

IMPACT INVESTING DESKBOOK SERIES

Mission Lock Mechanisms for Mission-Driven Companies

What happens when visionary founders with a passionate impact-oriented mission leave the company? Or when the original impact-oriented investors who backed the mission no longer control the company? Perhaps, the company goes public and is subject to the profit pressures of Wall Street and new shareholders and directors demanding higher returns. How do you ensure from the outset that the company's original mission will still be front and center years from now? How do you avoid "mission drift" and achieve "mission lock"?

There are many creative ways mission-driven companies, founders, investors and even lawmakers have sought to protect a company's mission. Sometimes it's built into the choice of entity (e.g., a public benefit corporation or a nonprofit) or a manipulation of shareholder voting rights (e.g., non-economic super-voting shares). Sometimes it's baked into the bylaws or articles. Sometimes it's by contract (e.g., strict licensing rights of critical IP or shareholder rights). Sometimes it's through oversight or control by "trusted" third parties. And sometimes it's even through shame (e.g., publication of mission failure). It's often a combination of two or more such mechanisms.

You can't talk about mission lock without a nod to two well-known companies, Tony's Chocolonely, a Dutch chocolate company, and Patagonia, an American retailer of outdoor recreational clothing, equipment, and food. Tony's Chocolonely's core mission is to eradicate "child and illegal labor from the chocolate industry," and it employs almost all the mechanisms available to ensure a virtual mission lockbox. Tony's Chocolonely also has taken the extra step of publicly sharing the details of its mission lock structure as a guide for adoption by other mission-driven companies, and many of its elements are described below.¹ Similarly, the founder of Patagonia has been very public about protecting his company's values of environmental protection and sustainability and in 2022 transferred all the voting stock of the company that he held to a special kind of trust also described below, a perpetual purpose trust, with a purpose and mission to control the company in alignment with the founder's environmental protection and sustainability values in perpetuity.

Corporate Structure: Baking in the Mission

The first step towards mission lock is often baking the mission into the organizational documents (i.e., the articles and bylaws) of a mission-related company. This may be in the form of a mission statement and/or guiding principles expressed in the articles of incorporation and/or the bylaws. For example, the articles of Tony's Chocolonely contain a mission statement as well as five specific "sourcing principles" to guide the operations of the company to achieve its mission. Its board of directors is required to uphold the mission and the sourcing principles.

¹ See Tony's Chocolonely's website for more: [Tony's Mission Lock](#) and [Tony's Mission Lock Open Source Guide](#).

Many jurisdictions now offer various forms of public benefit corporations and limited liability companies ("PBCs" and "PBLLCs") for publicly and legally acknowledging the mission at the heart of the enterprise, with the aim of providing a legal framework for mission-driven companies and their constituents to hold the companies accountable for their missions. The laws governing the formation of PBCs and PBLLCs typically require (i) a statement in the publicly filed articles of incorporation of the company's mission, which must fall within a defined public benefit, (ii) periodic reporting in regard to achieving the mission, and (iii) added legal protection for the directors when they make decisions that take into consideration the expressed mission and the interests of stakeholders other than just shareholders.

Additionally, PBC shareholders and PBLLC members have the right to bring a benefit enforcement proceeding, which is a derivative suit on behalf the company, when directors and officers fail to pursue the company's public benefit purpose. However, most jurisdictions require shareholders and members to meet a minimum threshold percentage of ownership interests held to have standing for a benefit enforcement proceeding.

Unfortunately, no matter how well the mission is baked in, it may still be vulnerable to future erosion or complete abandonment because organizational documents are always subject to amendment by shareholders whose interests, motives and circumstances may change and diverge from the mission over time.

The Golden Share: Concentrating Mission-Related Voting Control

With that in mind, to protect a baked-in mission against such amendments, companies have adopted a variety of equity structures in which a special class of shares is granted super-voting rights with either broad powers of management or more narrow mission-related veto rights. Such shares are typically held by founders or other trusted persons. The apotheosis in the evolution of this mission lock mechanism is the "golden share." A "golden share" is a single voting share (i.e., without an economic stake) in a company, which holds the power to prevent by veto any amendments or other legal changes to specified mission-related terms in a company's articles, bylaws or other constitutional documents. The golden share can be placed in the hands of a trusted shareholder, typically someone aligned with the company's mission. This may be the founders or, if even more protection of the mission is desired, someone independent of the company and without an economic interest that might create a conflict of interest. For example, Tony's Chocolonely has a single non-transferable golden share with no economic value, which is held by a nonprofit organization overseen by three appointed individual directors dubbed "Mission Guardians," who were selected by the founders and early investors for their skills and experience to "represent the business' mission."

"But with power!": Moving Beyond Veto Rights to Compliance

Not satisfied with just relying on veto powers, Tony's Chocolonely took its quest for mission lock one or two steps further than the norm. In addition to imbuing the golden share with veto powers, Tony's Chocolonely's bylaws further empowered the Mission Guardians (i.e., the directors of the nonprofit holding the golden share) with specific tools to enforce compliance with the mission statement and the sourcing principles. Any stakeholder who has a relationship with the company, including employees, cocoa farmers, business partners and "Choco Fans," can anonymously raise any serious concerns about mission drift with the Mission Guardians. The Mission Guardians have the right to investigate and discuss concerns in detail with management and suggest remedial steps. Solutions to issues raised are to be agreed within two months, after which management has six months to implement the solution. Where these issues are not resolved, the Mission Guardians have the right to escalate these concerns publicly via a double-page spread in the company's annual report, and, in addition, they have the right to publish any serious concerns in international full-page newspaper advertisements in each of the major markets in which Tony's is active. Tony's Chocolonely must also publish an explanation as to why it has not complied. Ultimately, the Mission Guardians can refer the matter for legal investigation and arbitration at

the Enterprise Chamber of the Court of Appeal in Amsterdam. And none of these terms in the bylaws can be modified without consent of the holder of the golden share. Boom, mic drop. Mission lock fully achieved.

Mission Lock by Contract: Intellectual Property Ownership and Licensing Terms

Impact-driven businesses that rely on critical intellectual property may consider structuring the ownership of such critical IP to create mission lock by contract through the terms for licensing and exploiting the critical IP. For instance, licensing terms may limit pricing or margins, making a product such as a new drug more affordable and more widely accessible economically and geographically. If the remedy for breach is loss of use of the critical IP, then adherence to the mission as operationalized in the license of the critical IP is an existential necessity. Similar to the power of a mission-aligned party holding a golden share, a mission-aligned party holding critical IP, also often in the form of a nonprofit entity, can achieve mission lock through contract.

Nonprofit Ownership and Control: Taming the Profit Motive

As demonstrated by the examples above of nonprofits owning a golden share or critical IP, nonprofit entities can be used in a variety of creative ways to maintain mission lock. For instance, a nonprofit entity could also be the actual operating company, though that often proves too limiting for successfully operating and competing in the for-profit world. A nonprofit entity could be the controlling shareholder of a mission-driven company. In each use case, the mission is insulated from the otherwise inevitable influence exerted by the profit motives of investors, officers and directors in for-profit entities. In a nonprofit entity, the mission is always paramount and its stewards are not beholden to act in a manner to serve the best interests of shareholders.

In the United States there are multiple types of nonprofits to choose from, both tax exempt and taxable, and each has its own specific utility and constraints.

- *501(c)(3) Public Charities or Private Foundations.* 501(c)(3) organizations are tax-exempt nonprofits that operate exclusively for “charitable, religious, educational, scientific, literary, testing for public safety, fostering national or international amateur sports competition, and preventing cruelty to children or animals.”² The primary benefit of 501(c)(3) status is that donations to a 501(c)(3) nonprofit are tax deductible. However, they are significantly restricted from lobbying and other political activities and are subject to oversight from the IRS in order to maintain their tax-exempt status. In addition, 501(c)(3) private foundations are subject to limitations on owning operating businesses that are not program-related investments or functionally related businesses (generally 20% of the voting stock of a corporation or profits interest of a partnership), a limiting factor in some situations.
- *501(c)(4) Public Welfare Organizations.* 501(c)(4) organizations are tax-exempt nonprofits that are “operated exclusively for the promotion of social welfare...”³ In contrast to a 501(c)(3) organization, a 501(c)(4) organization may engage in an unlimited amount of lobbying in furtherance of its social welfare purposes and a certain amount of political campaign activities (though the limits are currently in flux). In addition, donations to a 501(c)(4) are not tax deductible for income tax purposes, though they do not result in gift tax. There may be risks around estate tax for founders who endow a 501(c)(4) and retain control of the organization during their lives (careful structuring is required). Similar to a 501(c)(3), 501(c)(4) organizations are subject to oversight from the IRS in order to maintain their tax-exempt status.

² 26 U.S. Code § 501(c)(3).

³ 26 U.S. Code § 501(c)(4).

- *Taxable Nonprofits.* Nonprofit organizations may choose not to seek federal tax-exempt status, opting instead to pay corporate taxes on income. While not as common, this path is beneficial if an organization would like to limit itself to a nonprofit structure (including not having owners) without being subject to the regulatory restrictions applicable to 501(c)(3) or 501(c)(4) organizations, its operations do not rely on tax-deductible donations and tax-exemption is not a driving force. This structure protects the mission from private profit motives while avoiding the strict definitions and public scrutiny associated with tax-exempt status.

Given the complex compliance obligations of nonprofit organizations, it is critical to consult legal counsel that is expert in the laws and regulations governing nonprofits prior to implementing any structures involving a nonprofit entity that is being created or employed to provide mission lock.

Perpetual Purpose Trusts: an Alternative Model

Another increasingly popular method of achieving mission lock is a perpetual purpose trust (a “PPT”), also referred to as a private purpose trust, a special purpose trust, or a noncharitable purpose trust. Recognized by statute in a handful of US states, including Delaware, and other non-US jurisdictions, a PPT is a trust that is established for the achievement of a particular noncharitable purpose, and not for the benefit of a particular person or persons. Common traditional examples are trusts for the care of pets, the perpetual maintenance of real property, the maintenance of valuable or unique collections (e.g., cars, art, or memorabilia), or the promotion of a lawful cause. More recently, PPTs have been employed by mission-driven founders as a tool for the mission lock of commercial enterprises, such as Patagonia. For the purpose achieving of mission lock, Patagonia’s PPT serves the same function as the nonprofit entity that holds Tony Chocolonely’s golden share. The appeal of using a PPT for mission lock, in contrast to a nonprofit, can be the greater flexibility afforded in defining the mission (i.e., the purpose of the trust), the ability to make the trust very difficult to amend (or nearly impossible without court intervention), and the relative ease in forming and administering the trust. A PPT is not limited by a charitable purpose as defined by statute and, assuming it does not seek and obtain federal tax exemption, is not subject to the complex compliance obligations of tax-exempt organizations. However, a PPT is likewise a creature of statute and therefore must be formed and operated in accordance with its governing law. If it is not tax exempt, it must also comply with the requirements applicable to its particular tax status (e.g., as a trust taxpayer).

Investor Imposed Mission Lock: Transparency and Alignment

Sometimes it’s the investors, whether they are investing in an impact fund or directly into mission-driven companies, that want to hold the fund managers and company founders accountable for sticking to the mission they are promoting and generating the impact that the investor is seeking. The most common tools of impact investors looking for mission lock are seeking (i) transparency about progress made toward the desired impact and (ii) alignment of interest with the fund manager or entrepreneur to achieve the desired impact. The typical mission lock mechanisms employed by impact investors are:

- *Impact Reporting.* Side letters or contractual investor rights requiring periodic impact reporting and progress on achieving defined impact goals.
- *Redemption Rights.* Use of defined impact goals tied with redemption rights in case of mission drift. Redemption rights are most often seen in connection with program-related investments (“PRIs”) made by philanthropies subject to adverse tax consequences if the investment strays from the defined impact.
- *Impact-Linked Compensation.* Tying management compensation to impact goals to align interests of management and impact investors.

Conclusion

There are many options to choose from when striving for mission lock. However, no method (or combination of methods) is bulletproof or fully insulated from the natural vicissitudes of people. Therefore, we recommend (i) building in redundancy to your mission lock structure, (ii) working with people you trust, and (iii) hiring good counsel.

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For more information on the issues discussed here, please contact your [Morgan Lewis Impact Investing](#) attorney.

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