the re-application procedure.

In order to prevent these situations, the drafters may want to consider providing status of a social enterprise for an indefinite period. The social enterprise status is granted for an indefinite period for example in Slovenia, Italy and Denmark. Instead of re-application for the social enterprise status, the organizations submit annual or bi-annual activity and finance report to prove that they still meet the legal requirements.

Drafters may also want to **simplify the granting of the social enterprise status.** If there are clear criteria upon which the status is granted, there is no need to have a special committee to certify that the conditions were met. For example in Denmark, the Danish Business Authority verifies the documents filed by the organization and grants the status.[10] Similarly, in Slovenia, the registration authority verifies the memorandum of articles of the organization together with the application form and grants the status.

Recommendation: We recommend the drafters to review the procedure for granting the social enterprise status and simplify the rules, particularly with regard to the: (1) list of documents to be submitted by an applicant; (2) period for which the status is granted; (3) and registration authority.

- **BENEFITS FOR ORGANIZATIONS CARRYING OUT SOCIAL ENTREPRENEURSHIP**

Issue: The Draft Law Amendments propose tax exemptions to the social enterprises and benefits related to the public procurement. However, there are also other means of support that the drafters may want to take into consideration.

Discussion: The Draft Law Amendments provide certain benefits to organizations with social enterprise status. These include tax exemption on the income tax and preferential rules for the public procurement. From the comparative perspective there are also other direct and indirect benefits available for social enterprise, provided proportionately with additional requirements.

[10] Act on Registered Social Enterprises, available at: https://www.retsinformation.dk/forms/r0710.aspx?id=163865.

For example, integration social enterprises are typically provided with a range of **direct state support**. In Lithuania, all legally recognized integration social enterprises have:

- partial compensation for wages and state social insurance contributions;
- grants for creation of jobs, adaptation of workplaces for the disabled, and acquisition/adaptation of means of work for the disabled;
- grants for training of target groups.[11]

The Law also provides additional benefits to the integration social enterprises employing persons with disabilities.

In France, there are several **public support schemes** towards social entrepreneurship. They are often complemented by the support from the EU funds and social investment measures taken by the governments. The examples include Caisse des Dépôts and its branches and Future Investments Programme, both are described in a detail in the ECNL Comparative Analysis attached to these comments.

In many European countries, there is also an **institutional support** provided for the social enterprises. For example, in France[12], Slovenia and Spain[13], the laws establish councils for the support and promotion of the social economy. The councils may have diverse responsibilities, including preparation of the national development strategies for the social entrepreneurship, providing regular trainings and consultancy services and negotiate actual modalities of the legal regulation.

Recommendation: The drafters may want to consider including more benefits/support schemes to the Draft Law Amendments.

[11] Article 13 of the Law on Social Enterprises
[12] Law on Social and Solidary Economy No. 2014-856 of 31 July 2014, available at: https://www.legifrance.gouv.fr/affichTexte.do?cidTexte=JORFTEXT000029313296&categorieLien=id.
[13] Law on Social Economy No. 5/2011 from 9 March, available at: https://www.boe.es/boe/dias/2011/03/30/pdfs/BOE-A-2011-5708.pdf