

The Benefit Corporation

Can Changes to Corporate Law Change Business As Usual?

Anna R. Kimbrell*

Abstract: This article is an introduction to Benefit Corporations, a new type of legal business form for businesses that are motivated to create social and environmental benefits as well as profits. This article explains the evolution of and need for a business form that is unrestrained by the wealth maximization norms of traditional corporations. It explains the main goals of Benefit Corporation legislation and its success thus far. Finally, the article discusses criticisms of the legislation and concludes that, although new and untested, Benefit Corporations have strong potential to create positive and lasting change by using the power of business to address social and environmental problems.

The last decade has been marked with corporate scandals. From Enron to the subprime mortgage crisis, the BP oil spill to the Massey Energy mine explosion, Americans have become increasingly disillusioned with corporations.¹ At a time when unemployment rates are high and many Americans are struggling to make ends meet, the mere mention of “corporate America” brings to mind images of Wall Street fat cats lining their pockets with the hard-earned money of the less wealthy. Protestors involved in the Occupy Wall Street movement brought home the frustration and discontent with the “business as usual” attitude as they took to the streets to speak out against the traditional corporate culture of profit above all else.² In the midst of growing dissatisfaction with traditional corporate maxims, one organization has been working hard to change the corporate landscape and prove that corporations can do *good* and also do *well*.

* Anna Kimbrell is a 2014 dual degree JD/MBA candidate at the University of Kansas.

¹ Harris Interactive. “The 2012 Harris Poll Annual RQ Public Summary Report.” February 2012. (*reporting* that only 2 in 10 Americans say that corporate America’s reputation is positive).

² New York City General Assembly, “Declaration of the Occupation of New York City.” Ncyga.net. September 29, 2011. Accessed August 9, 2012.
<http://www.nycga.net/resources/declaration/>.

B-Lab and B-Corp Certification

B-Lab, a Pennsylvania nonprofit, was founded in 2007 to provide support to businesses and entrepreneurs who provide social and environmental benefits as well as make a profit. The organization created a certification for businesses, much like the “Fair Trade” or “Organic” certification that consumers are familiar with, in an effort to aid consumers in differentiating between good companies and companies with good marketing.³ The certification process attempts to measure impact on non-shareholder stakeholders and scores each business on a range of categories in four primary impact areas: employees, consumers, the community, and the environment. Businesses scoring above a threshold number are eligible for B-Corp certification.

The certification effort has been quite successful. At present, there are 574 certified B-Corps throughout the nation, representing 60 industries comprising \$3.35 billion in annual revenue.⁴ The Impact Assessment created by B-Lab is free to anyone and businesses are encouraged to use the free tool for self-governance and benchmarking purposes. To become certified, however, a business is required to pay certification fees, work with a B-Lab advisor, submit supporting documentation, be subject to periodic auditing, and publish its Impact Assessment report annually. The business must also alter its legal framework.

B-Lab encourages businesses to amend their governing documents to include language that expands traditional corporate responsibilities by requiring consideration of non-shareholder stakeholder interests, namely employees, consumers, the community, and the environment. Although courts may give some deference to inclusion of these rights and responsibilities in the corporation’s articles, many mission-driven corporations have struggled to fit within the existing traditional legal corporate framework.⁵

³ Clark, William H., and Larry Vranka. “White Paper The Need and Rationale for the Benefit Corporation: Why it’s the Legal Form that Best Addresses the Needs of Social Entrepreneurs, Investors, and, Ultimately, the Public.” January 26, 2012: 3. Accessed July 20th, 2012.
http://www.benefitcorp.net/storage/documents/The_Need_and_Rationale_for_Benefit_Corporations_April_2012.pdf.

⁴ Bcorporation.net. Accessed August 9, 2012. www.bcorporation.net.

Existing Business Forms and Traditional Corporate Law

Businesses with models that pursue a dual mission of making a profit and providing a social benefit are constrained by the choice of business forms available. The nonprofit form is not often a viable choice because of the inability to distribute profits and be privately owned. Nonprofits face difficulties in raising capital (both debt and equity) and have additional operational burdens imposed on them to maintain tax-exempt status.⁶ Further, the trend among nonprofits has been increasingly to rely on the revenue generated in furtherance of their social purpose (“earned” revenue) and less on philanthropic and government support. Operating costs for nonprofits have been increasing, private donations and governmental support has decreased, the number of nonprofit organizations has increased substantially causing competition for funds, and demand for the services provided by nonprofits has increased.⁷ This has caused many nonprofits to walk a fine line to keep their tax exempt status and others to seek a for-profit form that better suits their needs.

One of the most widely used forms of for-profit business is the corporation. There are many reasons why businesses choose the corporate form over other for-profit forms including tax considerations, profit disbursement, and availability of financing. The long legal and social history of profit-maximization as the central purpose of a corporation is at odds with the dual missions of social entrepreneurs. Social entrepreneurs fear that under traditional corporate law, they will be forced to make decisions that maximize profit for the corporation’s owners rather than pursue the social purpose of the company.

There is much debate over the extent to which directors and officers of corporations may pursue social purposes without breaching their fiduciary duties to shareholders. Typically business decisions are protected by the business judgment rule. The business judgment rule “is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company.”⁸ Whether or not the business judgment rule applies depends on the context that directors made the decision being challenged. Shareholders wishing

⁶ Murray, J. Haskell, and Edward I. Hwang. “Purpose with Profit: Governance, Enforcement, Capital-Raising and Capital-Locking in Low-Profit Limited Liability Companies.” *University of Miami Law Review*, 66. Fall 2011: 8-14.

⁷ Lane, Mark J. *Social Enterprise: Empowering Mission-Driven Entrepreneurs*, 8. Chicago: American Bar Association, 2011 (*listing* probable reasons for the trend as enumerated by the Social Enterprise Alliance).

⁸ *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984).

to sue directors for day-to-day decisions in which they considered other stakeholders, and failed to increase profits, are barred by the business judgment rule as long as directors can show some rational connection between the decision and stockholder benefit.⁹

In the context of a change-of-control situation, however, a director can be held liable for considering other constituents and failing to get the best price for shareholders.¹⁰ Also, when defending against takeover attempts the courts may look at director's decisions with heightened scrutiny.¹¹ In *eBay Domestic Holdings, Inc. v. Newmark* the Court dismissed the idea that a rights plan that specifically stated the public-service mission of the company was a legitimate corporate policy (which they would be protected by the business judgment rule to defend).¹² The court further stated that “directors of a for-profit Delaware corporation cannot deploy a rights plan to defend a business strategy that openly eschews stockholder wealth maximization— at least not consistently with the directors’ fiduciary duties under Delaware law.”¹³

Although some states have passed constituency statutes that allow directors to consider non-shareholder stakeholders when making decisions in takeover contexts, these statutes are rarely invoked and have little case law to support their interpretation.¹⁴ Notably, Delaware does not have a constituency statute. The cases described above and the lack of statutory authority giving corporate directors authority to pursue financial and nonfinancial goals has caused many mission-driven corporations to creatively structure their enterprises and protect their corporate mission with shareholder agreements, stock class restrictions, and amendments to the corporation’s articles. In response to this struggle to fit within the confines of the traditional corporate structure and existing corporate law B-Lab enlisted corporate attorney Bill Clark from Drinker, Biddle, & Reath LLP to draft model legislation and began a nationwide campaign to create a new legal business form, the Benefit Corporation.

⁹ Revlon Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 182 (Del. 1986).

¹⁰ *Id.*

¹¹ Unocal Corporation v. Mesa Petroleum Company, 293 A.2d 946 (Del. 1985).

¹² 16 A.3d 1, 34 (Del. 2010).

¹³ *Id.* at 35.

¹⁴ Lane, Mark J. Social Enterprise: Empowering Mission-Driven Entrepreneurs, 137-140. Chicago: American Bar Association, 2011.

Benefit Corporation Legislation

The main characteristics of Benefit Corporations are 1) a requirement that the corporation have a purpose to create a material positive impact on society and the environment; 2) a requirement that directors consider non-shareholder interests as well as shareholder interests when making decisions; and 3) a requirement to publish an annual report of its social and environmental performance measured by an independent third party standard.¹⁵ Electing to become a Benefit Corporation is voluntary and requires a two-thirds vote of the shareholders.

The requirement that a Benefit Corporation create a “material, positive impact on society and the environment, taken as a whole, as assessed against a third-party standard, from the business and operations of a benefit corporation”¹⁶ is a general purpose that a Benefit Corporation must adopt. Benefit Corporations are allowed to have a specific public benefit as well, and the Model Legislation lists many possibilities including: providing low-income or underserved individuals or communities with beneficial products or services, promoting economic opportunity for individuals or communities beyond the creation of jobs in the ordinary course of business, preserving the environment, and improving human health.¹⁷ The legislation is written so that financial interests of the corporation do not necessarily take precedence over the public benefit purposes.

Directors of a Benefit Corporation are accountable for their decisions and are required to consider the effects of any action or inaction on shareholders, employees, customers, the community, and the environment. Additionally, the legislation explicitly requires directors to consider both the long-term and short-term interests of the corporation and consider how decisions will affect the corporation’s ability to accomplish its general and/or specific public benefit purpose.¹⁸ In theory, shareholders could bring an action against directors and officers for failure to create a positive social and environmental impact but they cannot bring a claim for failure to maximize profit. The legislation does limit

¹⁵ Clark, William H., and Larry Vranka. “White Paper The Need and Rationale for the Benefit Corporation: Why it’s the Legal Form that Best Addresses the Needs of Social Entrepreneurs, Investors, and, Ultimately, the Public.” January 26, 2012: 3. Accessed July 20th, 2012.
http://www.benefitcorp.net/storage/documents/The_Need_and_Rationale_for_Benefit_Corporations_April_2012.pdf.

¹⁶ Model Benefit Corporation Legislation §105. Accessed August 9th, 2012.
http://benefitcorp.net/storage/documents/Model_Benefit_Corporation_Legislation.pdf

¹⁷ Model Benefit Corporation Legislation §102(a).

¹⁸ Model Benefit Corporation Legislation §301(a)(1).

director liability for monetary damages, however, so shareholders may be limited to injunctive relief from a court.

Further, the Benefit Corporation is required to create and publish an annual benefit report that includes a description of the ways the corporation created a material positive impact and any ways it failed to accomplish creating a positive impact. It is also required to explain why it chose, and how it applied, the third party standard that it used.¹⁹ Benefit Corporations do not have to use the third party standard created by B-Lab, nor do they have to become B-Corp certified, but they do have to use a standards organization that provides comprehensive, credible, independent, and transparent standards. Recommended organizations include: The Global Reporting Initiative (GRI), GreenSeal, Underwriters Laboratories (UL), ISO2600, Green America, and B-Lab. Some organizations may provide a better fit for a particular industry, business size, or regional area.

Maryland was the first state to pass Benefit Corporation legislation in April 2010. Since then ten states have passed the legislation: Vermont, New Jersey, Virginia, Hawaii, California, New York, Louisiana, South Carolina, Massachusetts, and Illinois. Four more states have introduced the legislation, and Washington State has passed “Special Purpose Corporation” legislation that requires corporations to adhere to a third-party corporate social responsibility standard if the requirement is included in their articles of incorporation. Although some attorneys and state bar associations have criticized the legislation, arguing that it is unnecessary or vague, it has passed with bipartisan support in every state.

Patagonia, the outdoor apparel retailer, was the first corporation to elect Benefit Corporation status in California after the legislation was passed in September, 2011. Patagonia is a privately held corporation and therefore is not subject to the same potential backlash by shareholders for pursuing non-financial goals. However, by incorporating as a Benefit Corporation Patagonia’s founder, Yvon Chouinard, ensures that the mission of the corporation will survive when the company is sold or his successor takes over. “Patagonia is trying to build a company that could last 100 years,” Yvon Chouinard said. “Benefit corporation legislation creates the legal framework to enable mission-driven companies like Patagonia to stay mission-driven through succession, capital raises, and even changes in ownership, by institutionalizing the values, culture, processes, and high standards put in place by founding entrepreneurs.”²⁰

¹⁹ Model Benefit Corporation Legislation §401(a).

²⁰ King, Bart. “Patagonia is First to Register for Benefit Corporation Status in California.” SustainableBrands.com. January 4, 2012. Accessed August 9, 2012,

Criticism of Benefit Corporation Legislation

Critics of Benefit Corporations are critical on a range of issues. Some argue that Benefit Corporations are unnecessary and that current corporate law is adequate to accommodate mission-driven businesses.²¹ Others argue that the vagueness of the public-benefit requirement and the third party standard opens the door to “greenwashing” or even fraud.²² Some argue that choosing to incorporate as a Benefit Corporation limits a company’s ability to attract capital because investors are less likely to invest in companies without profit as the primary goal.²³

Whether or not directors of mission-driven businesses breach their fiduciary duties by considering non-shareholders when making decisions depends considerably on the context of the decision, and is anything but clear. Benefit Corporation statutes clearly define the dual mission purpose of socially motivated businesses and go one step further in *requiring* directors and officers to consider other stakeholders when making decisions. Although individual statutes vary by state, the public benefit requirement in the Model Legislation is purposely broad to avoid allowing companies to choose one narrow specific public-benefit purpose and claim Benefit Corporation status. This reduces the likelihood that a corporation will falsely market itself as “green” or socially beneficial when it is actually doing very little good overall. The Model Legislation also contains detailed descriptions of independent third party standards and B-Lab has published guidelines for businesses choosing a third party standard. Many companies in many industries would be marginalized if the statute was written to assume a “one size fits all” approach with strict guidelines on which third party standards are acceptable.

The rapid growth of Socially Responsible Investing (SRI) and Impact Investing tends to prove that investors are looking at factors other than simply the highest return on investment when choosing where to invest their money. The SRI

http://www.sustainablebrands.com/news_and_views/articles/patagonia-first-register-%E2%80%98benefit-corporation%E2%80%99-status-california.

²¹ Underberg, Mark A. “Benefit Corporations vs. “Regular” Corporations: A Harmful Dichotomy.” *Harvard Law School Forum on Corporate Governance and Financial Regulation*. May 2012.

²² Brakman Reiser, Dana. “Benefit Corporations—A Sustainable Form of Organization?” *Wake Forest Law Review*, 46. Fall 2011: 611.

²³ Schoenjahn, Ashley. “New Faces of Corporate Responsibility: Will New Entity Forms Allow Businesses to Do Good?” *Journal of Corporation Law*, 37. Winter 2012: 471-472.

movement currently represents almost 10% of U.S. assets under management, roughly \$2.3 trillion.²⁴ Traditionally socially responsible investors boycotted companies that engaged in bad behavior (tobacco, alcohol, weapons, etc.). More recently, investors have begun to seek out “good” companies and invest in enterprises that will have the most social impact, called Impact Investing. A 2009 report published by the Monitor Institute estimates that Impact Investing has the potential to grow to about 1% of total managed assets over the next five to ten years, approximately \$500 billion.²⁵

B-Lab has developed a Global Impact Investing Ratings System (GIIRS) that provides rating and analytics for social and environmental impact of companies and funds similar to financial ratings and analytics. Launched in September 2011 it now boasts over \$4 billion impact assets under management, provides ratings for 246 companies and 32 funds, with an additional 103 companies and 28 funds in the pipeline. How much Impact Investing and SRI will grow in years to come is anyone’s guess, but no one can deny that the trend toward investing with more in mind than financial return is growing. This growing trend allows social entrepreneurs access to additional revenue streams and the possibility of patient capital investment.

Conclusion

Although Benefit Corporations are relatively new and untested, there is a growing demand for socially conscious business and a need for new legal business forms to accommodate them. Businesses that are firmly committed to pursuing social and environmental benefits should not be intimidated by traditional corporate norms and forced to bypass their mission for fear of being sued. The Benefit Corporation gives social enterprises a way to differentiate themselves from corporations with large marketing budgets and misleading claims about social and environmental responsibility. As with any new legislation there are questions about how the statutes will apply in certain situations and how courts will interpret them. Despite this, the legislation is an important step toward increased corporate accountability, transparency, and responsibility. Benefit Corporations are an important step toward changing the landscape of corporate America.

²⁴ United States Social Investment Forum (USSIF). “2010 Report of Socially Responsible Investment Trends in the United States.” 2010: 7. Accessed August 9, 2012.

²⁵ Freireich, Jessica, and Katherine Fulton. “Investing for Social and Environmental Impact Executive Summary.” *Monitor Institute*. January 2009: 3. Accessed August 9, 2012.
http://www.monitorinstitute.com/impactinvesting/documents/InvestingforSocialandEnvImpact_ExecSum_000.pdf.