Co-funded by the European Union

# STARTUP ACTS

## AN EMERGING INSTRUMENT TO FOSTER THE DEVELOPMENT OF INNOVATIVE HIGH-GROWTH FIRMS

**ICREPORT**

September 2021

ICREPORT IN THE SERIES ON INNOVATIVE FINANCE

Implemented by

# TABLE OF CONTENTS

# STARTUP ACTS:

## AN EMERGING INSTRUMENT TO FOSTER THE DEVELOPMENT OF INNOVATIVE HIGH-GROWTH FIRMS

## EXECUTIVE SUMMARY

Startup Acts are emerging and comprehensive legal instruments aimed at fostering the creation and development of startups, taking into account their particular needs. They are often designed through a participatory process involving the collaboration of different stakeholders in the entrepreneurship ecosystem. Although Startup Acts are still relatively new, if well designed, they can have a significant impact on improving private sector development and tackling high unemployment rates and economic gloom.

## KEY FINDINGS

- Startup Acts provide startups with targeted incentives aimed at addressing the challenges they face.
- In designing Startup Acts, policymakers should pay special attention to the importance of adopting a participatory process, an ecosystem approach as well as a clear and objective selection process to target beneficiaries.
- Besides Tunisia and Senegal, which adopted a Startup Act respectively in 2018 and 2019, at least 16 more African countries are in the process of adopting one.
- Startup Acts are often designed through a participatory process involving the collaboration of stakeholders from the entrepreneurship ecosystem from both public and private sectors.

# BACKGROUND

Governments have increasingly begun to focus on entrepreneurship as a mean of creating quality jobs, boosting the wider economy's productivity and delivering market-based innovations to development challenges. In this context, Startup Acts can be a new tool for addressing the specific challenges faced by businesses with high potential for growth and innovation. This instrument can also be used to foster public and private dialogue trough participatory processes and to reflect on general entrepreneurship policy reforms.

The objective of this report is to provide an introduction to Startup Acts and to allow a better understanding of their characteristics and potential. This report was preceded by a webinar organised in April 2021 by the ICR Facility, which brought together entrepreneurship experts and policy makers engaged in Startup Act design processes.

The report starts by defining the key characteristics of start-ups and Startup Acts, then presents a general overview of the adoption of Startup Acts and highlights the characteristics of the Italian, Senegalese and Tunisian Startup Acts and finally, provides recommendations for policy makers on the design and implementation of Startup Acts.

## KEY DEFINITIONS

**Startups are generally defined as companies in their first stage of operations with the ability to scale and grow rapidly.** Scalability is the characteristic of a system, model, or function that describes its capability to cope and perform under an increasing or expanding workload. According to the European Economic and Social Committee (2017)[1] 'all startups are SMEs, but not all SMEs are startups due to differences in set-up and vision [...] Moreover, the initial capital required to grow the business is commonly much higher (sometimes in the order of millions) for a startup than for SMEs in general'.

**Startup Acts are comprehensive legislative and regulatory frameworks aimed at fostering entrepreneurship and enabling the development of new firms with high growth potential** generally through the granting of targeted incentives (tax, subsidies, procurement, etc.).

Startup Acts have the particularity of often being designed through a participatory and frequently innovative process involving the collaboration of public and private stakeholders in the entrepreneurship ecosystem.

1 Comité économique social européen, 2017. « Study on the Assessment of the Effectiveness of the EU SME Policies 2007-2015 ». Bruxelles : Commission européenne.

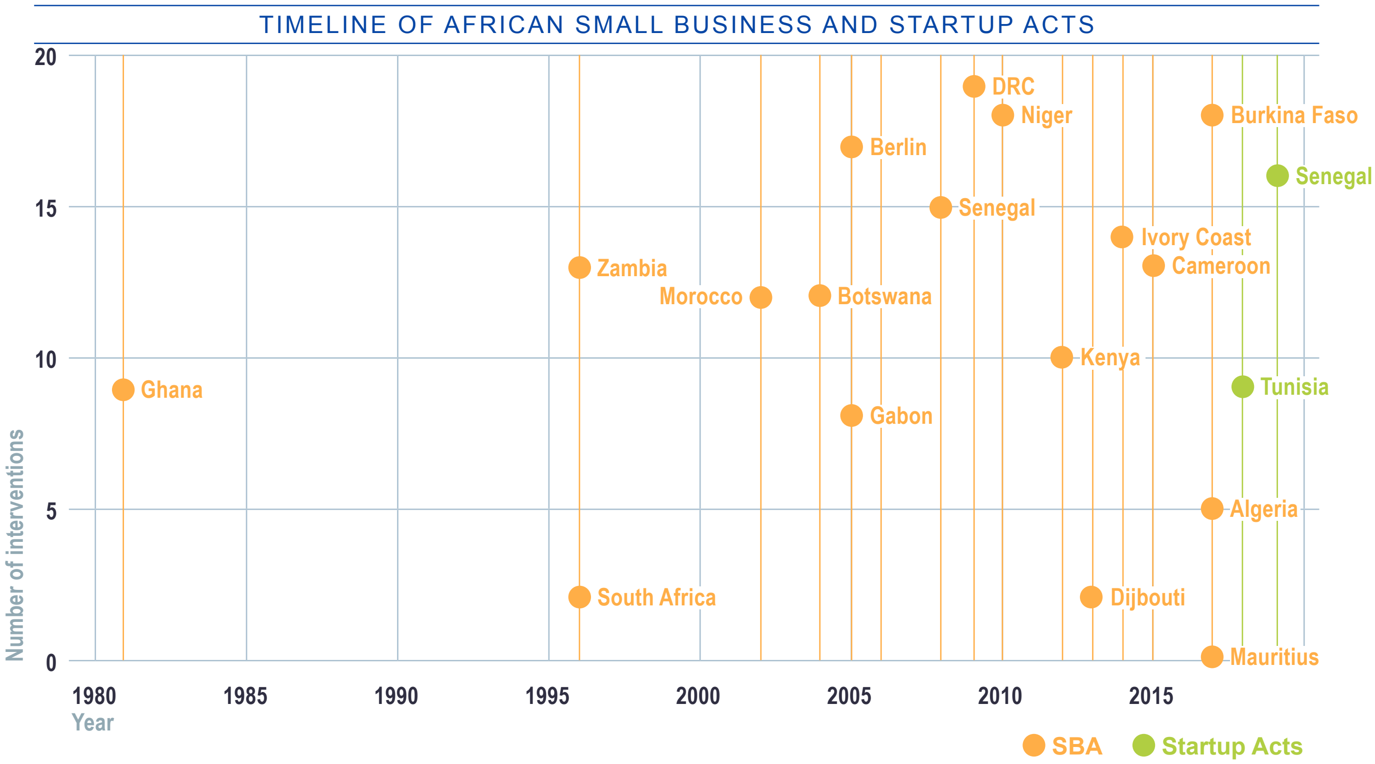
# OVERVIEW OF THE ADOPTION OF SMALL BUSINESS ACTS AND STARTUP ACTS

## SMALL BUSINESS ACTS

Most ACP countries[2] have focused first on creating specific legislation to support SMEs through Small Business Act (SBAs) before becoming interested in startups. SBAs are legislative instruments, with a transversal scope, aiming to boost the creation and development of small businesses. SBAs generally adopt a traditional classification of firms, based mostly on their size, on the grounds that these firms are disadvantaged due to their limited scale.

In Africa, for instance, there was a transition from, historically, focusing on small business policies to, recently, exploring the adoption of policies aimed at fostering the development of startups ((see *figure 1* below). The first Small Business Acts on the African continent were adopted between the 1980s and the 1990s: the Ghanaian National Board for Small-scale Industries Act (1981), the Zambian Small Enterprises Development Act (1996) and the South African National Small Business Act (1996). Since the 2000s, 15 other African countries have adopted regulations to promote and support the development of small and medium businesses.

### FIGURE 1: Timeline of SBA and Startup Acts in 19 African countries




*Source* : i4Policy Process v3.1, Innovation for Policy Foundation cc-by-sa

2 Countries members of the Organisation of African, Caribbean and Pacific States

## STARTUP ACTS

Historically, the first growth entrepreneurship policies appeared in the early 1990s in countries such as Finland, the Netherlands and Scotland. Since then, many countries have adopted policy measures specifically targeting startups, but these measures are often limited or isolated.

In Europe, for example, most countries have some measures specifically aimed at startups, without these measures being part of a broader legislative framework. For instance, in 2004 France introduced a tax break for young innovative companies (*Jeunes Entreprises Innovantes*) and offers ad hoc programmes to support companies that have the potential to become startups. In the United States, in the framework of the Startup America initiative, the federal government implemented a set of entrepreneur-focused policy initiatives in five areas: reducing barriers, unlocking access to capital, connecting mentors, accelerating commercialisation of research, and unleashing new market opportunities for entrepreneurs. In Asia, India and Israel stand out for having a broad policy strategy targeting startups with a combination of policies, programmes and legislative amendments to the classic entrepreneurship regulatory framework.

In Pacific and Caribbean countries, according to the World Bank's *Doing Business* report, starting a business has become much easier in recent years and some countries have adopted regulations specifically targeting startups. For instance, Jamaica has sought to attract innovative and high value investments through its Income Tax Relief (Large Scale Projects and Pioneer Industries) Act, 2013. However, those policies cannot necessarily be defined as Startup Acts.

As mentioned above, a Startup Act is a comprehensive targeted legislative framework codified in one main instrument, that is often complemented with other regulations, policies and programmes. Having most provisions in one main document make it easier for the firms to be aware of the benefits they may be granted. Also, Startup Acts are passed through bills of parliament or ministerial decrees and therefore, are more significant than simple policies. Moreover, when they have been adopted through a participatory process involving grassroot entrepreneurs, this can impulse a positive dynamic at national level and boost investors' trust.

The adoption of disparate, limited or isolated legal instruments for startups is not enough to qualify as a Startup Act. As a result, to date, there are very few countries in the world that are considered to have adopted a Startup Act. Without claiming to be exhaustive, we have identified only the following countries: Argentina,[3] the Philippines,[4] Italy,[5] Tunisia[6] and Senegal.[7]

Many other countries however, particularly in Africa (e.g. Mali, Kenya, Benin, DRC, Ghana, Togo, …), are interested in adopting a Startup Act and, to that end, have started to stimulate participatory stakeholder design processes.

The timeline *on the previous page* illustrates the adoption of SBA and Startup Acts over time in 19 African countries.

## WHY ADOPT A STARTUP ACT IN ACP COUNTRIES?

ACP countries need to continue pursuing policy and regulatory reforms that support their efforts to achieve sustainable and inclusive growth that demand innovative solutions. In this context, governments have increasingly begun to focus on entrepreneurship as a means of creating quality jobs, boosting the wider economy's productivity and growth, and delivering market-based innovations to development challenges. In fact, a study on the role of entrepreneurship and its benefits found that entrepreneurship has a significant long-term effect on productivity growth. Hence, entrepreneurship can be seen as a key driver for long-term economic growth.[8]

3 Argentina : *Ley 27349, Apoyo al capital emprendedor,* 29 March 2017.

4 Philippines: Republic Act NO. 11337, known as the "Innovative Startup Act", approved on April 26, 2019.

5 Italy: Decree-Law no. 179 of 18 October 2012 (the so-called "Italian Startup Act"); Decree-Law no. 3 of 24 January 2015; Law no. 232 of 11 December 2016 (2017 Budget Law); Law no. 145 of 30 December 2018 (2019 Budget Law); the National Plan for Industry 4.0 (from 2017 to 2019).

6 Tunisia: Law N°2018-20 of 17 April 2018 relating to Startups; Decree N°2018-840 of 11 October 2018 setting the conditions, procedures and deadlines for granting and withdrawing the startup label and the benefit of incentives and advantages under Startups and the organisation, prerogatives and modalities of operation of the Labelling Committee; Circulars of the Central Bank of Tunisia N°2019-01 and 2019-02.

7 Senegal: Law n°2020-01 of 6 January 2020 relating to the creation and promotion of Startups in Senegal.

8 Erken, H., Donselaar, P. & Thurik, R. "Total factor productivity and the role of entrepreneurship". J Technol Transf 43, 1493–1521 (2018). *https://doi.org/10.1007/s10961-016-9504-5*. Total factor productivity measures how much output can be produced from a certain number of inputs and is therefore usually seen as a proxy for productivity growth and innovation.

The full potential of entrepreneurship is often left untapped. This is due to the existence of a number of constraints on the business environment that hamper the development of the private sector, including unfavorable legal and regulatory frameworks, underdeveloped infrastructure, lack of business development services, limited access to finance, limited supply of skilled labor, and weak cultural support, among other barriers, which tend to affect SMEs and startups even more than large, established companies,[9] notably due to the more limited resources and inherent vulnerabilities of new firms. Startup Acts, because they are designed to address those challenges, are perceived as new tools for fostering the development of businesses with high potential of growth and innovation.

Startup Acts are too new in ACP countries, and external assessments are too few to make a general judgement about their overall effectiveness. However, in the case of Italy, an OECD report[10] shows that after six years of implementation, the cost-benefit balance is positive. The results indicate that the Startup Act has had a sizeable positive effect on both the inputs and the outputs of beneficiary firms. In particular, the policy allows firms to increase their revenues, value added, and assets by about 10 – 15 %, relative to similar start-ups that do not benefit from it, or benefit at a later stage. The analysis has also shown that the enrolled firms are more likely to receive credit from banks (first credit application increases by eight to 16 percentage points) and venture capital funding.

## COMPARISON OF THE ITALIAN, SENEGALESE AND TUNISIAN STARTUP ACTS

Among the few countries that have adopted a Startup Act, Italy, Senegal and Tunisia are interesting examples. They provide insights on the different level of intervention, different definitions of a startup and different incentives used, depending on each country's policy objectives. In Italy, the Startup Act has already been implemented for almost a decade and was subject to various evaluations that provides some perspective on the possible impacts of such legislation.

The Italian Startup Act encapsulates a large and diversified range of measures aiming at fostering the creation and development of startups through the creation of 'new instruments and support measures regarding subjects which have an impact on the whole lifecycle of a company, including the introduction of flexible corporate management tools, new ways to remunerate workers and consultants, facilitation in the access to capital and investment and support in the process of internationalization'.[11] The Italian Startup Act draws from the recommendations of the *Restart, Italia!* report, which was designed by a task force of twelve experts appointed by the Minister of Economic Development. The general objective of the Act is to promote sustainable growth, technological advancement and, in particular, to create favourable conditions for the development of a new business culture inclined towards innovation.

The Tunisian Startup Act was adopted in 2018. It is a legal framework that was designed in a collaborative and participatory process with the stakeholders of the startup ecosystem: entrepreneurs, accelerators, investors, administration, civil society, etc.[12] The Tunisian Startup Act provides incentives to three types of beneficiaries: entrepreneurs, startups and investors. The objective of the law is to set up an incentive framework for the creation and development of startups based, in particular, on creativity, innovation and the use of new technologies and achieving a strong added value and competitiveness at the national and international level.

In Senegal, the Startup Act was promulgated in January 2020 after a participatory process of policy co-creation that brought together various stakeholders including grassroot entrepreneurs, innovative hubs and policy makers. The law provides for a variety of incentives and support measures for startups, including the granting of tax, customs and social benefits, the creation of a platform for capacity building and the facilitation of access to public procurement.

9 Severino, JM, Hadjenberg, J. 2016. "Entrepreneurial Africa". [Entreprenante Afrique]. Paris. Odile Jacob.

10 Menon, C., et al. (2018), "The evaluation of the Italian "Start-up Act"", OECD Science, Technology and Industry Policy Papers, n° 54, Éditions OCDE, Paris. Available on: *https://doi.org/10.1787/02ab0eb7-en*.

11 Osimo, D., European Digital Forum, "the 2016 Startup National scoreboard: How European Union Countries Are Improving Policy Frameworks and Developing Powerful Ecosystems for Entrepreneurs", 2016.

12 Smart Capital, "Le Startup Act, une année après 2019 – 2020", Startup Act Annual Report.

## DEFINITION OF A STARTUP

All three Startup Acts set conditions to be considered as a startup. The conditions can be classified in two categories: those related to the company's characteristics (e.g. years of existence, number of employees, annual income, etc.) and those related to the company's potential of high growth or innovation.

Regarding the startup's characteristics, the Senegalese law only requires that any company seeking to be considered a startup must have been incorporated under Senegalese law for less than eight years and must be held by Senegalese nationals or residents or by legal entities with their headquarters in Senegal. Under Tunisian law, the human resources of the company cannot exceed one hundred employees, its total balance sheet and its annual turnover cannot exceed $5.3M and more than two-thirds of its capital should be held by individuals, venture capital investment companies, collective investment schemes, seed funds, any other investment body or by foreign startups. In Italy, the Startup Act requires companies to be incorporated for less than five years, to not have distributed profits, to have a yearly turnover lower than €5M, to have their headquarters in Italy or another EU country and to not be the result of a merger, split-up or selling-off of a company or branch.

For the criterion relating to growth or innovation, Senegal defines startups as 'innovative and agile companies […] that have a strong growth potential in search of a disruptive business model and financing mechanisms adapted to its specific characteristics in order to deploy its exceptional capacity for value creation'.[13] As for the Tunisian law, it requires two cumulative criteria; a business model with a strong innovative dimension, particularly technological, and an activity with strong growth potential. Under the Italian Startup Act, startups must have as exclusive or prevalent purpose the production, development and commercialisation of innovative goods or services of high technological value.

## THE LABELLING PROCESS: OBJECTIVE SELECTION VS DISCRETIONARY SELECTION

The granting of incentives provided by Startup Acts often depends on the ability of firms to meet the above-mentioned criteria and go through a labelling process. The selection process of firms receiving grants and/or incentives can be either objective or discretionary.

In an objective selection process or entitlement-based labelling process, firms are expected to apply to a designated institution and submit proof that they meet stated objective criteria. The Italian selection process falls into this category. Companies that meet the requirements can obtain the "innovative Startup status" by simply registering into a special section of the Italian Business Register. The registration process entails sending a self-certification of compliance with requirements and the legal benefits automatically apply starting from the date of registration. Thereafter, the chambers of commerce carry out routine checks to make sure that the legal requirements are met, and if so the benefits will be maintained up to the fifth year after incorporation.

In contrast, in a discretionary selection process companies applying for startup status have to go through a selection process managed by a committee (often composed of public and private actors) responsible for determining whether a company is innovative or has the required growth potential in accordance with the provisions of the Startup Act. The process is called "discretionary" because it is left to the committee to determine if a startup complies with the requirements through an analysis of the company's individual situation. The Tunisian and the Senegalese Startup Acts have opted for this kind of selection process. In Tunisia, the startup label is awarded by the Ministry in charge of the digital economy based on an assent from the Technical Committee. The Technical Committee is responsible for checking that the company meets the cumulative conditions of having a business model with a strong innovative dimension and an activity with strong growth potential. Under the Senegalese Startup Act, an Evaluation, Support and Coordination Commission is in charge of granting the startup label to companies that demonstrate a strong growth potential. The conditions of "growth potential" or "innovation" are subjective in the sense that they require an analysis of the situation of each company. Moreover, the discretionary selection process relies partly on the legislator's ability to anticipate the criteria that will enable companies to become innovative or high growth.

The adoption of a discretionary selection process can partly be explained by the attempt to filter in a more effective way and/or the wish to facilitate the administrative review of the applicant firms' compliance with the criteria.

13 Section 3 of the Senegalese Startup Act.

## INCENTIVES GRANTED TO STARTUPS

Startup Acts are omnibus instruments aimed at tackling a multitude of challenges facing startups through targeted incentives in different policy areas, such as, for instance, improved market access or financing for startups. The Italian, Senegalese and Tunisian Startups Acts provide a wide range of incentives adapted to the ecosystem of each country and to the specific objectives of these legal instruments. There are a wide variety of incentives adopted by Startup Acts that offer levers for countries to promote startups. Because one size does not fit all, these incentives need to be cost-benefit assessed to ensure that they meet the needs of the territories where they apply.

The table below presents the incentives aimed at improving the financing of Startups in the Senegalese, Tunisian and Italian Startup Acts. The following measures are listed in the Startup Acts themselves, but there are a number of other associated laws and regulations that resulted from the overall Startup Act dialogue process. In Tunisia, for example, a crowdfunding law was passed in 2020, recognising this mode of financing for companies and projects. In Senegal, the adoption of the Startup Act was also the opportunity for putting in place major tax reforms in the Tax Code.

Finance is essential to the growth of startups and it generally takes two major forms: external equity or debt. Equity financing, and particularly venture capital investments, is usually more appropriate for startups because they face higher risk than traditional businesses. The Italian Startup Act has chosen to improve startups' access to both equity and debt. The venture capital market is underdeveloped in Italy and the Startup Act has been trying to correct this with mixed results so far. Moreover, the Startup Act has also facilitated the access to bank loans through a guarantee fund on the condition of registration. However, according to an assessment report from Harvard University,[14] access to debt funding via debt guarantee schemes might have incentivised small firms with a suboptimal business idea that are unable to secure venture capital funding and this measure has been considered as distortive and costly for the Italian government. More generally, according to this report, the Italian policy is sufficient to deliver performance at the later stages of a startup but the finance mechanisms need to be improved to be more effective at the early stages. In fact, startups still lack professional award/seed capital to grow and test their product.

The strategy of the Tunisian Startup act consisted in providing financing tools to three types of actors: entrepreneurs, through the provision of an allowance given to the co-founder and shareholder to cover living expenses for one year; startups, via notably the creation of a €200 million fund of funds; and investors, who benefit from tax-deductible start-up investment as well as capital gains tax exemption of profits from the sale of shares in startups. Most recently, in July 2020, Smart Capital announced new financial support for Tunisian startups. This includes: a fund of $84 million to finance innovation projects, up to $1 million to support labelled start-ups impacted by COVID-19, support funding of $7 million to finance research and innovation, and a state innovation laboratory with funding of $3.5 million.

The Senegalese Startup Act was less specific in presenting its financing measures but recognises the inadequacy of traditional financing methods for the specific needs of startups and mandates its Commission with the task of setting up alternative financing strategies and mechanisms for startups.

14 De Angelis, L., "Italy and Startups: harnessing a country of innovators, a Policy Analysis of the Italian Startup Act and its effects on the Startup Ecosystem". Cambridge: Harvard Kennedy School, Harvard business school, 2017.

## TABLE 1: Comparison of the non-financial incentives in the Senegalese, Tunisian and Italian Startups Acts

The table below presents the different non-financial incentives granted by the Senegalese, Tunisian and Italian Startup Acts by area of policy reform, namely governance, business support, access to markets, digital infrastructure, labour market, and fiscal.

| Senegal | Tunisia | Italy |
|---|---|---|
| **GOVERNANCE[15]** | | |
| ▪ An online platform, allows startups to complete the registration and labelling formalities.<br>▪ Facilitation measures and customs procedures favorable to startups in accordance with the laws and regulations in force.<br>▪ Startups are supported in accessing national and international intellectual property protection bodies. | ▪ The Ministry in charge of the digital economy assumes the direct and indirect costs of intellectual property registration for startups in order to facilitate access to IP registration. | ▪ The incorporation and following statutory modifications can be done by means of a standard model with digital signature.<br>▪ Reduction of red tape and fees.<br>▪ "Fail fast" procedure.<br>▪ Certified incubators have a special track to use the Italia Startup Visa program. |
| **BUSINESS SUPPORT** | | |
| ▪ Public or private support structures such as incubators can benefit from incentives to facilitate the support of startups.<br>▪ The support and coordination commission sets up a training and capacity building platform dedicated to legally registered startups.<br>▪ Startups are supported in research and development activities. | ▪ All public agents and employees of a private company benefit from a Startup Leave to create a startup for a period of year, renewable once. | ▪ The Italian Trade Agency provides assistance in legal, corporate and fiscal activities, as well as real estate and credit matters. |
| **ACCESS TO MARKETS** | | |
| ▪ A 5 % preference margin is granted to any labelled startup participating in a call for tenders for a public contract.<br>▪ Applicants to a public contract, delegation or partnership contract who agree to subcontract 30 % of the services covered by the contract to startups or who submit a group offer with startups may benefit from a 5 % preference margin. | | ▪ Conversion to innovative SME status (extending the incentives to the stage of maturity). |

›››

15 By 'Governance' we mean laws and regulations affecting the startup and growth of firms, as well as associated implementation practices.

| Senegal | Tunisia | Italy |
|---|---|---|
| **FISCAL** | | |
| ▪ Exemption from the minimum flat-rate tax (Impôt minimum forfaitaire – IMF) for three years.<br>▪ Exemption from the lump-sum contribution payable by employers (CFCE) for three years.<br>▪ Abolition of the minimum collection of 500,000 FCFA for the IMF.<br>▪ Reduction (from 25,000 to 10,000) of registration fees for the creation of companies when the capital is equal to a maximum of one hundred (100) million FCFA. | ▪ The following are fully deductible and within the limit of income or profit subject to tax:<br>› Income and profits reinvested in the underwriting of the initial capital or increased capital of Startups.<br>› Income or profits reinvested in the capital subscription of venture capital companies, or placed with them in the form of venture capital funds, seed funds or any other investment body.<br>▪ The profits from the sale of shares in Startups are exempt from the capital gains tax.<br>▪ Exemption from corporation tax and the assumption by the State of employers' and employees' contributions to the statutory social security scheme. | ▪ Exemption from the duty to affix the compliance visa for compensation of VAT credit.<br>▪ Tax incentives for corporate and private investments in Startups, both by individuals and by legal entities.<br>▪ Exemption from fiscal penalties applied to so-called "dummy companies".<br>▪ Transfer of Startup fiscal losses to listed sponsor companies.<br>▪ R&D Tax credit.<br>▪ Patent box (exclude from taxation 50 % of the income deriving from commercial use of intangible assets). |
| **DIGITAL INFRASTRUCTURE** | | |
| ▪ Startups benefit from support in registering the domain name ".sn". | | ▪ Access to an online portal (opportunity to manage a public profile). |
| **LABOUR MARKET** | | |
| | ▪ Any young graduate legally eligible for the employment programs, and who creates a startup, retains the right to benefit from these programs for a maximum period of three years. | ▪ Tailor-made labor law.<br>▪ Flexible remuneration system. |

## TABLE 2: Comparison of the financial incentives in the Senegalese, Tunisian and Italian Startups Acts

There are a wide variety of incentives adopted by Startup Acts that offer levers for countries to promote startups. Because one size does not fit all, these incentives need to be cost-benefit assessed to ensure that they meet the needs of the territories where they apply.

The table below presents the incentives aimed at improving the financing of Startups in the Senegalese, Tunisian and Italian Startup Acts. The following measures are listed in the Startup Acts themselves, but there are a number of other associated laws and regulations that resulted from the overall Startup Act dialogue process. In Tunisia, for example, a crowdfunding law was passed in 2020, recognising this mode of financing for companies and projects. In Senegal, the adoption of the Startup Act was also the opportunity for putting in place major tax reforms in the Tax Code.

| Senegal | Tunisia | Italy |
|---|---|---|
| | **FINANCE** | |
| ▪ The State may subsidize the formalization of the company.<br>▪ Labelled startups benefit from funds, in particular in the form of loans, from public and private sources.<br>▪ Alternative strategies and mechanisms for financing startups will be defined and implemented by an inclusive commission established under the Startup Act. | ▪ Startups are legally entitled to issue convertible bonds, and are authorized to issue multiple convertible bonds, regardless of the option periods for conversion.<br>▪ The right to open a special account in foreign currency with approved intermediaries, without capital controls on funds raised.<br>▪ Any promoter of a startup may benefit from a startup scholarship for a duration of one year.<br>▪ Tax exemption on profits for investors.<br>▪ A Startup Guarantee Fund (yet to be created) aims to guarantee the participations of private equity firms, venture capital funds, seed funds and any other investment body. | ▪ Possibility to collect capital through equity crowdfunding on authorized online portals.<br>▪ Flexible corporate management, allowing startups to create categories of shares with specific rights, carry out financial operations on their own shares and offer shares to the public.<br>▪ Extension of terms for covering losses.<br>▪ Remuneration through stock options and work-for-equity schemes.<br>▪ Fast-track, simplified and free-of-charge access for innovative startups and certified incubators to the SME Guarantee Fund.<br>▪ Subsidized financing scheme for innovative Startups based in Italy. |

# KEY RECOMMENDATIONS FOR THE DESIGN AND IMPLEMENTATION OF STARTUP ACTS

The following recommendations are intended for policy makers and draw on best practices gleaned from a review of the literature on entrepreneurship policy, external assessments of Startup Acts and findings from i4Policy's experience in conducting deliberative entrepreneurship policy development projects, notably a benchmarking study on Small Business Acts (SBA) and Startup Acts in Africa.[16]

## ADOPTING A PARTICIPATORY PROCESS

Involving policy recipients in the process of co-designing and co-evaluating legislation and policies has proven to be crucial for enabling policy makers to better understand the needs and promote ownership during the implementation phase.

In the case of Startup Acts, the participation of entrepreneurs and other ecosystem players in the policy making process offers three advantages:

- It enables policy makers to better understand the needs and incorporate the knowledge and preferences of beneficiaries into their decision-making. The origin of any entrepreneurship or policy instrument needs to be grounded in an identified and studied problem or constraint, rather than in an ad hoc justification that can be the result of vested interests or pressure from particular stakeholders (Cirera et al. 2017 & 2020).[17]
- It strengthens social capital by building local capacity for self-reliance and collective action, by strengthening intra-ecosystem networks, cooperation, coordination and the flow of information – in other words, by turning individuals into public citizens and establishing shared norms for the public good.
- It ensures ownership and implementation supervision, by enabling citizens to hold states and markets accountable.

More particularly, deliberation is found to be a key success factor of such a participatory policy making process. Unlike surveying, voting or bargaining, deliberation can be transformative: it can result in changes in the determinants of actions and preferences,[18] shift social norms, facilitate coordination and ensure greater commitment from participants and elites.[19]

In the case of the Startup Acts in Tunisia, Senegal, and Mali, the entrepreneurship ecosystem stakeholders led the whole, deliberative process of co-creating legislation and lobbying the government. The process itself has been crucial in raising awareness around entrepreneurship issues with governments, in creating networks between entrepreneurs and governments, and in developing and galvanising the entrepreneurship community, which now remains strongly committed to the effective enactment of the Startup Acts. SBAs and Startup Acts can send a strong signal to local entrepreneurs and their supporters/investors that their government recognises the importance of entrepreneurship and will incentivize it (Hill 2018).[20] This signaling should not be dismissed, particularly in countries where broader reform has proven difficult, where attitudes to entrepreneurship may be negative, and where the entrepreneurial community is small and lacks influence.

16 Stever, J., Yawson, F., Rodrigues, E., & Duchatelet, S., i4policy, "Small Business Acts and Startup Acts in Africa", 2020.

17 Cirera, X., Maloney, W. 2017. "The Innovation Paradox: Developing-Country Capabilities and the Unrealized Promise of Technological Catch-Up". Washington, DC: World Bank and Cirera, X., Frías, J., Hill, J., Li., Y. 2020. "A Practitioner's Guide to Innovation Policy. Instruments to Build Firm Capabilities and Accelerate Technological Catch-Up in Developing Countries". Washington, DC: World Bank.

18 Gauri, V., Woolcock, M., Desai, D. 2013. "Intersubjective Meaning and Collective Action in Developing Societies: Theory, Evidence and Policy Implications". The Journal of Development Studies, 49:1, 160-172.

19 Heller, P., Rao, V. 2015. "Deliberation and Development: Rethinking the Role of Voice and Collective Action in Unequal Societies". Policy Research Report. Washington, DC: World Bank.

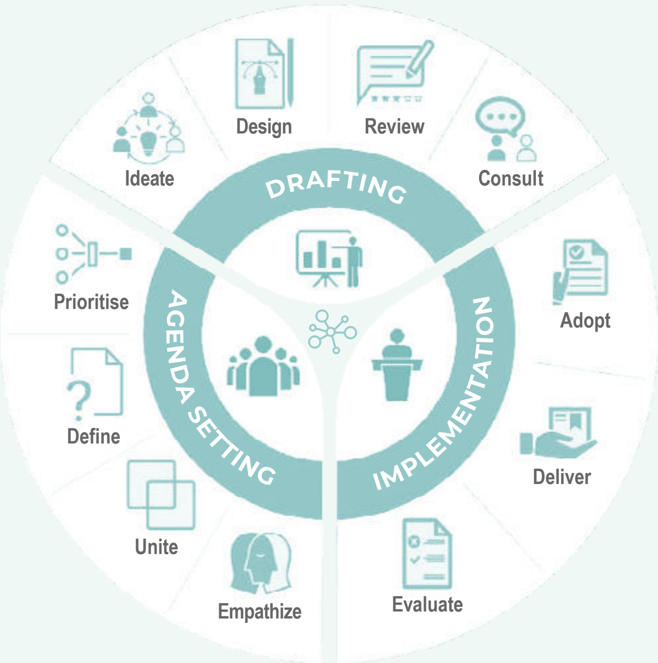
20 Hill, J. 2018. « Technical Review of startup Acts (Working Paper) ». Washington D.C.: World Bank.

## EXAMPLE OF A DELIBERATIVE POLICY-MAKING PROCESS: INNOVATION FOR POLICY

Inscribed within the suite of participatory and deliberative approaches, the *Innovation for Policy* process was designed by **i4policy**. It offers a number of tools (including digital technologies and facilitated engagements, such as Policy Hackathons) in an effort to optimize public policy reform for sustainable development outcomes. It is an iterative framework for policy reform that optimises public policy by elevating the knowledge and preferences of policy users, analysts and policy makers through deliberation, expert review, and inclusive participation.

This process was designed specifically to develop Startup Acts, and is currently being used in 18 countries for this purpose.

**FIGURE 2 : The different steps of the i4Policy process**




*Source :* i4Policy Process v3.1, Innovation for Policy Foundation cc-by-sa

The assumption, based on the literature on participatory development, is that policy developed through this process is expected to be more relevant, legitimate and effective, and generate knowledge in the process of design and delivery that informs future reform. This methodology was implemented in Senegal, Mali, Nigeria, Benin, Togo, Niger, Burkina Faso, Libya, Guinea, Madagascar, Mauritania, Tanzania, South Africa, Ivory Coast, Kenya, DRC and Rwanda.[21]

This policy-making process opens the way for new forms of policy dialogues including ones involving non-traditional actors such as grassroot entrepreneurs and innovative hubs.

21 Voir *https://i4policy.org/*. Le processus I4Policy est toujours en cours dans certains de ces pays.

## ADOPTING AN ECOSYSTEM APPROACH

Entrepreneurship legislation and policies must recognise the ecosystems and interconnections in which entrepreneurs grow, and it is imperative that policies are long-term, holistic, and well-coordinated.

The term 'ecosystem' was introduced into the entrepreneurship policy analysis specifically because the interaction between the components in the ecosystem is critical to understanding the challenges that may impede entrepreneurship and potential solutions.

For example, if a policy increases access to finance but entrepreneurial skills to develop a business are lacking, the financing might be difficult to disburse and financiers might complain about the lack of pipeline. It is therefore fundamental to adopt an ecosystem approach recognising the interdependence of multiple factors and the fact that policy measures could have positive or negative consequences on the business environment as a whole. Having holistic but realistic, long-term goals is considered as a best practice for Startup Acts.

Adopting an ecosystem approach is also a good way to avoid the adoption of disparate measures, which can sometimes be contradictory. Fragmented and overlapping programmes can have counterproductive outcomes and impede the good management of resources.[22] Priority should be given to involving a wide range of agencies and ministries in the development of entrepreneurial policies and to fostering good cooperation between them. In addition, Startup Acts should serve as reference documents for other government programmes and policies for firm development, thus preventing overlap.

## ADDRESSING FRAMEWORK CONDITIONS

Startup Acts are not only a law, but a participatory process that can be a catalyst for wider structural reforms. This process can be an opportunity to assess the general entrepreneurship framework and an occasion to improve the overall policy and regulatory instruments of a country.

According to the OECD,

*'an effective startup policy is not a sufficient condition for innovative small businesses to thrive. A number of 'horizontal" structural reforms benefitting the whole economy – e.g. improving the efficiency of civil justice (and of the public sector at large), fighting corruption and tax evasion – are also needed, as they would have a disproportionately positive effect on innovative startups. The need for synergic policy action is rooted on some of the specific weaknesses of the startup ecosystem – like e.g. the exiguity of venture capital (VC) investments and the weakness of the domestic end-market for innovative goods and services'*

(OECD/UE/ETF 2018).

The importance of addressing framework conditions and not only targeting startups is reinforced by recent research that warns against policies channeling public resources to specifically targeted firms and argues for a reorientation of public policy away from actively searching for high-potential firms toward the basics of growth entrepreneurship: improving allocative efficiency, encouraging business-to-business spillovers, and strengthening firm capabilities (innovation, managerial, and entrepreneurship skills).[23] These measures are positively correlated with firm productivity and growth. A 2016 European Commission report[24] also emphasises the need for an integrated approach balancing dedicated support actions for high-growth innovative enterprises and addressing framework conditions.

22 OECD/EU/ETF, 2018. "The Mediterranean Middle East and North Africa 2018: Interim Assessment of Key SME Reforms, SME Policy Index". Paris: OECD Publishing.

23 Grover, A., Medvedev, D., Olafsen, E. 2019. "High-Growth Firms: Facts, Fiction, and Policy Options for Emerging Economies". Washington, DC: World Bank.

24 Costa, P., Ribeiro, A., Van der Zee, F., Deschryvere, M., European Commission, 2016, "Framework conditions for high-growth innovative enterprises (HGIE)", final report.

## FAVORING A CLEAR AND OBJECTIVE SELECTION PROCESS FOR BENEFICIARY TARGETING

The differences between an objective selection process (or also called 'entitlement-based' process) and a discretionary selection process were explained above and examples were provided.

The implementation of discretionary selection processes presents challenges. The biggest obstacle linked to such a discretionary selection processes lies in the difficulty of developing, assessing and administering a definition and eligibility criteria for startups and innovative companies (Hill 2018). Due to government failures, experience has shown that operational constraints on public agencies and the risk-averse attitudes among public sector staff, combined with their lack of direct knowledge and experience with the private sector, entrepreneurship and innovation, make it extremely difficult to manage the sourcing and selection of beneficiary firms with the proper speed and flexibility. In the private sector, the growth and innovation potential of startups is mainly determined on the basis of the advice of investment professionals and is related to the characteristics of the company's team, and even then experienced venture capital investors struggle to distinguish successful startups from the ones that will fail.[25]

It is therefore preferable to opt for an entitlement-based selection process which offers clear-cut criteria for being considered as a beneficiary or not: either a firm meets these criteria, or it doesn't. The advantage of such entitlement selection processes is twofold.[26] First, there is less of a need to establish separate selection / labelling committees, which would be ill-positioned to accurately determine whether a firm has growth potential or is innovative. Second, there is less red tape surrounding the selection / labelling process, which means less bureaucratic bottlenecks and delays if the administration has to handle big volumes of applicants, and less potential for corruption. Entitlement processes are widely used – for example, to deploy most tax incentive programs for firms in the USA, as well as in Italy's Startup Act for wider supports and benefits.

If an entitlement selection process is not possible, it is recommended to adopt a sourcing and selection model based on private sector decision making, with proper support, transparent monitoring, and evaluation.[27] Such a model can be a selection committee composed of experienced members of the private sector considering the fact that private sector is generally better equipped to identify businesses with potential.

25 Nanda, R. 2016. "Financing High-Potential Entrepreneurship." Bonn: IZA World of Labor.

26 Cook, P., Desai, S., Olafsen, E. 2018. "Growth Entrepreneurship in Developing Countries: A Review of Policy Instruments in Developing Countries (Working Paper)". Washington, DC: World Bank.

27 Lerner, J. 2010. "The Future of Public Efforts to Boost Entrepreneurship and Venture Capital". Small Business Economics, 35(3), 255-264.

## PLANNING FOR OPEN IMPLEMENTATION AND MONITORING AND EVALUATION

Even though the importance of monitoring and evaluation is well established, the benchmarking study of African SBAs and Startup Acts revealed a critical gap in systematic results tracking and in evaluating the entrepreneurship interventions (i4policy, 2020). Many did not include specific monitoring and evaluation clauses. It appears essential to provide for a monitoring and evaluation mechanism in Startup Acts, to create a monitoring body composed of members from the public and the private sectors, in charge of monitoring and evaluation, and to establish a clear methodology, including regular and relevant surveys to gather the perceptions of benefiting firms. In this respect, the Italian Startup Act is a good example. A large variety of data is collected on firms, trough the Italian Chambers of Commerce which maintains a registry on the startups participating the programme. In addition, the Ministry of Economic Development conducted a detailed survey on all participants (with a response rate of more than 40 %) which provides specific information on ex-ante firm characteristics such as funding sources and employment composition.

The OECD SME Policy Index (2018) demonstrated that the implementation of concrete entrepreneurship strategies and action plans with detailed activities, responsibilities and budgets, is too often missing, and their approval does not automatically translate into results and impact. This can lead to well-known phenomena such as the superimposition of agencies intended to support entrepreneurs for instance, or the non-enactment of various by-laws and decrees that underpin SBAs or Startup Acts.

Priority should be given to the quality of execution and ensuring that monitoring and data collection mechanisms are in place to embed learning and iteration throughout.

**About the ICR Facility**

The ICR Facility is co-funded by the European Union (EU) and the Organisation of African, Caribbean, and Pacific States (OACPS), under the 11th European Development Fund (EDF), together with the German Federal Ministry for Economic Cooperation and Development (BMZ) and the British Council. The ICR Facility is implemented by GIZ, the British Council, Expertise France, and SNV.

The ICR Facility supports public and private stakeholders in ACP countries to improve their investment climate and business environment via public-private dialogue. The Facility supports specific and targeted interventions at the economy-wide, sectoral, and value-chain levels with Technical Assistance for up to 90 days based on requests. It also works to strengthen national and subnational development financial institutions and compiles and shares good practices for improving the business environment and investment climate.

**For more details** on the ICR Facility or to submit a request for Technical Assistance, visit: *www.icr-facility.eu*.

## CONCLUSION

Although, Startup Acts are no panacea on their own and cannot solve all entrepreneurship obstacles, the recent popularity of Startup Acts, particularly in Africa, shows that this instrument holds great promise for the development of innovation and high potential enterprises in ACP countries.

More than a new entrepreneurship policy, the true singularity of the Startup Act lies in its participatory design process that brings together policy makers and traditional as well as non-traditional stakeholders, such as grassroots entrepreneurs and their ecosystems.

In addition to providing solutions to the specific challenges of start-ups, this instrument allows for a renewal of public-private dialogue and instills a bottom-up approach in policy design processes that can produce positive spill-over effects for the whole economy and provide an opportunity for reflection on broader entrepreneurship policies in a country.

This paper was authored by Eveline Rodrigues, Innovation for Policy Foundation.

Valuable input was received from Jon Stever (Innovation for Policy Foundation) and Tim Gelissen (Innovation for Policy Foundation).

It is part of a series of ICReports on innovative financing solutions and financial regulations for start-ups, MSMEs, social enterprises and inclusive businesses.

### Other ICReports in this series are:

ICReport: *Honour loans: a comprehensive mechanism to foster development by supporting MSMEs*

ICReport: *Crowdfunding: an opportunity to increase access to finance for MSMEs in ACP countries*

ICReport: *Social Enterprises and Inclusive Businesses across ACP Countries: Variety and Access to Finance*

ICReport: *Supporting investment in inclusive business and social enterprises: Best practice for policymakers and investors in ACP countries*

**All ICReports have been produced after discussions at live events, which have been recorded and can be accessed at the ICR Facility's Knowledge Hub:**
***https://www.icr-facility.eu/knowledge-hub***

# IMPRINT

This paper was authored by Eveline Rodrigues, Innovation for Policy Foundation.
Valuable input was received from Jon Stever (Innovation for Policy Foundation) and
Tim Gelissen (Innovation for Policy Foundation).

The ICR Facility supported the production of this publication. It is co-funded by the European Union (EU), the Organisation of African, Caribbean and Pacific States (OACPS) under the 11th European Development Fund (EDF), the German Federal Ministry for Economic Cooperation and Development (BMZ) and the British Council.
The ICR Facility is implemented by GIZ, the British Council, Expertise France, and SNV.
The contents of the publication are the sole responsibility of the author and do not necessarily reflect the views of the EU, OACPS, BMZ or the implementing partners.

The ICR Facility supports countries and regional institutions of the Organisation of African, Caribbean and Pacific States (OACPS) in their public-private dialogue process to create a more conducive and sustainable investment climate.

**PUBLISHER:**
ICR Facility, Rond-Point Robert Schuman 6 / 7th Floor, 1040 Brussels – Belgium
www.icr-facility.eu

**AUTHOR:**
Eveline Rodrigues | Fondation Innovation for Policy

**DESIGN / LAYOUT:**
Atelier Löwentor GmbH, Darmstadt

**URL LINKS:**
Responsibility for the content of external websites linked in this publication always lies with their respective publishers.
The ICR Facility expressly dissociates itself from such content.

Brussels, September 2021

## INVESTMENT CLIMATE REFORM FACILITY

ANY QUESTIONS? CONTACT US.

**ICR Facility**
Rond-Point Robert Schuman 6 / 7th Floor
1040 Brussels
Belgium

**GET IN TOUCH:**
info@icr-facility.eu
in /icr-facility

**VISIT US ONLINE:**
ICR Facility
**www.icr-facility.eu**