William & Mary Business Law Review

Volume 4 (2013)
Issue 2

Article 7

April 2013

The Social Enterprise Revolution in Corporate Law: A Primer on Emerging Corporate Entities in Europe and the United States and the Case for the Benefit Corporation

Robert T. Esposito

THE SOCIAL ENTERPRISE REVOLUTION IN CORPORATE LAW: A PRIMER ON EMERGING CORPORATE ENTITIES IN EUROPE AND THE UNITED STATES AND THE CASE FOR THE BENEFIT CORPORATION

ROBERT T. ESPOSITO*

ABSTRACT

Remarkably, in the face of a global recession, the social enterprise sector continued to experience extraordinary growth in both financial support and the number of newly authorized corporate entities aimed at social entrepreneurs who seek to use the power of business to simultaneously achieve profit and social or environmental benefits. This Article highlights recent developments in the social enterprise movement in Europe and the United States and focuses on the emergence of a surprisingly broad range of newly authorized corporate entities on both continents in response to the needs of social entrepreneurs. These include social cooperatives and the community interest company in Europe, as well as the L3C, the flexible purpose corporation, the social purpose corporation, and the benefit corporation in the United States. In so doing, this Article emphasizes the truly international scope of the social enterprise movement and explains the growing divergence in approaches to social enterprise between continental Europe and the United States. This Article suggests that the benefit corporation, which imposes a new duty to consider stakeholder interests, is currently the most effective vehicle through which social entrepreneurs can ensure their blended value goals are being considered and achieved. This Article concludes by responding to critiques of profit-distribution in social enterprise, making the case for the benefit corporation, and suggesting some statutory and tax reforms to further foster the social enterprise revolution.

---

* Dartmouth College, B.A., 2007; Wake Forest University School of Law, J.D., 2010; The George Washington University Law School, LL.M., 2012. The author thanks Theresa Gabaldon, Miriam Galston, Kyle Westaway, Benjamin Leff, J. Haskell Murray, Dana Brakman Resier, David Carter, William H. Clark, Jr., William J. Callison, and Bruce Campbell for their valuable insight and helpful comments on earlier drafts.

TABLE OF CONTENTS

INTRODUCTION

I would leave this to the Consideration of all who are concern'd for their own or their Neighbor's Temporal Happiness; and I am humbly of Opinion, that the Country is ripe for many such Friendly Societies, whereby every Man might help another, without any Disservice to himself.[1]

An increasing number of voices are calling for a corporate revolution that promotes socially and environmentally responsible business practices, and in turn gives sustainable goods and services greater market access. Business luminaries like Muhammad Yunus,[2] Bill Gates,[3] and Richard Branson[4] have voiced their frustrations with the predominance of shareholder wealth maximization, and have joined the ranks of long-time sustainability advocates like John Elkington[5] in encouraging a new generation of entrepreneurs to consider stakeholder interests and embrace socially and environmentally responsible business models. In other words, they argue that doing good will be good for business.[6] Moreover, they submit

[1] Benjamin Franklin, *Silence Dogood, No. 10*, NEW-ENGLAND COURANT, Aug. 13, 1722, at 1, *reprinted in* BENJAMIN FRANKLIN, SILENCE DOGOOD, THE BUSY-BODY, AND EARLY WRITINGS 32–33 (J.A. Leo Lemay ed., 2002).

[2] *See* MUHAMMAD YUNUS, BUILDING SOCIAL BUSINESS: THE NEW KIND OF CAPITALISM THAT SERVES HUMANITY'S MOST PRESSING NEEDS xv–xvi (2010). Yunus argues that our existing theory of capitalism is flawed insofar as it misrepresents human nature, and concludes that capitalism's portrayal of human beings as "one-dimensional beings whose only mission is to maximize profit" represents a "badly distorted picture" because it fails to recognize that human beings are also driven by selfless motivations. *Id.* at xv.

[3] *See* Bill Gates, Remarks at the 2008 World Economic Forum: Creative Capitalism (Jan. 24, 2008) (transcript and video available at http://www.gatesfoundation.org/speeches-commentary/Pages/bill-gates-2008-world-economic-forum-creative-capitalism.aspx). Gates submits that, in general, people benefit in inverse proportion to their need in a pure capitalist system and challenges his audience to find ways for businesses and governments to "create measures of what companies are doing to use their power and intelligence to serve a wider circle of people." *Id.*

[4] RICHARD BRANSON, SCREW BUSINESS AS USUAL 96 (2011) ("One of the more devastating theories of the 1970s was that no matter what it took to achieve it, the primary purpose of business was to maximize value for its shareholders. This principle has led to a variety of social ills where businesses discard employees (at the drop of a hat), pollute our air and waters, or create short-term gains that are unsustainable.").

[5] John Elkington, co-founder of the international consultancy SustainAbility, is credited with coining terms like "triple-bottom line" and is recognized as a leading advocate for sustainable development. For more information, see generally Elkington's website, JOHNELKINGTON.COM, http://www.johnelkington.com (last visited Mar. 23, 2013). *See also* JOHN ELKINGTON & PAMELA HARTIGAN, THE POWER OF UNREASONABLE PEOPLE: HOW SOCIAL ENTREPRENEURS CREATE MARKETS THAT CHANGE THE WORLD 1–2 (2008).

[6] BRANSON, *supra* note 4, at 24–25.

that the recent global financial crisis has brought to bear the shortcomings of traditional corporate models, and provides an opportunity for serious reconsideration of corporate governance.[7] Most importantly, they have a growing audience of young social entrepreneurs who want to harness the power of business to address social and environmental problems.[8]

Recent data suggests that the market has begun to take these calls for change seriously; in fact, despite the worst financial crisis since the Great Depression, businesses engaged in socially and environmentally responsible enterprise now enjoy unprecedented financial support.[9] According to a recent report published by the U.S. Social Investment Forum (US-SIF), "assets involved in sustainable and socially responsible investing increased more than 13 percent"[10] from 2007 to 2010, while the broader universe of professionally managed assets remained stagnant.[11] In 2007, 9.4% of total assets under professional management in the United States were involved in socially responsible investing.[12] In the face of a recession, that figure increased to 12.2%, or $3.07 trillion, by 2010.[13] J.P. Morgan estimated that the ten-year profit potential from such investments ranges between $183

---

[7] *See* YUNUS, *supra* note 2, at 29 (suggesting that the current financial crisis provides an opportunity for "bold experimentation"); *see also* Marjorie Kelly, *Not Just for Profit*, 54 STRATEGY+BUSINESS, Feb. 26, 2009, at 4, http://www.strategy-business.com/media/file/enews-02-26-09.pdf (arguing that the best way to avoid future collapses is to redesign corporate ownership and governance); Thomas Kelley, *Law and Choice of Entity on the Social Enterprise Frontier*, 84 TUL. L. REV. 337, 377 (2009) (opining that the current recession may give rise to "an open moment when Americans and their lawmakers may be willing to reconsider the theoretically rigid boundaries between the for-profit and nonprofit sectors"). *See generally* Engobo Emeseh et al., *Corporations, CSR and Self Regulation: What Lessons from the Global Financial Crisis?*, 11 GERMAN L. J. 230 (2010).

[8] David Gergen, *The New Engines of Reform*, U.S. NEWS & WORLD REP., Feb. 20, 2006, at 48 (identifying social enterprise as one of the "hottest movements" among young people in the United States); *see also* BRANSON, *supra* note 4, at 2 ("Just making money, in order simply to give it away, is out of date. There's a massive generational shift occurring that will blur the distinction between doing good and doing business.").

[9] *See* Katharine V. Jackson, *Towards a Stakeholder-Shareholder Theory of Corporate Governance: A Comparative Analysis*, 7 HASTINGS BUS. L.J. 309, 327 (2011); Tom Zeller, Jr., *Can Business Do the Job All by Itself?*, N.Y. TIMES, Mar. 28, 2010, http://www.nytimes.com/2010/03/29/business/energy-environment/29green.html (socially responsible investing is growing more popular because U.S. institutional investors are increasingly recognizing that "doing good ... also enhance[s] shareholder value").

[10] SOC. INV. FORUM FOUND., REPORT ON SOCIALLY RESPONSIBLE INVESTING TRENDS IN THE UNITED STATES 8 (2010), http://ussif.org/resources/research/documents/2010TrendsES.pdf [hereinafter 2010 US-SIF REPORT].

[11] *Id.*

[12] Alina Tugend, *Picking Stocks That Don't Sin*, N.Y. TIMES, Mar. 17, 2007, https://www.nytimes.com/2007/03/17/business/17shortcuts.html?pagewanted=print.

[13] *Id.*

billion and $667 billion.[14] The growth of social enterprise is now so pronounced that in 2011, for the first time in its ninety-four-year history, *Forbes Magazine* released the "Impact 30," a list of the world's leading social entrepreneurs.[15]

As a result, the legal frustrations of social entrepreneurs who seek to simultaneously pursue profits and social or environmental benefits have taken center stage. A 2007 poll showed that 71% of social entrepreneurs considered the choice of entity to be the single greatest challenge for their enterprise,[16] reflecting a general dissatisfaction with the for-profit/nonprofit dichotomy offered by traditional corporate law.[17] These frustrations stem from the fact that for-profit entities are beholden to the overriding influence of profit-maximization at the expense of social or environmental goals, while nonprofits have charitable goals as their polestar, but are prohibited from distributing profits.[18] This Article focuses on corporate law's response in both Europe and the United States to this increasing demand for innovative corporate entities. In doing so, the author hopes to illustrate two main points: first, that social enterprise is a truly global movement; and second, that the newly authorized entities lie on a surprisingly broad spectrum of approaches to social enterprise.

Some commentators have observed that corporate law does not formally enslave all businesses to shareholder wealth maximization, but rather explicitly permits for-profit entities to make significant contributions to charity.[19] Others have contended that the flexible approach desired by social entrepreneurs is made possible through constituency statutes,[20] which

---

[14] J.P. MORGAN GLOBAL RESEARCH, IMPACT INVESTMENTS: AN EMERGING ASSET CLASS 6 (2010), http://www.jpmorgan.com/directdoc/impact_investments_nov2010.pdf; *see also* William H. Clark, Jr. & Elizabeth K. Babson, *How Benefit Corporations Are Redefining the Purpose of Business Corporations*, 38 WM. MITCHELL L. REV. 817, 822–23 (2012).

[15] Helen Coster, *Forbes' List of the Top 30 Social Entrepreneurs*, FORBES (Nov. 30, 2011, 11:48 AM), http://www.forbes.com/sites/helencoster/2011/11/30/forbes-list-of-the-top-30-social-entrepreneurs/.

[16] ALLEN R. BROMBERGER, PERLMAN & PERLMAN LLP, SOCIAL ENTERPRISE: A LAWYER'S PERSPECTIVE 2 (2008), *available at* http://www.perlmanandperlman.com/publications/articles/2008/socialenterprise.pdf; *see also* Robert A. Katz & Antony Page, *The Role of Social Enterprise*, 35 VT. L. REV. 59, 85 (2010) [hereinafter Katz & Page, *Role of Social Enterprise*].

[17] Dana Brakman Reiser, *Benefit Corporations—A Sustainable Form of Organization?*, 46 WAKE FOREST L. REV. 591, 591 (2011) ("Social entrepreneurs believe social good can be produced along with profits and desire hybrid forms of organization to smooth a single enterprise's path to realizing both goals."); *see also* Katz & Page, *supra* note 16, at 86–93; Kelley, *supra* note 7, at 339.

[18] *See generally* Kelley, *supra* note 7.

[19] Einer Elhauge, *Sacrificing Corporate Profits in the Public Interest*, 80 N.Y.U. L. REV. 733, 763 (2005).

[20] Janet E. Kerr, *Sustainability Meets Profitability: The Convenient Truth of How the Business Judgment Rule Protects a Board's Decision to Engage in Social Entrepreneurship*,

have been enacted in over thirty states.[21] In theory these options appear adequate, but in practice, they fall far short of addressing the needs of social entrepreneurs. In reality, profit-maximization continues to dictate business decisions, and constituency statutes require no material change to business as usual.[22]

On the other hand, social enterprise entities stand in stark contrast to corporate law's heretofore passive responses to the demands of social entrepreneurs. These entities straddle the divide between for-profit and nonprofit and seek to blend the production of shareholder wealth with social and environmental goals under the umbrella of a single entity.[23] In looking at recently authorized entities in Europe and the United States, this Article finds considerable support for the contention that social enterprise is an international movement.[24] The thesis here is that while the social enterprise revolution rages on in various sectors of the economy like energy, construction, and transportation, corporate law is on the precipice of a momentous sea-change whose hallmark will be social enterprise entities that consider the interests of shareholders and stakeholders alike.[25]

---

29 CARDOZO L. REV. 623, 634 (2007); *see also* Stephen M. Bainbridge, *Interpreting Nonshareholder Constituency Statutes*, 19 PEPP. L. REV. 971, 973–74 (1992).

[21] John Tyler, *Negating the Legal Problem of Having "Two Masters": A Framework for L3C Fiduciary Duties and Accountability*, 35 VT. L. REV. 117, 132–39 (2010).

[22] *See id.* at 134.

[23] *See* Kelley, *supra* note 7, at 340. In this sense, the author concurs with Kelley's observation that we are witnessing the emergence of a "fourth sector" of our economy that encompasses elements of both business and nonprofit sectors. *Id.*; *see also* Heerad Sabeti, *The For-Benefit Enterprise*, HARV. BUS. REV., Nov. 2011, at 99–104 ("With formalization of the for-benefit structure, we will see the emergence of a fourth sector of the economy, interacting with but separate from governments, nonprofits, and for-profit businesses.").

[24] Rosemary E. Fei, *Beyond Taxation: A Guide to Social Enterprise Vehicles*, 22 TAXATION OF EXEMPTS, Jan.-Feb. 2011, at 13–14 ("More so than in many areas of law, social enterprise is international in practice. Different national legal regimes—themselves in different stages of development—have responded more or less quickly and in a variety of ways to the challenge of creating new legal constructs for operating activities that are not quite business as usual, nor charity as usual, nor even social change as usual."); *see also* Alissa Mickels, Note, *Beyond Corporate Social Responsibility: Reconciling the Ideals of a For-Benefit Corporation with Director Fiduciary Duties in the U.S. and Europe*, 32 HASTINGS INT'L & COMP. L. REV. 271, 292–94 (2009) (noting a global trend towards stakeholder-centered corporate governance models). While this Article focuses on social enterprise in the United States and Europe, social enterprise is not limited to those continents. Some commentators have observed the beginnings of the social enterprise revolution in Asia. *See, e.g.*, Rosario Laratta, *The Emergence of the Social Enterprise Sector in Japan*, 9 INT'L J. CIV. SOC'Y L. 35, 49 (2011); Rebecca Lee, *The Emergence of Social Enterprises in China: The Quest for Space and Legitimacy*, 2 TSINGHUA CHINA L. REV. 79, 84–91 (2009).

[25] *See* Sabeti, *supra* note 23, at 99.

But what, exactly, is meant by "social enterprise?" Definitions range from simply "the use of market-based strategies to promote the public good"[26] to complex factor-based analyses of an organization's profit distribution and management structure.[27] Professors Robert Katz and Antony Page adopt Paul Light's definition, to wit: "an organization or venture that achieves its primary social or environmental mission using business methods, typically by operating a revenue-generating business."[28] In contrast, in 2002 the U.K. Department of Trade and Industry published *Social Enterprise: A Strategy for Success*, which defined social enterprise as "a business with primarily social objectives whose surpluses are principally reinvested for that purpose in the business or in the community, rather than being driven by the need to maximise profit for shareholders and owners."[29] European commentator Jacques Defourny suggests several criteria to determine the existence of a social enterprise, including "[a] continuous activity producing goods and/or selling services," "[a] high degree of autonomy," "[a] minimum amount of paid work," "[a]n explicit aim to benefit the community," "[a] participatory nature, which involves the various parties affected by the activity," and "limited profit distribution."[30]

Despite the infancy of social enterprise, much ink has already been spilt attempting to define it. This Article submits that the distinction between European social enterprise and American social enterprise prevents the crafting of an internationally acceptable definition. Most European jurisdictions view social enterprise as an alternative to traditional charities,[31] while the

---

[26] Briana Cummings, Note, *Benefit Corporations: How to Enforce a Mandate to Promote the Public Interest*, 112 COLUM. L. REV. 578 (2012); *see also* James J. Fishman, *Wrong Way Corrigan and Recent Developments in the Nonprofit Landscape: A Need for New Legal Approaches*, 76 FORDHAM L. REV. 567, 598 (2007) (defining social enterprise as "for-profit vehicles committed to philanthropic activity"); Kyle Westaway, *Something Republicans and Democrats Can Agree On: Social Entrepreneurship*, STAN. SOC. INNOVATION REV. (Apr. 17, 2012), http://www.ssireview.org/blog/entry/something_republicans_and_democrats_can_agree_on_social_entrepreneurship (defining social enterprise as "market-based solutions to social and environmental problems").

[27] *See* Jacques Defourny, *Social Enterprise in an Enlarged Europe: Concept and Realities* (1994), *available at* http://www.emes.net/fileadmin/emes/PDF_files/Articles/Defourny/Defourny.Soc.ent.CEE.3.06.pdf (excerpt from conference paper).

[28] Katz & Page, *supra* note 16, at 59 (quoting PAUL C. LIGHT, THE SEARCH FOR SOCIAL ENTREPRENEURSHIP 5 (2008)) (internal quotation marks and footnotes omitted).

[29] DEP'T OF TRADE & INDUS., SOCIAL ENTERPRISE: A STRATEGY FOR SUCCESS 7 (2002), *available at* http://www.seeewiki.co.uk/~wiki/images/5/5a/SE_Strategy_for_success.pdf.

[30] Defourny, *supra* note 27, at 9–10. Defourny's criteria represent an "ideal-type" of social enterprise, and are not conditions precedent to an entity qualifying as a social enterprise. He suggests that they should be used as "a tool, somewhat analogous to a compass, which can help the researchers locate the position of certain entities relative to one another." *Id.* at 11.

[31] *See* Jacques Defourny & Marthe Nyssens, *Social Enterprise in Europe: Recent Trends and Developments*, 4 SOC. ENTERPRISE J. 202, 204 (2008).

United States has embraced a broader view of social enterprise as an emerging "fourth sector" of the economy, wherein profit maximization may be usurped by social or environmental goals.[32]

In addition, other new and related terms such as "social business," "social entrepreneurship," "impact investing," and "corporate social responsibility" are being used with increased frequency in business and legal literature and merit a brief review. "Social business" is a term coined by Muhammad Yunus, a renowned economist and the father of the microfinance industry.[33] According to Yunus, a social business is either a "non-loss, non-dividend company devoted to solving a social problem and owned by investors who reinvest all profits,"[34] or "a profit-making company owned by poor people."[35] For Yunus, the defining characteristic of social business is the prohibition on profit-distribution to wealthy investors.[36] In this respect, social business represents a subcategory of social enterprise, which in many cases embraces profit distribution. "Social entrepreneurship," in contrast, is a broader term generally referring to any venture that creates social or environmental benefits.[37] Such activities range from corporate social responsibility initiatives to double- or triple-bottom line investment techniques.[38] "Impact investing," a form of social entrepreneurship, is also known as "mission investing, responsible investing, double or triple bottom line investing, ethical investing, sustainable investing, or green investing."[39] These terms are used interchangeably and refer in general to "an investment discipline that considers environmental, social and corporate governance criteria to generate long-term competitive financial returns and positive societal impact."[40] Impact investing is largely fueled by socially responsible investment funds.[41] These institutional funds take into account nonfinancial and social benefit considerations when screening potential investment opportunities by either avoiding companies engaged in socially or environmentally harmful activities or actively seeking

[32] Kelly, *supra* note 7, at 340.

[33] *See generally* YUNUS, *supra* note 2.

[34] *Id.* at 1.

[35] *Id.* at 2.

[36] *Id.*

[37] *See id.* at 4.

[38] *See* Defourny & Nyssens, *supra* note 31, at 203; Kelly, *supra* note 7, at 339.

[39] *Sustainable and Responsible Investing Facts*, US-SIF, http://ussif.org/resources/sriguide/srifacts.cfm (last visited Mar. 23, 2013).

[40] 2010 US-SIF REPORT, *supra* note 10, at 13; *see also Sustainable and Responsible Investing Facts*, *supra* note 39.

[41] *See, e.g.*, *Our Fund*, GOOD CAPITAL, http://www.goodcap.net/ourfund.php (last visited Mar. 23, 2013).

companies engaged in positive pursuits.[42] Finally, "corporate social responsibility" (CSR) is a term that has largely defied definition but is loosely based around notions of voluntary corporate transparency.[43] Some commentators have observed that CSR lacks any identifiable manifestation or consensus on regulatory enforcement,[44] a shortcoming responsible for CSR's failure to square voluntary corporate transparency with perceived ethical imperatives.[45] While many welcome CSR's emphasis on corporate transparency, social enterprise and its accompanying emerging entities go much further than CSR's malleable, voluntary approach.[46]

Social enterprise advocates argue that their model of corporate governance will benefit society and the environment, and will also be good for business.[47] Early studies appear to confirm this assertion.[48] Furthermore, as Professors Katz and Page note, by creating a "fourth sector" of the economy, social enterprise largely sidesteps the longstanding debate regarding shareholder wealth maximization by offering new entities with blended corporate purposes.[49] Lastly, and most pragmatically, these entities have consistently received bipartisan political support.[50] As Kyle Westaway, founder of the social enterprise boutique firm Westaway Law, explains: "Liberals love [social enterprise] because it proves that business can be socially and environmentally

---

[42] Kelley, *supra* note 7, at 358.

[43] *See* JENNIFER A. ZERK, MULTINATIONALS AND CORPORATE SOCIAL RESPONSIBILITY: LIMITATIONS AND OPPORTUNITIES IN INTERNATIONAL LAW 30–31 (2006) (discussing multiple views of CSR and clarifying CSR as distinct from concepts of corporate governance); Larry Catá Backer, *From Moral Obligation to International Law: Disclosure Systems, Markets and the Regulation of Multinational Corporations*, 39 GEO. J. INT'L L. 591, 617 (2008) [hereinafter Backer, *Moral Obligation*] (noting that there is no consensus on the definition and value of CSR); Jackson, *supra* note 9, at 325 n.112 (citing CSR EUROPE, A GUIDE TO CSR IN EUROPE: COUNTRY INSIGHTS BY CSR 2 (Oct. 2009)).

[44] Backer, *supra* note 43, at 617.

[45] *See* ZERK, *supra* note 43, at 30.

[46] *See* Kelly, *supra* note 7, at 350–51.

[47] *See* Kerr, *supra* note 20, at 634–35.

[48] BRANSON, *supra* note 4, at 25 (quoting a FTSE study finding that "companies that consistently manage and measure their responsible business activities outperformed their FTSE 350 peers on total shareholder return in seven out of the last eight years"); *see also* Kerr, *supra* note 20, at 634–35.

[49] *See* Antony Page & Robert A. Katz, *Is Social Enterprise the New Corporate Social Responsibility?*, 34 SEATTLE U. L. REV. 1351, 1353 (2011) [hereinafter Page & Katz, *New Corporate Social Responsibility*].

[50] Kyle Westaway, *New York Unanimously Passes Benefit Corporation Bill*, SOCENTLAW (July 6, 2011), http://socentlaw.com/2011/07/new-york-unanimously-passes-benefit-corporation-bill (noting that a recent bill authorizing benefit corporations passed in the New York legislature by a 62-0 vote in the Senate and a 139-0 vote in the Assembly).

responsible. Conservatives love it because it offers the free market, not government, as the solution to social and environmental problems."[51]

The benefit corporation is one of the latest developments in the social enterprise revolution in corporate law. In 2011, benefit corporations statutes were enacted in five states[52] and proposed legislation was introduced in four others.[53] As of March 2013, benefit corporations are authorized in twelve states and the District of Columbia.[54] Furthermore, 2011 also witnessed the introduction of two additional social enterprise entities—namely, the flexible purpose corporation (FPC) and the social purpose corporation (SPC).[55]

This Article identifies a number of recently enacted entities in Europe and the United States and argues that the benefit corporation is currently the most effective in achieving the blended value goals of the social enterprise movement.[56] To that end, Part I provides a background on corporate responsibility and discusses the failure to effectively regulate the world's largest corporations.[57] Part II introduces the concept of social enterprise from a European perspective and highlights the differences between continental Europe's social cooperatives and the U.K.'s Community Interest Company.[58] Part III turns to social enterprise in the United States and identifies several emerging entities, including low-profit limited liability companies (L3Cs), flexible purpose corporations, social purpose corporations, and benefit corporations.[59]

---

[51] *Id.*

[52] CAL. CORP. CODE §§ 14600–14631 (West 2012) (effective Jan. 1, 2012); HAW. REV. STAT. §§ 420D-1 to -13 (2012) (effective July 8, 2011); N.J. STAT. ANN. §§ 14A:18-1 to -11 (West, Westlaw current through L.2012, c. 45 and J.R. No. 1) (effective Mar. 1, 2011); New York, N.Y. BUS. CORP. LAW §§ 1701–1709 (McKinney 2012) (effective Feb. 10, 2012); VA. CODE ANN. §§ 13.1-782 to -791 (2012); *see also Passing Legislation*, B CORP., http://www.bcorporation.net/what-are-b-corps/legislation (last visited Mar. 23, 2013).

[53] S.B. 11-005, 68th Gen. Assemb., Reg. Sess. (Colo. 2011); S.B. 359, 96th Leg., Reg. Sess. (Mich. 2011); S.B. 360, 96th Leg., Reg. Sess. (Mich. 2011); H.B. 4615, 96th Leg., Reg. Sess. (Mich. 2011); H.B. 4616, 96th Leg., Reg. Sess. (Mich. 2011); S.B. 26, 2011-12 Gen. Assemb., Reg. Sess. (N.C. 2011); S.B. 433, 195th Leg., Reg. Sess. (Pa. 2011); H.B. 1616, 195th Leg., Reg. Sess. (Pa. 2011); *see also Passing Legislation*, B CORP., *supra* note 52.

[54] California, Hawaii, Illinois, Maryland, Massachusetts, Louisiana, New Jersey, New York, Pennsylvania, South Carolina, Vermont, and Virginia have all enacted statutes authorizing benefit corporations. *State by State Legislative Status*, BENEFIT CORP INFO. CENTER, http://www.benefitcorp.net/state-by-state-legislative-status (last visited Mar. 23, 2013).

[55] CAL. CORP. CODE § 2502, et seq. (West 2012); S.H.B. 2239, 62d Leg., Reg. Sess. (Wash. 2012).

[56] Kelly, *supra* note 7, at 10 (arguing that alternative corporate designs "are likely to prove better adapted to the cultural and ecological demands of the 21st century than the industrial age models they might one day replace").

[57] *See infra* Part I.

[58] *See infra* Part II.

[59] *See infra* Part III.

Based on an analysis of emerging social enterprise corporate forms on both continents, Part IV concludes that the benefit corporation most successfully integrates the flexibility and accountability required for social enterprise's blended value goals.[60] Part IV also addresses some critiques of profit-distribution in social enterprise and suggests possible reforms for future benefit corporation legislation.[61]

I. A REVIEW OF CORPORATE RESPONSIBILITY AND REGULATION

In the 1930s, Adolf Berle and E. Merrick Dodd pioneered the field of corporate governance scholarship; indeed, many find the genesis of the modern debate surrounding corporate responsibility in the 1931–1932 issues of the *Harvard Law Review*.[62] Berle advanced a trustee model in which the corporation's directors acted as trustees of corporate property on behalf of the shareholder-beneficiaries.[63] Berle's trustee model is generally seen as the forefather of contractarian shareholder-primacy.[64] On the other hand, Dodd argued that corporations were economic institutions, "which ha[d] a social service as well as a profit-making function."[65] In this sense, Dodd was the predecessor of progressive "communitarian" theories of corporate governance.[66] However, as some commentators have observed, the legal debate has

---

[60] *See infra* Part IV.

[61] *See infra* Part IV.

[62] *Compare* Adolf A. Berle, Jr., *Corporate Powers as Powers in Trust*, 44 HARV. L. REV. 1049, 1049 (1931), *and* Adolf A. Berle, Jr., *For Whom Corporate Managers Are Trustees: A Note*, 45 HARV. L. REV. 1365, 1365–66 (1932), *with* E. Merrick Dodd, Jr., *For Whom Are Corporate Managers Trustees?*, 45 HARV. L. REV. 1145, 1147–48 (1932). For a more thorough history of the debate, see generally Bainbridge, *supra* note 20; Page & Katz, *New Corporate Social Responsibility*, *supra* note 49, at 1354–61.

[63] *See* ADOLF A. BERLE, JR. & GARDINER C. MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY 7 (1932).

[64] Page & Katz, *New Corporate Social Responsibility*, *supra* note 49, at 1356; *see also* Henry Hansmann & Reinier Kraakman, Essay, *The End of History for Corporate Law*, 89 GEO. L.J. 439, 444 n.6 (2001); Bainbridge, *supra* note 20, at 972 ("Berle contended that ... the board of directors should operate the corporation for the sole benefit of the shareholders."); *cf.* Page & Katz, *New Corporate Social Responsibility*, *supra* note 49, at 1357–58 (emphasizing that Berle's views evolved over time, and that by 1954, Berle had expressed a preference for a more communitarian model of corporate governance).

[65] Dodd, *supra* note 62, at 1148; *see also* Bainbridge, *supra* note 20, at 972–73 ("Dodd ... saw shareholders as absentee owners whose interests can be subjugated to those of other corporate constituencies and those of society at large.").

[66] In an attempt to broaden the legal literature beyond traditional neoclassical economic analysis, advocates of progressive corporate law adopted a multidisciplinary understanding of corporate law. *See generally* Joel Seligman, *Foreword* to PROGRESSIVE CORPORATE LAW ix (Lawrence E. Mitchell ed., 1995). In doing so, proponents of progressive corporate law

been spinning its wheels since the 1930s.[67] Indeed, more than eight decades later, most commentators acknowledge the failure of the legal debate to resolve these competing interpretations of corporate responsibility.[68]

While the legal debate remained relatively stagnant, multinational corporations[69] (MNCs) continued to grow in size and influence.[70] Indeed, MNCs now

---

challenged shareholder primacy. *See, e.g.*, Lynne L. Dallas, *Working Toward a New Paradigm*, *in* PROGRESSIVE CORPORATE LAW, *supra*, at 35, 36 (contending that "market theories define efficiency too narrowly and that efficiency cannot be separated from concepts of social justice and normative goals"); David Millon, *Communitarianism in Corporate Law: Foundations and Law Reform Strategies*, *in* PROGRESSIVE CORPORATE LAW, *supra*, at 1, 1 ("[Progressives] ha[ve] challenged corporate law's traditional commitment to the shareholder primacy principle ... [catalyzed by] concern about the harm to nonshareholders that can occur as a result of managerial adherence to the shareholder primacy principle."); Lawrence E. Mitchell, *Trust. Contract. Process.*, *in* PROGRESSIVE CORPORATE LAW, *supra*, at 185, 187 (criticizing contractarian models of corporate governance as "necessarily limit[ing] the room available for trust," which in turn encourages parties to act entirely out of self-interest and "ultimately damages the fabric of a community").

[67] Stephen M. Bainbridge, Book Review, *Community and Statism: A Conservative Contractarian Critique of Progressive Corporate Law Scholarship*, 82 CORNELL L. REV. 856, 902–03 (1997) ("In the 1930s, we had the Berle-Dodd debate. In the 1950s, Berle and others revisited the issue. In the 1970s, there was a major fracas over corporate social responsibility. Finally, today we have the nonshareholder constituency debate.... [E]ach iteration adopts a new terminology, focuses on a slightly different facet of the problem, and develops some new ideas. But, all-in-all, we have been here before." (footnotes omitted)); *see also* Page & Katz, *New Corporate Social Responsibility*, *supra* note 49, at 1360–61.

[68] *See* Lewis D. Solomon, *On the Frontier of Capitalism: Implementation of Humanomics by Modern Publicly Held Corporations—A Critical Assessment*, *in* PROGRESSIVE CORPORATE LAW, *supra* note 66, at 281 ("This controversy regarding corporate goals and stakeholder interests has spanned most of the twentieth century."); Page & Katz, *supra* note 49, at 1361 ("[A]lthough CSR may have good ideas about corporate behavior, it has generally failed to produce meaningful large-scale legal reform."); C.A. Harwell Wells, *The Cycles of Corporate Social Responsibility: An Historical Retrospective for the Twenty-first Century*, 51 U. KAN. L. REV. 77, 78 (2002). *But see* Lynn A. Stout, *Bad and Not-So-Bad Arguments for Shareholder Primacy*, 75 S. CAL. L. REV. 1189, 1190 (2002) (arguing that there has been "some intellectual progress" in the area of corporate responsibility).

[69] The author acknowledges that the definition of the term "multinational" has evolved since it was coined by David E. Lilienthal in 1960. *See* PETER T. MUCHLINSKI, MULTINATIONAL ENTERPRISES & THE LAW 5 (2d ed. 2007) (quoting D.K. Fieldhouse, *The Multinational: A Critique of a Concept*, *in* MULTINATIONAL ENTERPRISE IN HISTORICAL PERSPECTIVE 9, 10 (Alice Teichova et al. eds., 1986)). For the purposes of this Article, the author adopts the OECD's definition of "multinational," which emphasizes the degree to which one entity exerts control and influence over other entities located in different jurisdictions. *See id.* at 52–53; ZERK, *supra* note 43, at 51 (observing that most general-purpose definitions of multinational now emphasize relationships of control instead of ownership relationships between entities).

[70] *See* Gralf-Peter Calliess, *Introduction: Transnational Corporations Revisited*, 18 IND. J. GLOBAL LEGAL STUD. 601, 606 (2011).

have revenues that exceed the Gross Domestic Product (GDP) of many developing countries, allowing them to exert considerable economic and political pressure on governments.[71] Furthermore, as Peter Muchlinski observes, the recent trend in mature MNCs has been one towards heterarchy, not hierarchy, encouraging the geographic spread of functions across international borders.[72] It is this increase in transnational and transjurisdictional operations,[73] working in concert with a shareholder-centric model of corporate governance, which drives MNCs to exploit looser environmental and labor regulations in developing countries.[74]

In response, the international community made attempts to regulate these organizations and hold them accountable for their negative social and environmental outputs.[75] Recent examples of these efforts fall under the umbrella of CSR,[76] achieved through charity funds set aside by a for-profit corporation for good works in local communities,[77] or through "community programs, or holistic decision making" that align with the corporation's profit-making purpose.[78] CSR advocates maintain that it presents an effective alternative

---

[71] JOSEPH E. STIGLITZ, MAKING GLOBALIZATION WORK 187–88 (2006); Issachar Rosen-Zvi, *You Are Too Soft!: What Can Corporate Social Responsibility Do for Climate Change?*, 12 MINN. J. L. SCI. & TECH. 527, 531–32 (2011); *see also* Gralf-Peter Calliess, *supra* note 70, at 613–14 (2011) (discussing Horst Eidenmuller's observations that law protecting public interests is frequently circumvented by transnational corporations and Karsten Nowrot's suggestion that transnational corporations be more deeply integrated within the international legal process); Dan Danielsen, *How Corporations Govern: Taking Corporate Power Seriously in Transnational Regulation and Governance*, 46 HARV. INT'L L.J. 411, 412 (2005) (discussing the myriad of ways in which corporations engage in and exercise influence on governance); Issachar Rosen-Zvi, *You Are Too Soft!: What Can Corporate Social Responsibility Do for Climate Change?*, 12 MINN. J.L. SCI. & TECH. 527, 531–32 (2001). *See generally* Gralf-Peter Calliess & Jens Mertens, *Transnational Corporations, Global Competition Policy, and the Shortcomings of Private International Law*, 18 IND. J. GLOBAL LEGAL STUD. 843 (2011).

[72] MUCHLINSKI, *supra* note 69, at 45–49 (citing BP, General Electric, and IBM as examples of multinational enterprises that "have moved towards a more flexible and innovation driven structure"); *see also* CHRISTOPHER A. BARTLETT ET AL., TRANSNATIONAL MANAGEMENT: TEXT CASES AND READINGS IN CROSS-BORDER MANAGEMENT 774–813, (McGraw Hill Irwin Press, 4th ed. 2004).

[73] *See generally* ZERK, *supra* note 43.

[74] *See* Sean D. Murphy, *Taking Multinational Corporate Codes of Conduct to the Next Level*, 43 COLUM. J. TRANSNAT'L L. 389, 399–400 (2005).

[75] *See generally* ZERK, *supra* note 43 (identifying and analyzing several different regulatory approaches to multinational corporations).

[76] *See* Emesh et al., *supra* note 7, at 236–37 (defining CSR as an attempt "to expand the scope of corporate obligations beyond the traditional duty of care to their shareholders recognized by the law but also to their workers and the community in which they operate").

[77] YUNUS, *supra* note 2, at 9.

[78] Steven Munch, Note, *Improving the Benefit Corporation: How Traditional Governance Mechanisms Can Enhance the Innovative New Business Form*, 7 NW. J.L. & SOC. POL'Y 170, 178 (2012).

to government regulation by encouraging more socially and environmentally responsible approaches to corporate governance.[79] Critics counter that CSR's voluntary transparency is simply an attempt to preempt government regulation and protect a corporation's brand image.[80] This Part identifies several examples of CSR, including corporate responsibility reporting (CR reporting), corporate codes of conduct, and constituency statutes.[81] Part I.A concludes that MNCs remain largely unaccountable for their negative social or environmental outputs despite CSR's various manifestations.[82]

Next, Part I.B turns to existing regulation of MNCs.[83] This Part concludes that the combination of jurisdictional hurdles and weak regulatory tools results in a general inability to effectively regulate MNCs, and finds both CSR and existing regulatory tools insufficient for addressing corporate responsibility.[84] While the kneejerk reaction for more regulation has been advanced by some commentators,[85] this Article suggests that the hallmark of the social enterprise movement—the blended corporate purpose—has the potential to change the legal landscape of corporate responsibility.

A. Corporate Responsibility

1. Corporate Responsibility Reporting

Corporate responsibility (CR) reporting is the increasingly widespread practice amongst MNCs of voluntarily reporting their environmental, social, and economic impacts.[86] Indeed, nearly all of the world's largest corporations

---

[79] *See* Guy Mundlak & Issi Rosen-Zvi, *Signaling Virtue? A Comparison of Corporate Codes in the Fields of Labor and Environment*, 12 THEORETICAL INQUIRIES L. 603, 604 (2011); Rosen-Zvi, *supra* note 71, at 537.

[80] Rosen-Zvi, *supra* note 71, at 539.

[81] The author acknowledges that socially and environmentally responsible shareholder proposals have also been another method pursued by CSR. *See* Ian B. Lee, *Corporate Law, Profit Maximization, and the "Responsible" Shareholder*, STAN. J.L. BUS. & FIN., Spring 2005, at 31, 71–72 (discussing the sources of authority for socially responsible investing and supporting the existing availability of shareholder proxies for socially responsible shareholder proposals). However, such shareholder proposals often obtain less than 30% of the votes and are generally voted down. *See* 2010 US-SIF Report, *supra* note 10, at 50 fig.4.6 (showing that in 2010, only 29% of social and environmental shareholder proposals received greater than 30% support). For examples of such proposals related to climate change, see Perry E. Wallace, *Climate Change, Fiduciary Duty, and Corporate Disclosure: Are Things Heating Up in the Boardroom?*, 26 VA. ENVTL. L.J. 293, 322 (2008).

[82] *See infra* Part I.A.4.

[83] *See infra* Part I.B.

[84] *See infra* Part I.C.

[85] *See* Emesh et al., *supra* note 7, at 253–54.

[86] Adam Sulkowski & Steven White, *Financial Performance, Pollution Measures and the Propensity to Use Corporate Responsibility Reporting: Implications for Business and Legal Scholarship*, 21 COLO. J. INT'L ENVTL. L. & POL'Y 491, 492 (2010).

now issue CR reports. KPMG's latest triennial survey of CR reporting shows that, as of 2011, 95% of the Global Fortune 250 (G250) companies engage in some form of CR reporting, up from 81% in 2008.[87] The 2011 KPMG survey also reported that the Global Reporting Initiative (GRI) standards are used by 80% of G250 companies engaged in CR reporting.[88]

At first glance, these statistics seem to suggest that CR reporting has been a great success. Indeed, to the extent CSR aims to require CR reports, it has succeeded. However, critics emphasize that despite its near-universal practice, CR reporting remains voluntary and without any binding legal obligations.[89] Moreover, CR reports are unaudited and fail to require any standardized methodology,[90] calling into question the accuracy of self-reported data.[91] Critics contend that the malleable nature of CR reporting favors corporations, who are free to skew or omit data regarding negative social or environmental outputs.[92]

In addition, recent data suggests that executives increasingly view CR reporting as a public relations tool rather than a vehicle for increased transparency or consideration of stakeholder interests.[93] KPMG's 2011 survey includes polling results from executives of G250 corporations regarding the perceived drivers underlying CR reporting.[94] KPMG's 2008 survey indicated that executives' prime motivators were ethical and economic considerations.[95] However, in the wake of the recession, the leading motivator behind CR reporting shifted to concern for the corporation's reputation and brand image.[96] This rise of brand image as the single greatest driver of CR reporting

---

[87] KPMG, INTERNATIONAL SURVEY OF CORPORATE RESPONSIBILITY REPORTING 2011, at 6–7 (2011), http://www.kpmg.com/PT/pt/IssuesAndInsights/Documents/corporate-responsibility2011.pdf [hereinafter 2011 KPMG SURVEY]; *see also* Sulkowski & White, *supra* note 86, at 494 (identifying and analyzing data from KPMG's 2008 International Survey).

[88] 2011 KPMG SURVEY, *supra* note 87, at 20–21; *see also* Sulkowski & White, *supra* note 86, at 494.

[89] *See* Rosen-Zvi, *supra* note 71, at 531–34. *See generally* ZERK, *supra* note 43.

[90] *See* Rosen-Zvi, *supra* note 71, at 543–44; Jackson, *supra* note 9, at 389–90.

[91] *See* Rosen-Zvi, *supra* note 71, at 543–44; Jackson, *supra* note 9, at 389–90.

[92] *See* 2011 KPMG SURVEY, *supra* note 87, at 26 ("Unlike financial reporting, the disclosure of sustainability metrics to the market is largely unregulated."); Jackson, *supra* note 9, at 389.

[93] *See* 2011 KPMG SURVEY, *supra* note 87, at 18–19.

[94] *Id.* at 19.

[95] KPMG, INTERNATIONAL SURVEY ON CORPORATE RESPONSIBILITY REPORTING 2008, at 18 (2008), *available at* http://www.kpmg.com/global/en/issuesandinsights/articlespublications/pages/sustainability-corporate-responsibility-reporting-2008.aspx; *see also* Sulkowski & White, *supra* note 86, at 496–98, 498 n.41.

[96] 2011 KPMG SURVEY, *supra* note 87, at 18–19 (reporting that the number one motivator behind CR reporting was "reputation/brand" with 67%; "ethical considerations" trailed

today raises the specter of "greenwashing" and appears to justify the healthy skepticism regarding the accuracy and comprehensiveness of these reports.[97]

Furthermore, critics emphasize that CR reporting fails to involve board members in the process. Indeed, a majority of G250 directors have no direct involvement with CR reports, resulting in a failure to embed CSR's social and environmental goals in the highest levels of the corporate decision-making process.[98] Additionally, CR reports are seldom issued in conjunction with, or included in, a corporation's annual financial report.[99] This practice reflects a purposeful attempt to avoid government oversight of CR reports, as explained by consultants at KPMG:

> The current practice of a separate CSR report (regardless of the medium used) from the annual report leaves freedom in reporting in terms of the associated legal risks. An annual report comes with specific reporting requirements, external oversight and legal accountability towards parties with a financial interest in the company. Therefore, if integrated reporting is approached as integrating CSR information (and other business-impacting information) into the annual report, additional legal risks can appear that you would rather avoid.[100]

Moreover, critics argue that CR reporting does not ensure any standardized methodology, which leads to inaccurate results. In conducting an empirical study on thirty MNC's CR reports to assess their effectiveness regarding efforts to combat climate change, Issachar Rosen-Zvi highlights how variances in methodology allow major energy companies to effectively hide significant greenhouse gas emissions,[101] and permit major automobile manufacturers to choose the most favorable baseline years from which their greenhouse gas emissions are measured.[102] Additionally, many CR reporting standards against

---

significantly behind at number two with 58%, and "economic considerations" dropped off significantly to just 32%).

[97] *See* ZERK, *supra* note 43, at 100–01 ("Some multinationals have seen their environmental initiatives dismissed as 'greenwash', while others have been accused of using CSR-related initiatives as a way of diverting attention away from bad press elsewhere or as a tactical concession to avoid more stringent legislation at some later stage." (footnotes omitted)).

[98] 2011 KPMG SURVEY, *supra* note 87, at 27 ("[N]early half of the reporting companies either do not disclose—or possibly do not have—board member responsibility or involvement, which would be a key condition to embedding CR reporting into an organization.").

[99] KPMG, INTEGRATED REPORTING: CLOSING THE LOOP OF STRATEGY 3 (April 2010) [hereinafter INTEGRATED REPORTING], http://www.kpmg.com/GR/en/IssuesAndInsights/ArticlesPublications/Sustainability/Documents/Sustainable-insight-April-2010.pdf; *see also* 2011 KPMG SURVEY, *supra* note 87, at 23 (indicating that only 27% of the G250 corporations include some form of CR reporting in their annual report).

[100] INTEGRATED REPORTING, *supra* note 99, at 8.

[101] Rosen-Zvi, *supra* note 71, at 543–48.

[102] *Id.* at 548–52.

which MNCs measure their practices, such as the GRI Guidelines, the American Society of Testing and Materials (ASTM) standards, the International Organization for Standardization (ISO) 14000 International Environmental Standards, and the Coalition for Environmentally Responsible Economies (CERES) Principles, fail to provide any mathematical formula or valuation metric for a corporation's social and environmental benefits.[103]

In sum, CR reporting is increasingly recognized for what it is—a public relations tool that pays lip service to increased corporate transparency but does little, if anything, to alter the corporate decision-making process.[104]

2. Corporate Codes of Conduct

Modern corporate codes of conduct are not a recent development and are now common in many jurisdictions.[105] In theory, codes serve to "enhance corporations' social and environmental commitments by articulating the norms and standards by which they profess to be bound."[106] Like CR reporting, most corporate codes of conduct are voluntary.[107] However, the current voluntary promulgation and adherence to codes of conduct belies the original intent of modern codes.[108] Indeed, codes promulgated in the 1970s had a distinctly international flavor and were originally devised as third party regulatory tools for international organizations (IOs).[109] To that end, IOs like the United Nations (UN),[110] the Organization for Economic

---

[103] *But see* Allison M. Snyder, *Holding Multinational Corporations Accountable: Is Non-Financial Disclosure the Answer?*, 2007 COLUM. BUS. L. REV. 565, 593 (2007) (noting that, in contrast to GRI and other popular CR reporting standards, the CSI Social Footprint does provide mathematical valuation for a corporation's social and environmental benefits).

[104] Snyder, *supra* note 103, at 605 ("Empirical evidence illustrates that corporations do, in fact, use reports as a form of public relations and often fail to take social concerns seriously.").

[105] *See generally Index of Codes*, EUR. CORP. GOVERNANCE INST., http://www.ecgi.org/codes/all_codes.php (last visited Mar. 23, 2013) (providing links to corporate codes of conduct in over 80 jurisdictions).

[106] Rosen-Zvi, *supra* note 71, at 537; *see also* Ans Kolk & Rob van Tulder, *Setting New Global Rules? TNCs and Codes of Conduct*, 14 TRANSNAT'L CORPS. 1, 3–4 (2005) (arguing that companies may also develop codes for the purpose of influencing other societal actors).

[107] Rosen-Zvi, *supra* note 71, at 537.

[108] For a more thorough historical analysis of corporate codes of conduct, see Mark B. Baker, *Promises and Platitudes: Toward a New 21st Century Paradigm for Corporate Codes of Conduct?*, 23 CONN. J. INT'L L. 123, 125–29 (2007).

[109] *See id.* at 126–27, 129.

[110] The UN Commission on Transnational Corporations (UNCTC) was charged with drafting a code of conduct for transnational corporations in 1976. *Background and Activities of the Commission and the Centre on Transnational Corporations*, UNITED NATIONS CONFERENCE ON TRADE & DEV., http://unctc.unctad.org/aspx/UNCTC%20from%201976%20to%201979.aspx (last updated June 13, 2003).

Co-operation and Development (OECD),[111] and the International Labor Organization (ILO)[112] promulgated mandatory codes of conduct for multinationals. Efforts at enforcement, however, proved largely unsuccessful. Professor José Alvarez argues that the Reagan Administration, concerned over the potential impact of the "The New Regulatory Order"[113] on U.S. corporations, joined with business interests to defeat efforts to promulgate enforceable codes of conduct, or to shift negotiations to more favorable fora.[114] This approach proved successful. The UNCTC's efforts were abandoned in 1993 after fourteen years of unsuccessful negotiations.[115] Both the OECD's Declaration and the ILO's Tripartite Declaration survive, but they remain voluntary and "toothless"[116] soft law.[117] At most, these declarations are "part of an important inter-organizational dialogue concerning the legal responsibilities of multinational corporations[,]"[118] but they fail to effect any

---

[111] The governments of OECD Member Countries adopted the Declaration on International Investment and Multinational Enterprises on June 21, 1976. *See* ORGANISATION FOR ECON. CO-OPERATION & DEV., INTERNATIONAL INVESTMENT AND MULTINATIONAL ENTERPRISES 15–22 (1984). As of May 2011, all thirty-four OECD Members, Argentina, Brazil, Chile, and seven other non-OECD countries have adopted the Declaration. *OECD Declaration on International Investment and Multinational Enterprises*, OECD (May 25, 2011), http://www.oecd.org/daf/internationalinvestment/investmentpolicy/oecddeclarationoninternationalinvestmentandmultinationalenterprises.htm.

[112] INT'L LABOR ORG., TRIPARTITE DECLARATION OF PRINCIPLES CONCERNING MULTINATIONAL ENTERPRISES AND SOCIAL POLICY (Nov. 16, 1977), *reprinted in* 17 I.L.M. 422, 423 (1978).

[113] JOSÉ E. ALVAREZ, INTERNATIONAL ORGANIZATIONS AS LAW-MAKERS 255 (Oxford Univ. Press, 2005) (citing Jeane J. Kirkpatrick, *Foreword* to INTERNATIONAL REGULATION: NEW RULES IN A CHANGING WORLD ORDER (Carol C. Adelman ed., 1988)).

[114] *Id.*

[115] *See UNCTC Evolution*, UNITED NATIONS CONFERENCE ON TRADE & DEV., http://unctc.unctad.org/aspx/UNCTCEvolution.aspx (last visited Mar. 23, 2013) (describing the 1993 dissolution of the UNCTC and the transfer to the UNCTAD). In 2003, the UN promulgated the *Norms on the Responsibilities of Transnational Corporations and Other Business Enterprises with Regard to Human Rights*, U.N. Doc. E/CN.4/Sub.2/2003/12/Rev.2 (Aug. 13, 2003), *available at* http://www1.umn.edu/humanrts/links/norms-Aug2003.html [hereinafter *UN Norms*]. Like its predecessor, the UN Norms were abandoned and replaced with the voluntary Global Compact Project. *See Overview of the UN Global Compact*, UNITED NATIONS GLOBAL COMPACT, http://www.unglobalcompact.org/AboutTheGC/ (last updated Dec. 1, 2011); John H. Knox, *The Human Rights Council Endorses "Guiding Principles" for Corporations*, AM. SOC'Y OF INT'L LAW (Aug. 1, 2011), http://www.asil.org/pdfs/insights/insight110801.pdf.

[116] ALVAREZ, *supra* note 113, at 256.

[117] *Id.* at 230 (noting that the ILO's decision to promulgate these principles as a Declaration "suggests the intent to render this a truly 'soft' form of soft law [and] presumably reflects ... emphasis on affecting the conduct of private entities within states").

[118] *Id.*

substantive changes in and of themselves. At the international level, chances of establishing enforceable codes of conduct on MNCs appear very low.

At the domestic level, some legislators attempted to pick up this torch by proposing legislation that would require MNCs to adopt corporate codes of conduct. However, these bills all died silent deaths in committee. In the United States, former Rep. Cynthia McKinney (D-GA), along with thirty-two cosponsors, introduced the Corporate Code of Conduct Act (CCCA) in June of 2000.[119] The CCCA would require any U.S. corporation employing "more than 20 persons in a foreign country, either directly or through subsidiaries[,] ... [to] take the necessary steps to implement [a] Corporate Code of Conduct."[120] The CCCA was tabled,[121] reintroduced on May 11, 2006 as H.R. 5377,[122] and was tabled again by the House Financial Services Committee.[123] Comparable legislation introduced in Australia[124] and the European Parliament[125] suffered similar fates.

For the moment, it appears that business interests have succeeded in stifling both international and domestic attempts to mandate enforceable corporate codes of conduct. The consistent failures to legislate in this area underscore the lack of political will necessary to pass codes with effective government enforcement and regulatory mechanisms on MNCs.

As a result, corporate codes of conduct have become increasingly individualistic,[126] vesting MNCs with broad discretion in drafting and enforcement. MNCs are free to choose whether to author codes independently or with stakeholder representatives, and whether to adopt unilateral codes, codes promulgated by industry groups, or model codes promulgated by international organizations or trade unions.[127] Mark Baker argues that these options offer the benefit of flexibility, but that the resulting codes are flawed insofar as they: (i) fail to contain any specific content requirement;[128] (ii) do

[119] Baker, *supra* note 108, at 155–56.
[120] *Id.* at 156–57.
[121] *Id.* at 156.
[122] H.R. 5377, 109th Cong. (2006).
[123] *See H.R. 5377 (109th): Corporate Code of Conduct Act*, GOVTRACK.US, http://www.govtrack.us/congress/bills/109/hr5377 (last visited Mar. 23, 2013). No further action has been taken by Congress.
[124] ZERK, *supra* note 43, at 165–66 (noting that the Australian Code of Conduct Bill was not recommended by the Statutory Committee).
[125] *Id.* at 170 (noting that the European Parliament's Resolution on a Voluntary Code of Conduct for European Enterprises Operating in Developing Countries was never formally implemented).
[126] *See* Baker, *supra* note 108, at 129.
[127] Rosen-Zvi, *supra* note 71, at 538.
[128] Baker, *supra* note 108, at 131.

not ensure they will be taken seriously by either managers or employees;[129] (iii) "do not contain adequate monitoring and enforcement procedures to ensure compliance[;]"[130] and (iv) are largely confined to corporations dealing in consumer goods.[131] Moreover, due to the lack of content requirements and standardized methodologies for measuring social and environmental performance, observers have found it increasingly difficult to compare and contrast one MNC's social or environmental benefits with those of another.[132]

Even where codes of conduct and internal monitoring mechanisms are in place, there is no guarantee they will effect any substantive changes in business operations.[133] Consider Nike, for example.[134] Allison M. Snyder points to a recent study of 800 Nike factories in fifty-one different countries that assessed the effectiveness of codes of conduct in improving working conditions.[135] The study concluded that despite Nike's efforts, internal monitoring for code compliance alone did not improve its suppliers' working conditions.[136]

In sum, while the adoption of codes of conduct should be commended insofar as they acknowledge the negative social and environmental externalities produced by MNCs, it appears these codes maintain the involuntary, malleable, and legally unenforceable qualities of the aforementioned CR reports. As several commentators conclude, "the grim fact remains that [MNCs] owe no legal obligations to anyone when they fail to abide with particular provisions of such Codes, or choose to extricate themselves totally from its provisions."[137]

---

[129] *Id.* at 132.

[130] *Id.* at 133; *see also* 2011 KPMG SURVEY, *supra* note 87, at 26 ("Unlike financial reporting, the disclosure of sustainability metrics to the market is largely unregulated."); ZERK, *supra* note 43, at 164 (noting that there is no effective way of ensuring compliance with voluntary codes of conduct).

[131] Baker, *supra* note 108, at 134.

[132] *See* Rosen-Zvi, *supra* note 71, at 538–39 (opting to rely on hard numbers provided by corporations regarding their environmental emissions, rather than "the softer public relations statements they make" in their CSRs).

[133] *See* Richard M. Locke et al., *Does Monitoring Improve Labor Standards?: Lessons from Nike*, 61 INDUS. & LAB. REL. REV. 3, 8–9, 20–21 (2007).

[134] *Id.*

[135] Snyder, *supra* note 103, at 595–96 (citing Locke et al., *supra* 133, at 20).

[136] Locke et al., *supra* note 133, at 20–21; *cf.* Larry Catá Backer, *Multinational Corporations as Objects and Sources of Transnational Regulation*, 14 ILSA J. INT'L & COMP. L. 499, 518 (2008) [hereinafter Backer, *Multinational Corporations*] (describing how Gap, Inc.'s 2005 Code of Vendor Conduct permitted Gap to "effectively assess civil penalties, impose training or other rehabilitation programs, compel changes in internal organization or terminate the contractual relationship with the enterprises subject to its standards").

[137] Emeseh et al., *supra* note 7, at 258; *see also* ZERK, *supra* note 43, at 161 (discussing the fact that codes of conduct generally do not provide for the imposition of legal sanctions).

3. Constituency Statutes

Yet another example of CSR's efforts to enhance transparency and promote consideration of stakeholder interests is the constituency statute.[138] Several commentators characterize constituency statutes as legislative responses to the frenzy of hostile corporate takeovers of the 1980s.[139] In 1983, Pennsylvania became the first of about thirty states to enact constituency statutes.[140] In general, "[t]hese statutes explicitly permit directors to consider the effects of their decisions on a variety of nonshareholder interests[,]"[141] including the long- and short-term effects of their decisions on constituency groups such as suppliers, employees, creditors, local communities, and customers.[142] While most lawmakers likely had change-of-control decisions in mind when enacting constituency statutes, CSR proponents observe that the application of constituency statutes is not necessarily limited to situations in which the corporation is for sale,[143] and argue that such statutes attract socially responsible businesses, which, in turn, foster innovation and competition.[144] Thus, on paper, constituency statutes are applicable to any business decision, and have potentially far-reaching effects on corporate governance and decision-making.

However, in all but three states, constituency statutes are written in permissive language.[145] Critics emphasize that most constituency statutes *permit* directors to consider stakeholder interests, but "do not force a corporation to conduct itself in a socially responsible manner."[146] Permissive constituency

---

[138] Gary von Stange, Note, *Corporate Social Responsibility Through Constituency Statutes: Legend or Lie?*, 11 HOFSTRA LAB. L.J. 461, 479–81 (1994).

[139] *See* Bainbridge, *supra* note 20, at 973 ("In the wake of the 1980s' merger mania, the corporate social responsibility debate resurfaced [as constituency statutes]."); Anthony Bisconti, Note, *The Double Bottom Line: Can Constituency Statutes Protect Socially Responsible Corporations Stuck in* Revlon *Land?*, 42 LOY. L.A. L. REV. 765, 780–81 (2009); Gary von Stange, *supra* note 138, at 467–69 (portraying constituency statutes as a reaction to "the feeding frenzy atmosphere of numerous hostile takeovers" in the 1980s).

[140] Gary von Stange, *supra* note 138, at 479. As of 2012, thirty-three states have enacted some form of constituency statute. *See* Clark & Babson, *supra* note 14, at 830, 830 n.64.

[141] Bainbridge, *supra* note 20, at 973; *see also* Kerr, *supra* note 20, at 634.

[142] Bainbridge, *supra* note 20, at 986.

[143] *See* Bainbridge, *supra* note 20, at 986; Clark & Babson, *supra* note 14, at 829 ("With the increase of mission-driven and triple-bottom-line corporations, these constituency statutes are now being analyzed outside the context of a hostile takeover."); Eric W. Orts, *Beyond Shareholders: Interpreting Corporate Constituency Statutes*, 61 GEO. WASH. L. REV. 14, 30–31 (1992).

[144] Bisconti, *supra* note 139, at 786.

[145] Gary von Stange, *supra* note 138, at 480–81 (noting that only Arizona, Idaho, and Connecticut have enacted constituency statutes that are mandatory).

[146] *Id.* at 483; *see also* Fei, *supra* note 24, at 41.

statutes also fail to require transparency on social and environmental performance.[147] Professor Bainbridge concludes that constituency statutes "are frustratingly silent on many key issues,"[148] lack any substantive or procedural standards, and offer "surprisingly little guidance"[149] to both board members and courts. Other critics observe the dearth of case law interpreting constituency statutes[150] and conclude that the statutes "function only to the extent that they do not conflict with shareholder primacy."[151]

From the perspective of judicial review, constituency statutes appear to hold some promise in the context of day-to-day decisions or defensive decisions, where courts will generally apply the business judgment rule and give deference to the board's decision.[152] However, the impotence of constituency statutes is most evident in the context of a change-of-control decision, which triggers the so-called *Revlon*[153] duty to maximize shareholder wealth.[154] The *Revlon* rule of shareholder primacy dealt a significant blow to proponents of constituency statutes insofar as it essentially nullified constituency statutes with respect to the most crucial of all business decisions—the sale of the corporation.[155] Moreover, subsequent case law regarding constituency statutes appears to follow the Delaware Supreme Court's approach. For example, in *Baron v. Strawbridge & Clothier*[156] a Pennsylvania district court applied the *Revlon* duty in the context of a single-party takeover attempt.[157]

---

[147] Fei, *supra* note 24, at 41.

[148] Bainbridge, *supra* note 20, at 988.

[149] *Id.* at 974.

[150] Bisconti, *supra* note 139, at 784.

[151] *Id.*

[152] For a more thorough analysis of the three different levels of scrutiny courts will apply in evaluating business decisions, see Clark & Babson, *supra* note 14, at 834–36; Felicia R. Resor, Comment, *Benefit Corporation Legislation*, 12 WYO. L. REV. 91, 96–97 (2012).

[153] Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173, 185 (Del. 1986).

[154] The *Revlon* case involved a change-of-control situation wherein competing parties engaged in several rounds of bidding. *Revlon*, 506 A.2d at 177–79; *see also* Bainbridge, *supra* note 20, at 982. The Delaware Supreme Court held that once the directors decided to sell the company, their sole responsibility was to maximize shareholder value, or, in the words of the court, to become "auctioneers charged with getting the best price for the stockholders," thus precluding any consideration of stakeholder interests. *Revlon*, 506 A.2d at 182.

[155] Bainbridge, *supra* note 20, at 982–84 (noting that *Revlon* "sharply limits" consideration by directors of stakeholder interests, and "puts considerable teeth into the" shareholder-centric theory of corporate governance); *see also* Bisconti, *supra* note 139, at 784, 786–88 (observing that "[c]onstituency statutes are essentially rendered impotent in [the *Revlon*] scenario").

[156] *Baron*, 646 F. Supp. 690 (E.D. Pa. 1986).

[157] *See id.* at 697 (attributing to corporate directors in Pennsylvania a duty to act in the best interests of shareholders); Bisconti, *supra* note 139, at 788–89 (arguing that the court

Some critics have gone so far as to suggest that constituency statutes are harmful in an "unscrupulous director" scenario.[158] In authorizing directors to consider stakeholder interests, Professor Bainbridge argues that they also serve as a shield for unscrupulous directors to consider their own interests.[159] As Gary von Stange notes, this risks vesting "more unbridled power in the hands of management."[160]

4. Conclusion

As this review has shown, CSR's attempts to increase transparency and integrate consideration of stakeholder interests into corporate decision-making have not succeeded. CR reporting, corporate codes of conduct, and constituency statutes have largely failed to affect any observable changes in business as usual.[161] The unaudited, unenforceable, and voluntary nature of CR reports and corporate codes of conduct render them ineffective approaches to enhancing corporations' social and environmental commitments. Permissive constituency statutes have likewise failed to bring about any significant change. While they grant directors broad discretion to consider stakeholder interests in day-to-day decisions and defensive decisions, their voluntary language leaves stakeholders to "rely upon the goodwill of the board."[162] Moreover, in light of the *Revlon* duty to maximize shareholder value, constituency statutes have been rendered meaningless in the context of change-of-control decisions and do not cover the recurring public benefit actions social entrepreneurs seek to engage in.[163] With the shortcomings of CSR in mind, this Article next turns to existing tools for regulating MNCs.

B. Regulation of Multinational Corporations

"It is a longstanding principle of American law 'that legislation of Congress, unless a contrary intent appears, is meant to apply only within the

---

focused on protecting or benefiting shareholders to avoid determining how much weight should be given to constituency statutes).

[158] Bainbridge, *supra* note 20, at 1025; *see also* Gary von Stange, *supra* note 138, at 488–89 (arguing that corporate managers may actually have encouraged adoption of constituency statutes to protect their own interests by enlarging their discretionary powers).

[159] Bainbridge, *supra* note 20, at 1025.

[160] Gary von Stange, *supra* note 138, at 489.

[161] Page & Katz, *New Corporate Social Responsibility*, *supra* note 49, at 1360–61 ("But despite decades of commentary and scholarship, the legal debate has failed to advance CSR in any significant way ... although CSR may have good ideas about corporate behavior, it has generally failed to produce meaningful large-scale legal reform." (footnotes omitted)).

[162] Jackson, *supra* note 9, at 347.

[163] Munch, *supra* note 78, at 178–79.

territorial jurisdiction of the United States.'"[164] As a result, unless Congress explicitly intends otherwise, courts will presume a statute is "primarily concerned with domestic conditions."[165] This traditional presumption against extraterritorial application of domestic law rests on the assumption that the subjects and objects of regulation share common jurisdictional identities.[166] However, the simultaneous spread of globalization and investment treaties has undermined this assumption with respect to MNCs.[167]

As a result, MNCs are able to avoid effective regulation in developed states by moving operations to developing states where their power and influence effectively "substitute themselves as new regulators of behavior."[168] Thus, while domestic statutes provide an avenue for domestic regulation,[169] there is no corollary on the international level. As Jennifer Zerk explains, obtaining territorial jurisdiction over MNCs' negative social and environmental externalities presents a significant obstacle for potential plaintiffs.[170] With this jurisdictional hurdle as a backdrop, this Part turns to two main aspects of the legal landscape with respect to regulation of MNCs—namely, disclosure requirements and private enforcement.

1. Disclosure Requirements

In the United States, all publicly-traded companies are subject to the Securities Exchange Commission's (SEC) disclosure requirements.[171] SEC regulation S-K provides the framework for annual and quarterly disclosure

---

[164] EEOC v. Arabian Am. Oil Co., 499 U.S. 244, 248 (1991) (quoting Foley Bros. v. Filardo, 336 U.S. 281, 285 (1949), *as cited in* Morrison v. Nat'l Austl. Bank Ltd., 130 S. Ct. 2869, 2877 (2010)).

[165] *Morrison*, 130 S. Ct. at 2877 (quoting *Arabian Am. Oil Co*., 499 U.S. at 248).

[166] *See* Larry Catá Backer, *Private Actors and Public Governance Beyond the State: The Multinational Corporation, the Financial Stability Board, and the Global Governance Order*, 18 IND. J. GLOBAL LEGAL STUD. 751, 754 (2011) [hereinafter Backer, *Private Actors*].

[167] *See* Backer, *Multinational Corporations*, *supra* note 136, at 504; Backer, *Private Actors*, *supra* note 166, at 754 (discussing the effects of globalization).

[168] Backer, *Private Actors*, *supra* note 166, at 754; *see also* Backer, *Multinational Corporations*, *supra* note 136, at 503–04 (explaining that while states' regulatory powers often "extend no further than their political borders," mutlinationals "tend to operate across political borders – to move assets, operations and activities in ways in which political borders become incidental to their activities").

[169] *See* Backer, *Multinational Corporations*, *supra* note 136, at 503 (noting that while the interaction of traditional frameworks has been effective in regulating domestic entities, "it has proven to be less useful in the management of multinational corporations and similar entities").

[170] *See generally* ZERK, *supra* note 43, at 104–42 (discussing the problem of jurisdiction as it relates to regulation of the social and environmental activities of multinational corporations).

[171] *See* Securities Exchange Act of 1934, 15 U.S.C. §§ 78m, 78q (2006).

requirements contained in the Securities Act of 1933 and the Securities Exchange Act of 1934.[172] These reporting requirements were recently revised pursuant to the Sarbanes-Oxley Act of 2002.[173] However, none of these statutes requires that a corporation report its negative social outputs, and the Sarbanes-Oxley amendments do not impose additional requirements with respect to a corporation's environmental impacts.

Environmental concerns are, however, relevant to Regulation S-K, Items 101,[174] 103,[175] 303,[176] and 503.[177] Item 101 requires disclosure of costs of complying with environmental law.[178] Item 103 requires disclosure of any "administrative or judicial proceeding ... arising under any Federal, State or local" environmental law.[179] Item 303 requires disclosure of known trends, events, commitments, and uncertainties that are reasonably likely to have a material effect on the registrant's financial condition or results of operation.[180] Lastly, Item 503 requires a discussion of the most significant factors, such as environmental factors, that make an investment in the company speculative or risky.[181] Despite the fact that Sarbanes-Oxley did not impose increased environmental reporting,[182] some commentators note that the SEC's interpretations of the existing regulations suggest the agency is applying greater scrutiny on certifying and quantifying such environmental liabilities.[183]

---

[172] *See* 17 C.F.R. § 229.10 (2011).

[173] Sarbanes-Oxley Act of 2002, Pub. L. No. 107-204, §§ 401–409, 116 Stat. 745, 785–791 (2002) (amending 15 U.S.C. § 78m).

[174] 17 C.F.R. § 229.101(c)(xii).

[175] 17 C.F.R. § 229.103.

[176] *See* 17 C.F.R. § 229.303(a) (requiring the disclosure of rare events that materially affect the company).

[177] *See* 17 C.F.R. § 229.503 (requiring disclosure of risk factors); HERBERT S. WANDER, PRACTISING LAW INSTITUTE CORPORATE LAW AND PRACTICE COURSE HANDBOOK SERIES: SECURITIES LAW DISCLOSURE AFTER SARBANES-OXLEY AND DODD-FRANK 493, 670–71, 883–84 (2011) (explaining that Item 503 requires disclosure of risk factors and how Items 101, 103, and 303 apply to environmental disclosures).

[178] 17 C.F.R. § 229.101(c)(xii) (2010).

[179] 17 C.F.R. § 229.103.

[180] 17 C.F.R. § 229.303.

[181] 17 C.F.R. § 229.503(c) (specifying that risk factor disclosure should clearly identify the risk and articulate how that risk affects the company).

[182] *See* GOV'T ACCOUNTABILITY OFFICE, ENVIRONMENTAL DISCLOSURE: SEC SHOULD EXPLORE WAYS TO IMPROVE TRACKING AND TRANSPARENCY OF INFORMATION 8 (2004), *available at* http://www.gao.gov/assets/250/243371.pdf (concluding that "[w]hile [Sarbanes-Oxley] does not contain provisions that specifically address environmental disclosure, some of them *could* lead to improved reporting of environmental liabilities") (emphasis added)).

[183] WANDER, *supra* note 177, at 889–90.

Consider, for example, the SEC's February 8, 2010 interpretive release on climate change.[184] SEC Chairman Mary Schapiro emphasized that it neither created any new legal requirements nor modified existing requirements, but that it instead was "intended to provide clarity and enhance consistency"[185] regarding climate change-related disclosures. To that end, the release identified four main areas in which climate change may prompt disclosure requirements, to wit: (1) impact of legislation and regulation;[186] (2) impact of international accords;[187] (3) indirect consequences of regulation or business trends;[188] and (4) physical impact of climate change.[189]

Practically speaking, disclosure under Item 303—"Management's Discussion and Analysis of Financial Condition and Results of Operations, or MD&A"[190]—is potentially the most fruitful avenue by which a corporation might disclose its environmental impacts in relation to climate change. However, the SEC's climate change release does not change the framework for preparing MD&A disclosure, and simply reiterates the traditional MD&A analysis that turns entirely on management's conclusions regarding the "material effect" of environmental impacts on the company's financial condition.[191]

The "materiality" standard has been criticized by some scholars for its failure to fully account for a corporation's total environmental impacts.[192] Jennifer Zerk explains: "apart from information that is necessary to assess the *financial* position and prospects of the corporate group, these [environmental and social] disclosures are still largely voluntary."[193] In addition to

[184] Commission Guidance Regarding Disclosure Related to Climate Change, 75 Fed. Reg. 6290 (Feb. 8, 2010) [hereinafter Climate Change Release].

[185] Mary Schapiro, Chairman, U.S. Sec. & Exch. Comm'n, Statement Before the Open Commission Meeting on Disclosure Related to Business or Legislative Events on the Issue of Climate Change (Jan. 27, 2010), *available at* http://sec.gov/news/speech/2010/spch012710mls-climate.htm; *see also* Subcommittee on Annual Review, Committee on Federal Regulation of Securities, ABA Section of Business Law, *Annual Review of Federal Securities Regulation: Section I: Regulatory Developments 2010*, 66 BUS. LAW 665, 749–54 (2011); Wander, *supra* note 177, at 892–93.

[186] Disclosure Related to Climate Change, Exchange Act Release No. 33-9106, 75 Fed. Reg. 6925, 6295–96 (Feb. 8, 2010).

[187] *Id.*

[188] *Id.*

[189] *Id.* at 6295–97.

[190] *Id.* at 6294–95.

[191] *See id.* at 6295; *see also* Management's Discussion and Analysis of Financial Condition and Results of Operations: Certain Investment Company Disclosures, Exchange Act Release No. 33-6835, 54 Fed. Reg. 22,427, 22,429 (May 24, 1989).

[192] Mitchell F. Crusto, *Endangered Green Reports: "Cumulative Materiality" in Corporate Environmental Disclosure After Sarbanes-Oxley*, 42 HARV. J. ON LEGIS. 483, 497, 500 (2005).

[193] ZERK, *supra* note 43, at 175.

the voluntary nature of environmental disclosure, other commentators argue that federal securities law has been unsuccessful in promoting corporate environmental protection in general.[194] Mitchell Crusto has described the SEC's materiality standard as "elusive"[195] and suggests adopting the American Society of Testing and Materials (ASTM) Cumulative Materiality Standards of Corporate Environmental Disclosure to broaden the scope of materiality to include total environmental impacts, not simply those that are material to a corporation's financial condition.[196] Alternatively, drawing upon recent shareholder proposals, Perry Wallace suggests the introduction of a fiduciary duty to investigate and monitor greenhouse gas (GHG) emissions.[197] At present, however, it appears that the SEC will stay the course and continue to require the traditional materiality standard, ensuring that corporations traded publicly in the United States remain free to omit, or selectively disclose, "non-material" environmental impacts.

2. Private Enforcement

Many states do not grant to non-residents any rights to enforce domestic environmental or health and safety regulations.[198] This does not mean, however, that foreign plaintiffs are left without a forum to pursue an enforcement action against MNCs. This Section identifies three vehicles through which individuals may assert claims against MNCs: trade practice actions, OECD actions, and the Alien Tort Statute.[199]

a. Trade Practice Actions

Private individuals opposing the actions of MNCs may file a complaint under domestic trade practice legislation.[200] However, these actions only address a MNC's "statements and representations"[201] regarding its trade practices. Accordingly, trade practice actions provide a remedy for indirectly holding MNCs accountable for alleged trade practice violations.[202]

---

194 Crusto, *supra* note 192, at 500.
195 *Id.* at 497.
196 *Id.* at 500–09.
197 Wallace, *supra* note 81, at 322 (citing Interfaith Ctr. on Corp. Responsibility, *Proposed Shareholder Resolution on Embedded Climate Risk*, *available at* http://www.iccr.org/shareholder/proxy_book03/environment/climaterisk_oxy.htm (accessed by entering URL in the Internet Archive index)).
198 ZERK, *supra* note 43, at 182–83.
199 *See id.* at 183–85.
200 *Id.* at 185.
201 *Id.*
202 *Id.*

Despite the indirect nature of these actions, some proponents point to the *Nike, Inc. v. Kasky*[203] litigation in the United States as evidence of the "potential to cause a great deal of embarrassment for companies."[204] In that case, sweatshop activist Marc Kasky brought suit against Nike in California, alleging that Nike had misled the public regarding the company's foreign suppliers' workplace standards, in violation of the California Business and Professions Code.[205] Nike prevailed in the California Court of Appeals but lost in the California Supreme Court, and the U.S. Supreme Court ultimately dismissed the appeal.[206] Three months after the Supreme Court's decision, the parties reached a settlement[207] in which Nike agreed to pay $1.5 million to the Fair Labor Association without admitting any wrongdoing.[208]

The apparent success of the *Kasky v. Nike* litigation belies the fact that Nike continues to purchase materials from foreign clothing suppliers with substandard workplace conditions.[209] Furthermore, California stands alone as the only state to offer the particular "private attorney general action"[210] used by Kasky.[211] As this suggests, the effectiveness of this unique right of action depends largely on "shaming" MNCs through media spotlight and public outrage. Moreover, as the settlement terms and subsequent practice suggest, even where trade practice actions are successful, they fail to persuade MNCs to modify their business practices.

b. OECD Actions

The Organization for Economic Co-operation and Development (OECD) is an international organization comprised of thirty-four member states focused

---

[203] 539 U.S. 654 (2003) (per curiam); *see* SARAH JOSEPH, CORPORATIONS AND TRANSNATIONAL HUMAN RIGHTS LITIGATION 101–11 (Colin Harvey ed., 2004) (providing an overview of the case and its impact on both corporations and consumer rights litigation).

[204] ZERK, *supra* note 43, at 185.

[205] *See Nike*, 539 U.S. at 656 (Stevens, J., concurring); ZERK, *supra* note 43, at 185. *See generally* CAL. CORP. CODE §§ 17200–17209 (West 2012) (providing the governing provisions of the California Business and Professions Code).

[206] JOSEPH, *supra* note 203, at 102. The case was ultimately dismissed on jurisdictional grounds. *See Nike*, 539 U.S. at 657–58 (Stephens, J., concurring) (articulating the reasons that supported the decision to dismiss the grant of certiorari, including failure by the California Supreme Court to properly enter final judgment and a lack of standing by either party).

[207] JOSEPH, *supra* note 203, at 102, 104–05.

[208] *Id.* at 104–05.

[209] *See* Locke et al., *supra* note 133, at 20–21 (discussing how Nike's new monitoring systems failed to produce an improvement in working conditions within Nike's suppliers); Snyder, *supra* note 103, at 595–96 (discussing the same).

[210] ZERK, *supra* note 43, at 185; *see also* CAL. CORP. CODE §§ 17203, 17206.

[211] ZERK, *supra* note 43, at 185. The Australian Trade Practices Act of 1974, however, permits "any person" to apply "to have legislative prohibitions on misleading or deceptive conduct enforced" regardless of whether the person is a resident of Australia and without a showing of personal harm by the defendant's conduct. *Id.* (internal quotation marks omitted).

on "promot[ing] policies that will improve the economic and social well-being of people around the world."[212] In 1976, pursuant to this mission, the OECD proposed Guidelines for Multinational Enterprises (OECD Guidelines).[213] The OECD Guidelines were adopted by the OECD Council as part of the broader Declaration on International Investment and Multinational Enterprises.[214] The OECD Guidelines are occasionally updated, most recently on May 25, 2011 in conjunction with the OECD's fiftieth anniversary.[215] A total of forty-four governments, representing 85% of the world's foreign direct investment, have agreed to adhere by the OECD Guidelines and encourage their enterprises to observe them wherever they operate.[216]

Private individuals may raise issues concerning compliance with the OECD Guidelines with the correct National Contact Point (NCP).[217] Notably, the 2000 Revision to the OECD Guidelines extends its scope to non-adhering countries, theoretically easing the burden of territorial jurisdiction over MNCs.[218] Once a compliance issue has been raised, the NCP is obligated to "contribute to the resolution of issues that arise relating to implementation of the *Guidelines* in specific instances."[219] In resolving these issues, the NCP is authorized to make an initial assessment of whether the issues merit further examination and to offer aid to parties involved in resolving the issues.[220] If the parties fail to reach an agreement, the NCP is required to issue a statement containing appropriate "recommendations on the implementation of the *Guidelines*."[221]

OECD actions may overcome the hurdle of territorial jurisdiction and bring the parties to the table. However, these actions lack any enforcement mechanism to ensure compliance.[222] Furthermore, the NCP's mediation procedures

---

[212] *About the OECD: The Organisation for Economic Co-operation and Development (OECD)*, OECD, http://www.oecd.org/pages/0,3417,en_36734052_36734103_1_1_1_1_1,00.html (last visited Mar. 23, 2013).

[213] *See OECD Guidelines for Multinational Enterprises, 2011 Update*, OECD, http://www.oecd.org/document/28/0,3746,en_2649_34889_2397532_1_1_1_1,00.html (last visited Mar. 23, 2013).

[214] OECD, *OECD Guidelines for Multinational Enterprises*, at 13 (2011), http://www.oecd.org/daf/internationalinvestment/guidelinesformultinationalenterprises/48004323.pdf.

[215] *Id.* at 3.

[216] *About the OECD*, *supra* note 212.

[217] OECD, *The OECD Guidelines for Multinational Enterprises: Revision 2000*, at 31–33, 35–37 (June 2000), http://www.jussemper.org/Resources/Corporate%20Activity/Resources/OECDGuidelines15419.pdf; ZERK, *supra* note 43, at 184.

[218] *See id.* at 31.

[219] *OECD Guidelines for Multinational Enterprises*, *supra* note 213, at 72.

[220] *Id.*

[221] *Id.* at 73.

[222] ZERK, *supra* note 43, at 184 (also noting that the Guidelines are non-binding).

are confidential, and recommendations are only revealed to the public if the NCP determines confidentiality would be contrary to effective implementation of the OECD Guidelines.[223]

c. Alien Tort Statute

In recent decades, the Alien Tort Statute (ATS)[224] has been at the forefront of litigation against MNCs in the United States. The ATS provides that "[t]he district courts shall have original jurisdiction of any civil action by an alien for a tort only, committed in violation of the law of nations or a treaty of the United States."[225] The decades following the landmark case of *Filartiga v. Pena-Irala*[226] witnessed some success in using the ATS to hold MNCs responsible for their participation in human rights abuses.[227] Similar actions against MNCs for their participation in environmental abuses, however, were not as successful due to the reluctance on the part of federal courts to find that principles of international environmental law have crystallized into customary international law as contemplated by *Filartiga*.[228]

Moreover, the window of corporate liability under the ATS may be quickly closing. On February 28, 2012, the U.S. Supreme Court heard oral arguments in *Kiobel v. Royal Dutch Shell*.[229] The main issue in *Kiobel* is whether corporations may be held liable for violations of the law of nations, such as torture, extrajudicial killings, or genocide.[230] Surprisingly, less than one week later, on March 5, 2012, the Supreme Court ordered the case "restored to the calendar for reargument" and directed the parties to file briefs on

---

[223] *Id.* at 184–85.

[224] Alien Tort Statute, 28 U.S.C. § 1350 (2006).

[225] *Id.*

[226] 630 F.2d 876 (2d Cir. 1980).

[227] *See, e.g.*, Presbyterian Church of Sudan v. Talisman Energy, 244 F. Supp. 2d 289, 318–19 (S.D.N.Y. 2003) ("Historically, states, and to a lesser extent individuals, have been held liable under international law. However, ... substantial international and United States precedent indicates that corporations may also be held liable under international law, at least for gross human rights violations.").

[228] *See, e.g.*, Beanal v. Freeport McMoran, Inc., 197 F.3d 161, 167 (5th Cir. 1999) (holding that plaintiff and amici submissions "refer to a general sense of environmental responsibility and state abstract rights and liberties devoid of articulable or discernable [sic] standards and regulations to identify practices that constitute international environmental abuses or torts"); Flores v. S. Peru Copper Co., 414 F.3d 233, 250–52 (2d Cir. 2003) (articulating and applying the sources of international law).

[229] 621 F.3d 111 (2d Cir. 2010), *cert. granted*, 132 S. Ct. 472 (Oct. 17, 2011); *Kiobel v. Royal Dutch Petroleum*, SCOTUSBLOG, http://www.scotusblog.com/case-files/cases/kiobel-v-royal-dutch-petroleum/?wpmp_switcher=desktop (last visited Mar. 23, 2013).

[230] *Kiobel*, 621 F.3d at 115–17.

the issue of "[w]hether and under what circumstances the Alien Tort Statute, 28 U.S.C. §1350, allows courts to recognize a cause of action for violations of the law of nations occurring within the territory of a sovereign other than the United States."[231] The expansion of the issue from general corporate liability under the ATS to the existence of a cause of action under the ATS does not bode well for the statute's proponents, as it may signal that the Court is inclined to interpret the ATS as a jurisdictional statute not giving rise to any special cause of action. Such a result would effectively remove one of the sharpest arrows from the quivers of potential foreign plaintiffs seeking to hold MNCs accountable in U.S. courts.

C. Conclusion

This Part has explained the shortcomings and flaws of CSR and the current regulatory regime with respect to MNCs. The various iterations of CSR, including CR reporting, codes of conduct, and constituency statutes, are voluntary, passive, and unenforceable mechanisms to regulate corporate behavior. Any attempt to expand private rights of action against MNCs has been consistently met with swift political opposition. Extraterritorial regulation of MNCs remains elusive at the international level, and prospects for changing this status quo are slim.

The reality is that the world's largest corporations operate in a supranational arena where traditional jurisdictional boundaries are increasingly irrelevant. Moreover, as the history of CSR and attempted global regulatory schemes makes clear, there is no "silver bullet" solution to this problem. Larry Catá Backer opines that the failure of CSR "might indicate that political institutions might not be the appropriate vehicle for the elaboration of regulatory systems based on such substantive notions .... Rather it might suggest the possibility of substantive regulation devolving to non–political actors."[232] Backer makes a valuable point, which invites the question of how to incentivize "non–political actors" (for example, corporations) to enforce substantive regulations.

One can come much closer to a viable solution to this problem once one accepts the limitations of regulation and entertains the idea of fundamentally altering the *very nature and purpose of the corporate entity itself*. After decades of unsuccessful attempts to regulate MNCs, the pendulum of corporate law has begun to swing away from government regulation and towards

---

[231] Order in Pending Case, Kiobel v. Royal Dutch Petroleum, 132 S. Ct. 472 (2012) (Order No. 10-1491) (Mar. 5, 2012), *available at* http://www.supremecourt.gov/orders/courtorders/030512zr.pdf.

[232] Backer, *Moral Obligation*, *supra* note 43, at 620.

the creation of innovative corporate forms that weave social and environmental responsibility into the fabric of these entities. By constantly pursuing blended values, social enterprise forces all interested parties, including investors, shareholders, directors, courts, counsel, and stakeholders, to confront and resolve competing interests with the overarching goal of achieving measurable social and environmental benefits. The growing demand for innovation in this arena has led to the rapid enactment of social enterprise entities in both Europe and the United States. This Article now departs from the world of CSR and corporate regulation and turns to social enterprise in Europe, focusing on how the social enterprise movement manifests itself in European corporate law.

II. Social Enterprise in Europe: Social Cooperatives and the Community Interest Company

A. Introduction to European Social Enterprise

Europe is the birthplace of modern social enterprise, having arisen out of traditional concepts of social cooperation.[233] In general, the modern European movement is defined by different types of social cooperatives aimed at providing work integration services and personal services for the disadvantaged.[234] Jacques Defourny identifies the Italian Parliament's enactment of the "social solidarity cooperative" in 1991 as the beginning of the modern social enterprise movement in Europe.[235] In Italy, these organizations quickly gained acceptance. As of 2005, Italy was home to more than 7300 social cooperatives employing some 244,000 people.[236] Other European countries quickly followed Italy's lead and enacted their own social cooperative organizations.[237]

This Part traces the development of social enterprise in Europe during the preceding two decades. In doing so, this Part contrasts the social cooperatives of continental Europe with the United Kingdom's Community Interest Companies (CICs) and identifies a recent resurgence in social enterprise in the wake of a global recession. This Part concludes by outlining the European Parliament's efforts to use social enterprise as a tool to boost the European economy.

---

[233] *See* Defourny, *supra* note 27.

[234] *See generally* Defourny & Nyssens, *supra* note 31.

[235] *Id.* at 205–06. The Italian law identifies two types of social cooperatives, to wit: (1) *cooperative sociali di tipo a* ("Type-A Social Cooperatives"), which provide social, health and educational services; and (2) *cooperative sociali di tipo b* ("Type-B Social Cooperatives"), which provide work integration for disadvantaged people. *Id.* at 205.

[236] *Id.*

[237] *Id.* at 206.

B. Social Cooperatives

Social cooperatives are the most widespread social enterprise entities in Europe. Since 1991, nearly every European jurisdiction has authorized its own social cooperative entity.[238] However, the concept of social enterprise in Europe remains narrowly interpreted as a synonym for charitable work.[239] As a result, the majority of the social enterprise sector in Europe focuses on social, not environmental, problems. Furthermore, like charities, social cooperatives are generally prohibited from distributing profits to shareholders.[240] The result of these policies is generally a work integration social enterprise (WISE), the most popular type of social cooperative in Europe, whose singular goal "is to help low-qualified unemployed people, who are at risk of permanent exclusion from the labour market."[241]

For example, WISEs have been available to social entrepreneurs in Portugal and Spain for over a decade. In 1997, Portugal authorized the *cooperativa de solidariedade social* (social solidarity cooperative),[242] and in 1999, Spain created the *cooperativa de iniciativa social* (social initiative cooperative).[243]

Some social cooperatives were introduced to tackle very specific issues. For example, Greece created the *Koinonikos Syneterismos Periorismenis Eufthinis*, *KoiSPE* (limited liability social co-operative), an entity designed to promote partnerships between psychiatric hospital workers and individuals with psychosocial disabilities.[244] In 2002, France created the *société coopérative d'intérêt collectif*, (SCIC) (collective interest co-operative society), a multi-stakeholder cooperative dedicated to local development projects.[245] In 2003, Finland introduced the Finnish Act of Social Enterprise, which created a WISE specifically aimed at creating employment for people with disabilities.[246]

Belgium, in contrast, has taken a different approach. In 1996, Belgium created the *société à finalité sociale*, (SFS) (social purpose company) designation[247]

---

[238] *Id.* at 206–07; *see also* EVA HECKL ET AL., STUDY ON PRACTICES AND POLICIES IN THE SOCIAL ENTERPRISE SECTOR IN EUROPE 5 (2007) (noting that these new entities are usually implemented in concert with new regulatory provisions and financial support instruments).

[239] *See generally* Defourny & Nyssens, *supra* note 31, at 206–09.

[240] *See infra* Part IV; Fei, *supra* note 24, at 37 (observing that "in continental Europe the phrase [social enterprise] often has a narrower meaning, sometimes conditioned on the presence of specific attributes in the enterprise with less emphasis on its business aspects").

[241] Defourny & Nyssens, *supra* note 31, at 207.

[242] *Id.* at 206.

[243] *Id.*

[244] *Id.*

[245] *Id.*

[246] *Id.* at 208.

[247] *Id.* at 206.

and introduced project grants for environmental cooperatives engaged in the recycling and reuse of materials.[248] As the term "designation" suggests, Belgium's legislation did not create a new corporate entity, but rather created a certification available to all types of business organizations. In order to obtain this certification, the organization must define a profit allocation policy and permit employee participation in the organization's governance structure through ownership of capital shares.[249]

More recently, social cooperatives have spread to central and eastern European countries. Defourny argues that the growth of social enterprise in eastern European countries lagged behind their western counterparts due in large part to cultural and legal obstacles that remained after the fall of the Soviet Union in 1989.[250] He highlights several obstacles to social enterprise in eastern Europe, including cultural opposition and skepticism to cooperative forms, excessive dependence on donor contributions, the absence of legal frameworks to regulate cooperatives, a general lack of confidence in solidarity movements, and the predominance of parochial political cultures that eschewed alternative corporate governance structures.[251] Despite these barriers, Defourny estimates that half of all central and eastern European states have enacted at least one new cooperative organization in recent years.[252]

A review of the emergence of social cooperatives throughout Europe makes clear that these new entities enjoy near-universal support. Social cooperatives are designed to encourage "entrepreneurial and commercial dynamics that are an integral part of a social project ... provid[ing] a way of formalising the multi-stakeholder nature of numerous initiatives."[253] However, this narrow view of social enterprise has not succeeded in addressing local or regional environmental concerns, nor has it encouraged social cooperatives to expand into the growing sectors of low-carbon energy production or so-called "clean technology." Moreover, countries that

---

[248] *See* HECKL ET AL., *supra* note 238, at 27.

[249] Defourny & Nyssens, *supra* note 31, at 206–07. Defourny and Nyssens criticize this approach as unsuccessful, explaining that it "involve[s] a considerable number of requirements ... without bringing a real value added for the concerned organizations." *Id.* at 207. In a similar vein, other European countries offer government-sponsored awards to corporations in an effort to induce them to make significant contributions to sustainability or human rights issues. ZERK, *supra* note 43, at 194. Examples of such awards can be found in the Netherlands, Denmark, Spain, and the UK. *Id.* While these government-sponsored awards are available to any organization, social cooperatives appear to be uniquely positioned to take advantage of these awards given their social purpose, community involvement, and innovative business models.

[250] Defourny, *supra* note 27.

[251] *Id.*

[252] *Id.* (identifying examples in the Czech Republic, Hungary, and Slovakia).

[253] *Id.*

have explored alternative corporate designations, like Belgium, have not proved successful. Belgium's SFS designation imposes restrictions on profit distribution but does not offer any advantages for raising capital other than the branding value associated with the designation.[254] As Matthew Doeringer notes, in the eight years following the creation of the SFS designation, "only 400 SFSs registered with the Belgian government."[255]

Thus, while social cooperatives dominate continental Europe, the adherence to the narrow view of social enterprise has hamstrung a movement seeking to offer alternative business models in many areas beyond work integration. The United Kingdom has taken a markedly different approach. A decade ago, the U.K. adopted a view of for-profit, mission-driven social enterprise, and it now enjoys the most robust social enterprise sector in Europe.[256]

C. Community Interest Companies (CICs)

In 2010, Stephen Lloyd, one of the architects of the CIC, explained that the idea for this entity arose out of a growing sense of frustration with corporate law in the U.K.[257] Lloyd noted that traditional English corporate law made it "quite complicated to embed social purposes in a legal form because there was not an off-the-shelf, simple-to-use legal entity ready for social enterprise unless you used the old-fashioned industrial and provident societies—the law for which has not been updated since 1965."[258] Lloyd proposed the creation of just such an "off-the-shelf" entity for social entrepreneurs, the CIC.[259]

In 2001, the British government "established the Social Enterprise Unit ... to identify barriers to the growth of the social-enterprise sector ... and to develop strategies to overcome these obstacles."[260] In its first report, issued one year later, the Unit defined social enterprise as "a business with primarily social objectives whose surpluses are principally reinvested for that purpose in the business or in the community, rather than being driven by the need to maximise profit for shareholders and owners."[261] In contrast

---

[254] Matthew F. Doeringer, Note, *Fostering Social Enterprise: A Historical and International Analysis*, 20 DUKE J. COMP. & INT'L L. 291, 309 (2010).

[255] *Id.*

[256] HECKL ET AL., *supra* note 238, at 12; *see also* Doeringer, *supra* note 254, at 309–10.

[257] Stephen Lloyd, *Transcript: Creating the CIC*, 35 VT. L. REV. 31, 31–32 (2010).

[258] *Id.* at 33.

[259] *See id.* (describing his vision of the CIC as "piggybacking" on legislation already in place for existing companies).

[260] Doeringer, *supra* note 254, at 310.

[261] OFFICE OF THE THIRD SECTOR, CABINET OFFICE, SOCIAL ENTERPRISE ACTION PLAN: SCALING NEW HEIGHTS 10 (2006) [hereinafter SOCIAL ENTERPRISE ACTION PLAN], http://web

to continental Europe's definition, the Unit's definition does not relegate social enterprise to work integration and, importantly, permits profit distribution.

With popular and government support behind the Social Enterprise Unit's conclusions, policies were quickly put into place to foster the growth of social enterprise in the U.K. These included the creation of a website, the opening of regional social enterprise development centers, the selection of thirty-five social enterprise ambassadors tasked with spreading information in local communities, the establishment of a £10 million fund for investment in social enterprise, and the creation of programs to develop better metrics for valuing the social benefits produced by social enterprise.[262]

Most importantly, Parliament followed through with the Unit's suggestion to create a corporate entity specifically designed for social enterprise.[263] Three years after the creation of the Unit, Parliament authorized the CIC as part of the 2004 Companies Act.[264] In general, the CIC is a limited company, with governance primarily enshrined in the board of directors,[265] but subject to restrictions designed to ensure that it will serve community interests.[266]

These restrictions operate on both the entity and regulatory levels. At the entity level, a social entrepreneur incorporating a CIC has two choices, to limit the CIC by guarantee or by shares.[267] If limited by guarantee, the CIC adopts a charitable model by guaranteeing that all profits will be reinvested in the company.[268] If limited by shares, the CIC embraces a blended value model and operates like a traditional limited company.[269] CICs limited by shares are permitted to raise equity and distribute dividends to shareholders, capped at 35% of the aggregate total company profits.[270]

---

archive.nationalarchives.gov.uk/20070108124358/http:/cabinetoffice.gov.uk/third_sector/documents/social_enterprise/se_action_plan_2006.pdf; *see also* Doeringer, *supra* note 254, at 310.

[262] *See* SOCIAL ENTERPRISE ACTION PLAN, *supra* note 261, at 5; Doeringer, *supra* note 254, at 310–11.

[263] Doeringer, *supra* note 254, at 312.

[264] Companies (Audit, Investigations and Community Enterprise) Act, 2004, c. 27, § 26 (U.K.) [hereinafter Companies Act].

[265] Dana Brakman Reiser, *Governing and Financing Blended Enterprise*, 85 CHI.-KENT L. REV. 619, 632 (2010).

[266] Reiser, *supra* note 265, at 634–35.

[267] Lloyd, *supra* note 257, at 40–41; Reiser, *supra* note 265, at 631.

[268] *See* Reiser, *supra* note 265, at 631 (discussing how companies limited by guarantee are similar to U.S. nonprofits).

[269] *See* Lloyd, *supra* note 257, at 41 (discussing how CICs limited by shares can distribute equity to investors).

[270] Reiser, *supra* note 265, at 635 (adding that the dividend restrictions have recently been revised by the CIC Regulator).

At the regulatory level, all CICs are overseen by the CIC Regulator.[271] As a procedural matter, CICs must first register with the Companies House, a government registry in the U.K. similar to the Secretaries of State in the United States.[272] Founders of CICs must also sign a Community Interest Statement detailing how they will deliver a "community purpose."[273] CIC directors are thereafter responsible for submitting annual reports to the CIC Regulator, which must "confirm that access to the benefits it provides will not be confined to an unduly restricted group."[274] The overarching goal of CIC regulation is to ensure compliance with the so-called "Community Interest Test," to wit: whether "a reasonable person might consider [the] activity [as] being carried on [by the CIC] for the benefit of the community."[275] The CIC Regulator, who is appointed by the Secretary of State for Business and Innovation,[276] is responsible for maintaining public confidence in the CIC brand[277] and enforcing the community interest test.[278] To that end, the CIC Regulator has "surprisingly wide"[279] powers to intervene in CIC operations, including ordering independent audits at the Regulator's expense,[280] commencing civil proceedings to intervene in the CIC's affairs,[281] removing directors,[282] and appointing a "manager" to run the CIC after the directors have been removed.[283]

In addition to government regulation, CICs are also subject to an "asset lock."[284] The asset lock caps shareholder dividends,[285] and imposes a duty

[271] *Id.* at 630–31.
[272] Lloyd, *supra* note 257, at 35.
[273] *Id.*
[274] Reiser, *supra* note 265, at 633 (quoting THE REGULATOR OF CMTY. INTEREST COMPANIES, DEP'T FOR BUS. INNOVATION & SKILLS, FREQUENTLY ASKED QUESTIONS 8 (Oct. 2009), http://webarchive.nationalarchives.gov.uk/+/http://www.bis.gov.uk/assets/cicregulator/docs/leaflets/09-1648-community-interest-companies-frequently-asked-questions-leaflet.pdf).
[275] The Community Interest Company Regulations, 2005, S.I. 2005/1788, art. 2, ¶ 4 (U.K.); *see also* Lloyd, *supra* note 257, at 34–35.
[276] Lloyd, *supra* note 257, at 38 (citing Companies (Audit, Investigations and Community Enterprise) Act, 2004, c. 27, § 29-40A (U.K.)).
[277] Companies Act, § 41.
[278] *See id.* § 36A; *see also* Lloyd, *supra* note 257, at 38–39 (discussing the CIC Regulator's powers, including the ability to take over CIC property if the Regulator becomes convinced the CIC has lost its community purpose).
[279] Lloyd, *supra* note 257, at 38; *cf.* OFFICE OF THE REGULATOR OF CMTY. INTEREST COMPANIES, DEP'T TRADE & INDUS., COMMUNITY INTEREST COMPANIES 10–11 (Jan. 2005), http://www.dti.gov.uk/cics/pdfs/cicfactsheet2.pdf (stating that regulation of CICs will be by a "light touch"); Reiser, *supra* note 265, at 631.
[280] Companies Act, §§ 26, 43.
[281] *See id.* § 44.
[282] *Id.* § 46.
[283] *Id.* § 47; *see also* Lloyd, *supra* note 257, at 39 (referring to this manager as a receiver).
[284] Companies Act, § 30; OFFICE OF THE REGULATOR OF CMTY. INTEREST COMPANIES, DEP'T FOR BUS. INNOVATION & SKILLS, INFORMATION AND GUIDANCE NOTES § 6.1 (2012)

on CIC directors to ensure that they obtain fair market value on the sale of any CIC asset.[286] In practice, this prevents a CIC's assets from being raided by selling them for below-market prices to a for-profit company owned by the directors, simultaneously turning a considerable profit for the directors and undermining the community interest goal of the CIC.[287] Furthermore, in the event of dissolution, the asset lock prevents the distribution of assets to directors, members, or equity holders.[288] Instead, all assets must go to another entity whose assets are similarly "locked" into community benefits.[289]

Unlike many social cooperatives, which include stakeholder governance requirements, CICs are encouraged, but not required, to include stakeholder groups in their decision-making processes.[290] The CIC Regulator strongly encourages several techniques designed to incorporate stakeholders in governance, such as circulating newsletters, holding stakeholder meetings, establishing interactive websites, or giving certain stakeholder groups standing in the CIC's organic documents by requiring that they be consulted before CIC directors make certain types of decisions.[291] While none of these stakeholder integration techniques are mandated, all CICs must make some efforts and detail those efforts in the annual report submitted to the CIC Regulator.[292]

Thus, in contrast to continental Europe's social cooperatives, the U.K.'s CIC embraces a blended-value interpretation of social enterprise. Since 2004, CICs have grown faster than any social enterprise entity in Europe. In less than two years after its enactment, there were over 1000 CICs in the U.K.[293] As of April 2012, there were nearly 6400 registered CICs,[294] representing

---

[hereinafter INFORMATION & GUIDANCE NOTES], *available at* http://www.bis.gov.uk/assets/cicregulator/docs/guidance/12-1149-community-interest-companies-guidance-chapter-6-the-asset-lock.pdf; *see also* Lloyd, *supra* note 257, at 38; Reiser, *supra* note 265, at 634–35.

[285] Lloyd, *supra* note 257, at 38.

[286] *Id.*

[287] *Id.*

[288] Reiser, *supra* note 265, at 635; *see also* INFORMATION & GUIDANCE NOTES, *supra* note 284, § 10.5.2, *available at* http://www.bis.gov.uk/assets/cicregulator/docs/guidance/11-959-community-interest-companies-guidance-chapter-10-transfer-of-assets-and-ceasing-to-be-a-cic.pdf.

[289] Reiser, *supra* note 265, at 635.

[290] INFORMATION & GUIDANCE NOTES, *supra* note 284, § 9.1.3, *available at* http://www.bis.gov.uk/assets/cicregulator/docs/guidance/11-958-community-interest-companies-guidance-chapter-9-corporate-governance.pdf; *see also* Reiser, *supra* note 265, at 633.

[291] INFORMATION & GUIDANCE NOTES, *supra* note 284, § 9.2, *available at* http://www.bis.gov.uk/assets/cicregulator/docs/guidance/11-958-community-interest-companies-guidance-chapter-9-corporate-governance.pdf; *see also* Reiser, *supra* note 265, at 634.

[292] Reiser, *supra* note 265, at 634.

[293] Defourny & Nyssens, *supra* note 31, at 205.

[294] *Community Interest Companies Register*, DEP'T FOR BUS. INNOVATION & SKILLS, http://webarchive.nationalarchives.gov.uk/+/http://www.bis.gov.uk/cicregulator/cic-register (last updated Apr. 4, 2012) [hereinafter *CIC Register*].

more than double the rate of anticipated growth.[295] This accelerated growth is due in large part to the flexibility of CICs to operate in virtually any economic sector. Indeed, CICs have succeeded in agriculture, manufacturing, nurseries, and environmental projects like waste recycling, low-carbon micro-generation energy systems, and wind farms.[296]

Despite the growth and popularity of the CIC, some commentators suggest the entity is too restrictive. Doeringer notes that the ECT Group, one of the early success stories of the CIC form and the U.K.'s largest CIC in 2006 and 2007, suffered adversely from the dividend restrictions and found it difficult to raise capital in equity markets.[297] By 2008, the ECT Group was forced to sell nearly all of its assets to cover its debt.[298] Dana Brakman Reiser has also criticized the dividend restrictions, contending that CICs offer investors the opportunity to hold shares in a CIC but entitle the owners of such shares to receive "midstream profits only—and these profits remain capped."[299]

CICs do not confer any tax benefits beyond those available to traditional companies, and they are subject to entity-level taxes despite their dedication to charitable goals.[300] Stephen Lloyd has argued that tax breaks are necessary to encourage investment in CICs, in particular so-called "patient capital"—socially responsible investors looking for a "long term, bond rate of return."[301] In the absence of tax breaks, Lloyd, Michael Webber, and Arthur Wood have advocated for a new entity, the social enterprise limited liability partnership (SELLP), which would provide entrepreneurs with a pass-through tax entity to pursue the blended value missions of their enterprises.[302]

While the CIC may require some fine-tuning, its current structure has achieved considerable success. Although some have questioned the sustainability of this growth,[303] CICs continue to flourish in the traditionally charitable

---

[295] Lloyd, *supra* note 257, at 39.

[296] *Id.* at 40.

[297] Doeringer, *supra* note 254, at 315.

[298] *Id.*

[299] Reiser, *supra* note 265, at 648.

[300] *See* Lloyd, *supra* note 257, at 41–42; Reiser, *supra* note 265, at 632.

[301] Lloyd, *supra* note 257, at 42.

[302] Stephen Lloyd, *The Social Enterprise LLP—What Is It?; And What Is It For?*, BARRISTER MAG., http://www.barristermagazine.com/archive-articles/issue-48/the-social-enterprise-llp-%E2%80%93-what-is-it;-and-what-is-it-for.html (last visited Mar. 23, 2013) (explaining that "it is necessary to create a simple to use, cheap legal structure so as to combine charitable, government and private sector funding under one umbrella so as to achieve social goals as well as paying financial returns in a tax efficient structure. The SELLP is expressly designed to address this challenge.").

[303] Dennis R. Young, Can Social Enterprises Remain Sustainable and Mission-Focused? Applying Resiliency Theory, presented at the International Society for Third-Sector Research 10th International Conference (2012) (abstract available at http://www.istr.org/?SienaAbstracts).

areas, as well as in the private sector. This flexibility may alleviate concerns about the sustainability of the CIC and mitigate funding issues in certain sectors. While tax breaks or a refined dividend capping system might foster further investment in CICs, it appears that such reforms are not immediately necessary to fulfill the community interest goals already being achieved by thousands of CICs across the U.K.

D. The Future of Social Enterprise in Europe

Recently, the European Union (EU) acknowledged that its efforts to produce an efficient "internal market" have fallen short of expectations.[304] These shortcomings are painfully obvious in the current European economy, particularly in the so-called "PIGS" (Portugal, Italy, Greece, and Spain).[305] To remedy these shortcomings, the EU adopted a "Europe 2020" strategy,[306] which sets goals for "smart, sustainable and inclusive growth."[307] In order to implement the Europe 2020 strategy, the European Commission released several communications to the European Parliament advocating "measures likely to foster growth and employment."[308] These measures were set forth in the Commission's April 13, 2011 communication entitled *Single Market Act: Twelve Levers to Boost Growth and Strengthen Confidence*.[309] Given the relative success of social cooperatives and CICs, it is not surprising that one of these "levers" is social entrepreneurship.[310]

To that end, the Commission suggested comprehensive European legislation to develop a framework for social investment funds, which would "scale up the impact of national initiatives by opening Single Market opportunities"[311] to investors from all Member States. In this way, the Commission hopes to build upon the growing trend of social enterprise by promoting societal concerns such as social, ethical, and environmental development over financial profit.[312] Indeed, the Commission estimated that social cooperatives represent more than 4.8 million European jobs, and it believed that many more can be created to stem the rising tide of unemployment.[313]

---

[304] *See Single Market Act: Twelve Levers to Boost Growth and Strengthen Confidence*, at 24–25, COM (2011) 206 final (Apr. 13, 2011).
[305] *Id.*
[306] *See Europe 2020: A Strategy for Smart, Sustainable and Inclusive Growth*, at 2, COM (2010) 2020 final (Mar. 3, 2010).
[307] *Id.* at 5; *see also Single Market Act*, *supra* note 304, at 3.
[308] *Single Market Act*, *supra* note 304, at 3.
[309] *Id.*
[310] *Id.* at 14–15.
[311] *Id.* at 14.
[312] *Id.* at 14–15.
[313] *Id.* at 15 n.49.

In keeping with continental Europe's charity-centric view of social enterprise, the European Commission released a "Social Business Initiative" to operate within the framework of the European Platform against Poverty and Social Exclusion.[314] Notably, the Commission emphasized a 2009 study that concluded that approximately one in four businesses founded in Europe fall under the umbrella of social enterprise.[315] The Social Business Initiative addressed several shortcomings of the current social enterprise sector and set forth an action plan to address these concerns. First, echoing the suggestions of the "Twelve Levers" communication, the Commission suggested creating a regulatory framework for investment vehicles at the European level to increase private funding to social enterprises.[316] This includes a proposal for a €90 million financial instrument to facilitate cross-border funding for the start-up, development, and expansion of social enterprises.[317] Second, to increase the visibility of social enterprise, the Commission suggested identifying best practices in the sector, creating a public database of labels and certifications, and the promotion of mutual learning and capacity building at the national and regional level.[318] Third, to improve the legal environment, the Commission proposed reforming the Statute for a European Cooperative Society to simplify regulation and conducting a study on the status of social cooperatives in all Member States.[319] Lastly, to facilitate government funding of social enterprise, the Commission suggested simplifying the rules regarding State aid to work integration and personal services, and enhancing social and health elements in the government procurement process.[320]

These communications make clear that Europe's governing bodies are increasingly serious about fostering the growth of social enterprise. Creating a Europe-wide regulatory scheme and regional investment funds appear to be necessary steps to elevate social enterprise from the national level to the regional level. However, whether the European Parliament follows through with these suggestions remains to be seen.

For the moment, European social enterprise operates on the local and state levels. The legal landscape continues to be a patchwork of social cooperatives

---

[314] *Social Business Initiative: Creating a Favourable Climate for Social Enterprises, Key Stakeholders in the Social Economy and Innovation*, at 2, COM (2011) 682 final (Oct. 25, 2011) [hereinafter *Creating a Favourable Climate for Social Enterprises*].

[315] *Id.* at 3; *see also* SIRI TERJESEN ET AL., GLOBAL ENTREPRENEURSHIP MONITOR, 2009 REPORT ON SOCIAL ENTREPRENEURSHIP 20 (2009), *available at* http://www.gemconsortium.org/docs/download/2519.

[316] *Creating a Favourable Climate for Social Enterprises*, *supra* note 314, at 6–7.

[317] *Id.* at 8.

[318] *Id.*; *see also CIC Register*, *supra* note 294.

[319] *Creating a Favourable Climate for Social Enterprises*, *supra* note 314, at 10.

[320] *See id.* at 10–11.

and designations that enjoy varying degrees of success. The U.K.'s CIC, however, appears to confirm that embracing minimal profit distribution has been a key factor in the expansion and success of social enterprise. Despite this conclusion, the suggestions of the European Commission continue to reflect a narrow view of social enterprises as strictly charitable organizations. Indeed, the prohibition on profit distribution and the rejection of blended-value models will likely impede the growth of social enterprise in an economic climate that cries out for innovation and mold-breaking approaches. In contrast, the next Part explores the recent emergence of social enterprise entities in the United States, which bear a much closer resemblance to the U.K. than continental Europe.

III. SOCIAL ENTERPRISE IN THE UNITED STATES

A. First Generation Entities

In contrast with Europe, where social enterprise entities have been in existence for decades, the social enterprise revolution in corporate law in the United States is still in its early stages.[321] However, the past five years have witnessed significant growth in both financing for social enterprise and increased diversity along the spectrum of entities offered to social entrepreneurs. Indeed, socially responsible investments grew more than 13% in the face of the worst economic downturn since the Great Depression,[322] and account for more than $3 trillion in professionally managed assets in the United States.[323]

A number of entities have been authorized in U.S. jurisdictions that purportedly serve the mission-driven purpose of social entrepreneurs,[324] and unlike Europe, these entities are not subject to a prohibition on the distribution of profits to shareholders. In the United States, social enterprise and its accompanying entities constitute a so-called "fourth sector" of the economy[325] uniquely committed to simultaneously earning profits for shareholders

---

[321] *See* Sarah Stankorb, *Where Did Social Enterprise Come From Anyway?*, GOOD (Mar. 8, 2012), http://www.good.is/post/where-did-social-enterprise-come-from-anyway (quoting Jay Coen Gilbert, co-founder of B Labs: "this was a long process of gestation").

[322] *See* 2010 US-SIF REPORT, *supra* note 10, at 8.

[323] *Id.*

[324] *See generally infra* Part III.B–E (discussing L3Cs, Flexible Purpose Corporations, Social Purpose Corporations, and Benefit Corporations).

[325] Kelley, *supra* note 7, at 340 ("According to [proponents of social enterprise], we are in the process of moving beyond the traditional conception of society as divided neatly into three sectors—business, nonprofit, and government—and are witnessing the emergence of a new fourth sector that encompasses elements of both the business and nonprofit sectors."); J.

and creating social and environmental benefits.[326] This Part identifies and discusses four recently enacted social enterprise entities, to wit: (1) Low-Profit Limited Liability Companies (L3Cs), (2) Flexible Purpose Corporations (FPCs), (3) Social Purpose Corporations (SPCs), and (4) Benefit Corporations.

B. L3Cs

In 2008, Vermont became the first state to enact the L3C.[327] Several other states quickly followed suit. At the time of this writing, L3Cs have been enacted in six states and two Native American nations,[328] and they are under consideration in at least twelve state legislatures.[329] In general, L3C legislation amends a state's existing Limited Liability Company (LLC) statute, creating a specific type of LLC subject to certain restrictions designed to create a safe and reliable corporate entity for receiving Program Related Investments (PRIs) from private foundations.[330] In order for an organization

---

Haskell Murray & Edward I. Hwang, *Purpose with Profit: Governance, Enforcement, Capital-Raising and Capital-Locking in Low-Profit Limited Liability Companies*, 66 U. MIAMI L. REV. 1, 6–7 (2011).

[326] Defourny, *supra* note 27, at 5.

[327] Jim Condos, Vermont Secretary of State, *Low-Profit Limited Liability Company*, VT. SECRETARY OF ST. (2004), http://www.sec.state.vt.us/corps/dobiz/llc/llc_l3c.htm (last visited Mar. 23, 2013); *see also* VT. STAT. ANN. tit. 11, § 3001(27) (2012).

[328] Low-Profit Limited Liability Company, 805 ILL. COMP. STAT. 180/1-26 (2010); Limited Liability Companies, LA. REV. STAT. ANN. § 12:1302 (2010); Low-Profit Limited Liability Company, ME. REV. STAT. tit. 31, § 1611 (2010); Michigan Limited Liability Company Act, MICH. COMP. LAWS § 450.4102 (2009); North Carolina Limited Liability Company Act, N.C. GEN. STAT. § 57C-2-01 (2010). In addition, the Oglala Sioux Tribe and the Crow Indian Nation of Montana have also enacted L3C legislation. *Laws*, AMERICANS FOR COMMUNITY DEV., http://www.americansforcommunitydevelopment.org/laws (last visited Mar. 23, 2013). Utah and Wyoming enacted similar legislation, their L3C acts were subsequently repealed. Utah Revised Limited Liability Company Act, UTAH CODE ANN. § 48-2c-412 (West 2009); Limited Liability Companies, WYO. STAT. ANN. § 17-15-102 (2009).

[329] *See* Daniel S. Kleinberger, *A Myth Deconstructed: The "Emperor's New Clothes" on the Low-Profit Limited Liability Company*, 35 DEL. J. CORP. L. 879, 880 n.7 (2010) (listing the twelve states in which L3C legislation is currently under consideration).

[330] *See* MARC J. LANE, SOCIAL ENTERPRISE: EMPOWERING MISSION-DRIVEN ENTREPRENEURS 36 (2011); Doeringer, *supra* note 254, at 319 (describing the primary purpose of the L3C as making it cheaper and easier for foundations to determine where they can invest with PRIs, thus increasing available capital for social enterprise); J. William Callison & Allan W. Vestal, *The L3C Illusion: Why Low-Profit Limited Liability Companies Will Not Stimulate Socially Optimal Private Foundation Investment in Entrepreneurial Ventures*, 35 VT. L. REV. 273, 282 (2010) ("The L3C promoters seek to use this highly malleable LLC form to accomplish another goal, namely allowing private foundations to increase their PRIs and thereby to provide social benefit."); Kleinberger, *supra* note 329, at 884 ("L3C proponents claim that L3C status will streamline the PRI process."); Reiser, *supra* note 265, at 622 (discussing how

to qualify as a L3C, the entity's articles of incorporation must contain certain provisions, including: (1) stating a primary charitable or educational purpose, (2) conversely stating that the entity does not have a significant purpose for the production of income or appreciation of property, and (3) stating that the entity does not have a political or legislative purpose.[331] In addition, most states require that an L3C include the "L3C" designation in its name.[332]

To fully understand the L3C, one must first understand the Internal Revenue Code (IRC) provisions relevant to 501(c)(3) tax-exempt entities. Of the twenty-eight types of organizations entitled to be tax-exempt under the IRC, the 501(c)(3) entities are the most common, and are divided into two categories: private foundations and public charities.[333] All 501(c)(3)s are subject to the prohibition on private inurement to the benefit of any private shareholder or individual.[334] Private foundations, unlike charities, are subject to stricter regulations and graduated excise taxes,[335] but they are permitted to take advantage of PRIs, which have been part of nonprofit law since the Tax Reform Act of 1969.[336]

In short, PRIs are a way for grant-making foundations to make tax-free jeopardy investments in socially beneficial businesses rather than making traditional grants to charities.[337] When a foundation makes a PRI, the IRS permits the foundation to count that grant towards the 5% of the foundation's assets it is required to distribute annually, on pain of excise taxes and potential loss of tax-exempt status.[338] While PRIs offer foundations the option of

---

the L3C model was conceived as easily meshing with existing state LLC statutes and how it was to contain sufficient restrictions to enable L3Cs to qualify for receipt of PRIs under existing IRS rules).

[331] LANE, *supra* note 330, at 35.

[332] *See, e.g.*, VT. STAT. ANN. tit. 11, § 3005(a)(2) (2012).

[333] Fishman, *supra* note 26, at 568.

[334] *Id.* at 584.

[335] *Id.* at 582 ("Sections 4940 to 4945 were added to the IRC and imposed a sliding scale of excise taxes (depending upon the offending foundation's willingness to correct its wrong) for abuses in which Congress felt private foundations were most likely to engage."). For a more thorough discussion of the excise tax provisions applicable to private foundations, see Examples of Program-Related Investments, Prop. Treas. Reg. § 53.4944, 77 Fed. Reg. 23,429 (Apr. 19, 2012) (to be codified at 26 C.F.R. 53.4944-3).

[336] Tax Reform Act of 1969, Pub. L. No. 91-172, § 4944(c), 83 Stat. 487, 512 (1969).

[337] *See* Doeringer, *supra* note 254, at 317. Notably, the Ford Foundation has committed over $400 million in PRIs since pioneering the practice in 1968. *See* FORD FOUND., INVESTING FOR SOCIAL GAIN: REFLECTIONS ON TWO DECADES OF PROGRAM-RELATED INVESTMENTS 12 (1991).

[338] *See* I.R.C. § 4944 (2007); *see also*, *e.g.*, I.R.C. § 4942 (2007) (providing that if a foundation does not fulfill the 5% distribution requirement, it can be liable for a 100% tax on the undistributed amount).

making jeopardy investments to satisfy the 5% annual asset distribution requirement, the IRS has, until very recently, offered little guidance on what investments qualify as PRIs. In fact, the IRS has issued only one Private Letter Ruling concerning a PRI to a LLC[339] and has yet to issue any to a L3C.[340]

The historic confusion about tax treatment of PRIs has led to a reluctance on the part of foundations to actively pursue PRIs for fear of tax risks.[341] Indeed, such investments may be labeled "jeopardizing" by the IRS and incur the corresponding 5% tax on the investment.[342] Alternatively, the IRS may determine that the entity receiving the PRI does not adequately further an exempt purpose. Such an investment would be subject to the Unrelated Business Income Tax (UBIT) and would incur a corporate income tax on the profits earned from any nonexempt business activities.[343] Moreover, the investment would not count towards the foundation's 5% distribution requirement,[344] and it would also potentially incur a 20% tax on taxable expenditures.[345] As a result, many foundations have remained reluctant to distribute their assets via PRIs and instead opt for the safer course of simply distributing assets to charities.[346]

In an attempt to encourage foundations to increase their PRIs to social enterprises, drafters of L3C statutes transliterated the PRI requirements into

---

[339] *See generally* I.R.S. Priv. Ltr. Rul. 2006-10-020 (Mar. 10, 2006); *see also* Klienberger, *supra* note 329, at 892; Murray & Hwang, *supra* note 325, at 25–26.

[340] As Matthew Doeringer notes, the dearth of Private Letter Rulings in this regard may be explained by the fact that the IRS charges $8,700.00 per Private Letter Ruling, and the accompanying attorneys fees can be as much as $50,000.00. Moreover, foundations may incur additional costs in connection with investment oversight, as the IRS may require annual reports confirming the company is using the PRI to further an exempt purpose. Doeringer, *supra* note 254, at 318.

[341] Lauren Burnhill, *More PRI Funding for the BOP? Yes – and You Can Help!*, CENTER FOR FIN. INCLUSION BLOG (May 29, 2012), http://cfi-blog.org/2012/05/29/more-pri-funding-for-the-bop-yes-and-you-can-help/ (noting that "[f]or fear of endangering their tax status, most foundations have exclusively focused on making grants to non-profit organizations").

[342] *See* Treas. Reg. § 53.4944-1 (1972).

[343] Treas. Reg. § 1.501(c)(2)-1(b) (1960); *see also* Katz & Page, *Role of Social Enterprise*, *supra* note 16, at 79 (noting as well that, should a company involve itself in too many unrelated business activities, it can lose the exemption entirely).

[344] Doeringer, *supra* note 254, at 318–19.

[345] I.R.C. § 4945(a)(1) (2006). As Callison and Vestal note, there is also a 5% tax on foundation managers, and both taxes increase if the expenditure is not corrected within the statutory period. *Id.* § 4845(a)(2)–(b)(2); *see also* Callison & Vestal, *supra* note 330, at 278 n.29.

[346] Jonathan Greenblatt, *Opening the Door for Program Related Investments*, STAN. SOC. INNOVATION REV. BLOG (May 11, 2012), http://www.ssireview.org/blog/entry/opening_the_door_for_program_related_investments ("PRI's historically have not been used with much frequency because of confusion as to how they work and the high costs associated with them.").

the L3C statutes.[347] Indeed, L3Cs are required by statute to operate in accordance with IRS standards for organizations that qualify for PRIs.[348] While these provisions appear to ameliorate the tax risks posed by PRIs and give foundations a green light to streamline PRIs into L3Cs free from tax concerns, many commentators have criticized this approach as insufficient.

J. William Callison and Allan W. Vestal emphasize that Congress has not amended the IRC's PRI provisions to explicitly include investments in L3Cs,[349] and they conclude that "without changes to federal PRI rules, the L3C construct has little or no value."[350] Daniel S. Kleinberger has gone so far as to suggest that "the 'L3C' is an unnecessary and unwise contrivance; its very existence is inherently misleading."[351] He submits that the statutory restrictions placed on L3Cs are already possible under every state's flexible LLC statutes, and that without amendment to the IRC, "L3C legislation does nothing to help foundations seeking to assure themselves of PRI treatment."[352]

J. Haskell Murray and Edward I. Hwang concede this point, but they counter it by underscoring the fact that an L3C may not abandon its devotion to PRI requirements without sacrificing its specialized corporate status.[353] They contend that tax risks to foundations could be "reduced if prescient drafting of the foundation-L3C agreement includes a stop-loss provision or other reinvestment options upon an L3C cessation."[354] While a properly drafted agreement might reduce some tax risks to foundations, the fact remains that without guidance from the IRS, L3Cs do not live up to their purported ability to streamline the PRI process by providing a reliable PRI receiver. Tyler acknowledges this uncertainty but argues that L3Cs are not enentirely dependent on foundation funding, and that the entity "transcend[s] foundation involvement."[355] However, Tyler's argument for transcendence is hard to square with the almost universally PRI-centric arguments made by L3C proponents during the legislative process and after its enactment.[356]

---

[347] Murray & Hwang, *supra* note 325, at 26–33.

[348] *See, e.g.*, VT. STAT. ANN. tit. 11, § 3001(27)(A)(i) (2012) (requiring that an L3C "significantly further the accomplishment of one or more charitable or educational purposes within the meaning of [I.R.C. § 170(c)(2)(B)]"); VT. STAT. ANN. tit. 11, § 3001(27)(C) (requiring that an L3C not have the purpose of accomplishing "one or more political or legislative purposes within the meaning of [I.R.C. § 170(c)(2)(D)]").

[349] Callison & Vestal, *supra* note 330, at 273–74.

[350] *Id.* at 274.

[351] Klienberger, *supra* note 329, at 881.

[352] *Id.* at 908.

[353] *See* Murray & Hwang, *supra* note 325, at 32.

[354] *Id.*

[355] Tyler, *supra* note 21, at 125.

[356] *The Concept of the L3C*, AMERICANS FOR COMMUNITY DEV., http://americansforcommunitydevelopment.org/concept.html (last visited Mar. 23, 2013) ("The keys to an L3C's

In response to these critiques, Reps. Aaron Schock (R-IL) and Jared Polis (D-CO) introduced the Philanthropic Facilitation Act of 2011 (H.R. 3420) on November 14, 2011.[357] Notably, the bill sought to amend the IRC's definition of PRIs and provide for administrative review of whether investments qualify as PRIs.[358] The bill was referred to the House Committee on Ways and Means, and it has yet to emerge; nonetheless, its introduction appears to have had an impact. In fact, on April 19, 2012, the IRS released a notice of proposed rulemaking regarding PRIs.[359] The proposed regulations add nine new examples that "illustrate that a wider range of investments qualify as PRIs than the range currently presented in § 53.4944-3(b) ... [and] demonstrate that a PRI may accomplish a variety of charitable purposes."[360] These examples illustrate new PRI principles, to wit: (1) PRIs may be made to activities furthering charitable purposes in foreign countries, (2) PRIs are not limited to situations involving economically disadvantaged individuals or deteriorated urban areas, (3) a potentially high rate of return on investment does not automatically prevent an investment from being considered a PRI, and (4) PRIs can be achieved through a variety of investment instruments, "including loans to individuals, tax-exempt organizations and for-profit organizations, and equity investments in for-profit organizations."[361] Most importantly, the IRS has stated that taxpayers may rely on these examples "before these proposed regulations are finalized."[362]

While the L3C is not explicitly mentioned in the proposed amendments to § 53.4944-3(b), some of the examples do appear to apply to L3Cs. Example 16 posits a hypothetical in which X, an LLC, purchases coffee from poor farmers residing in a developing country.[363] Y, a private foundation, makes a low-interest loan to X to fund the provision of efficient water, pest and farm

---

operation is its use of low-cost foundation capital in a high risk tranche of its structure and its ability to allocate risk and reward unevenly over a number of investors, thus ensuring some a very safe investment with market return. As is appropriate under the PRI structure, foundations would normally be expected to assume the highest risk at very low return, making the rest of the investment far more secure."); *see also* Klienberger, *supra* note 329, at 894 n.72 (identifying the remarks of several legislators focusing on the L3C's supposed PRI fast track).

[357] The Philanthropic Facilitation Act of 2011, H.R. 3420, 112th Cong. (2011).

[358] *Id.*; *see also* Westaway, *supra* note 26.

[359] Examples of Program-Related Investments, Prop. Treas. Reg. § 53.4944, 77 Fed. Reg. 23,429 (Apr. 19, 2012) (to be codified at 26 C.F.R. 53.4944-3).

[360] *Id.* at 23,430.

[361] *Id.* at 23,429–30; *see also* Anne Field, *IRS Rule Could Help the Fledgling L3C Corporate Form*, FORBES, May 4, 2012, http://www.forbes.com/sites/annefield/2012/05/04/irs-rules-could-help-the-fledgling-l3c/.

[362] Examples of Program-Related Investments, Prop. Treas. Reg. § 53.4944, 77 Fed. Reg. at 23,429 (Apr. 19, 2012) (to be codified at 26 C.F.R. 53.4944-3).

[363] *Id.* at 23,431.

management, and crop cultivation.[364] Because Y's primary purpose in making the loan is the education of poor farmers, and not the production of income, the loan significantly furthers Y's exempt activities and qualifies as a PRI.[365] This example illustrates several principles: first, foundations may safely make PRIs to LLCs and, in theory, L3Cs; second, PRIs may be made to further educational and environmental purposes; and third, PRIs may be made to organizations with operations outside the United States.

The impact these examples will have on the PRI practices of private foundations remains unclear. However, the amendments and accompanying principles do address many concerns regarding the tax consequences of PRIs and appear to provide assurances for tax treatment of potential investments. Indeed, these new examples may signal the alignment of substance and form and usher in a new era of tranched investments in L3Cs and other mission-driven entities. However, such an outcome might also have negative effects on existing nonprofits, particularly public charities that already rely heavily on foundation funding.[366] Is social enterprise at the expense of traditional charity a desirable outcome?[367] This question raises much broader issues that are beyond the scope of this Article, but to the extent the IRS has succeeded in alleviating the tax concerns regarding L3Cs and opened the floodgates for PRIs, these issues merit a thoughtful discussion.

Looking beyond the funding issues associated with L3Cs, other commentators have criticized the governance structure of these entities. Some scholars have noted that the dual charitable and financial purposes of L3Cs "invite an apparent conflict of fiduciary duties"[368] and leave directors with little guidance regarding how to prioritize these duties when confronted with competing financial goals and tax-exempt purposes.[369] John Tyler dubs this the "problem of two masters" and argues that L3C statutes "clearly impose an unambiguous ordering of fiduciary priorities[:] ... the theory and purpose of the L3C [is to] prioritize charitable, exempt purposes as a fiduciary matter."[370] Thus, in Tyler's view, the charitable purpose trumps shareholder wealth-maximization, a conclusion that appears consistent

---

[364] *Id.*

[365] *Id.*

[366] *See* Anurag Gupta, Note, *L3Cs and B Corps: New Corporate Forms Fertilizing the Field Between Traditional For-Profit and Nonprofit Corporations*, 8 N.Y.U. J.L. & BUS. 203, 220 (2011).

[367] *Id.*

[368] Murray & Hwang, *supra* note 325, at 32.

[369] *See id.*; Kleinberger, *supra* note 329, at 900.

[370] Tyler, *supra* note 21, at 141.

with the "low-profit" moniker of the L3C.[371] Murray and Hwang share this view and argue that fiduciary duties imposed on managers of L3Cs should be modeled after the fiduciary duties imposed on nonprofit managers.[372] While this interpretation might provide some guidance at the highest levels of L3C governance, it still leaves much to be desired in the context of implementation on a day-to-day basis, and it does not adequately address how and to what extent the preeminence of charitable purposes effects directors' duties of care and loyalty. Some commentators embrace this apparent conflict and see it as a benefit that encourages "a candid harmonization of goals."[373] L3Cs would certainly invite a candid harmonization, but legitimate concern regarding the governance of L3Cs and managers' fiduciary duties may pose another hurdle for L3C proponents, notwithstanding any amendment to the IRC.

In sum, the L3C has been the most widely criticized social enterprise entity. However, recent developments appear to address some of the tax concerns regarding L3C funding. Despite this progress, legitimate questions remain about L3C governance and the fiduciary duties of L3C managers. At the moment, the L3C may be the right choice of entity for some social entrepreneurs with foundation support, but it is likely burdened by too much uncertainty for many aspiring social entrepreneurs.

C. Flexible Purpose Corporations

October 9, 2011 was a landmark day for emerging corporate entities in California. On that day, Governor Edmund G. Brown, Jr. signed two bills into law: first, AB 361,[374] which made California the sixth state to authorize the benefit corporation,[375] and second, SB 201, also known as the Corporate Flexibility Act of 2011.[376] The latter provided for a new type of

---

371 *Id.*; *see also* Murray & Hwang, *supra* note 325, at 40 ("The PRI requirements built into the L3C statute mandate that the L3C's *ultimate* master be 'charitable purpose' .... When the profit master and the charitable purpose master irreconcilably conflict in the operation of an L3C, however, the charitable purpose master must rule.").

372 Murray & Hwang, *supra* note 325, at 41. Conversely, the authors argue that enforcement of those duties should resemble for-profit enforcement mechanisms, including affording directors of L3Cs the protection of the business judgment rule. *Id.*

373 LANE, *supra* note 330, at 42.

374 *See Complete Bill History of AB 361*, OFFICIAL CAL. LEGIS. INFO., http://www.leginfo.ca.gov/pub/11-12/bill/asm/ab_0351-0400/ab_361_bill_20111009_history.html (last visited Mar. 23, 2013).

375 Sven Eberlein, *The Start of a Revolution*, DAILY KOS (Jan. 11, 2012, 3:46 PM), http://www.dailykos.com/story/2012/01/11/1053080/-The-Start-of-a-Revolution.

376 Corporate Flexibility Act of 2011, CAL. CORP. CODE §§ 2500–2517 (West 2011).

corporate entity—namely, the flexible purpose corporation (FPC).[377] This Section explores the governance structure and the liabilities associated with this new entity.

An FPC may be either publicly traded or closely held,[378] and it is required to include the words "flexible purpose corporation" or "FPC" in its name.[379] Its articles of incorporation must include a statement enumerating the purposes of the FPC.[380] Importantly, a FPC must be organized for one or more of the following purposes: (1) charitable purposes like those nonprofits carry out;[381] or (2) promoting positive short-term or long-term effects or minimizing adverse short-term or long-term effects of the FPC's activities on its "employees, suppliers, customers, and creditors," "the community and society," and "the environment."[382] These two broadly defined categories offer an FPC substantial discretion to select its blended value purpose and enshrine the hallmark flexibility of this entity in its articles of incorporation.

In addition to the mandatory provisions discussed above, a FPC's articles of incorporation may also include several discretionary provisions. Some of these include setting forth special qualifications for shareholders,[383] setting forth a termination date for the FPC,[384] restricting the business in which the FPC engages in,[385] or requiring a vote of a larger proportion or of all the shares of any class or series before the FPC takes "any or all corporate actions."[386] The articles may also limit the liability of directors for money damages in actions brought by the FPC or derivative actions brought by shareholders for breach of directorial duties.[387] However, these discretionary limits on liability are subject to numerous exceptions[388] and are only available for directors, not officers, of the FPC.[389]

---

[377] *Id.*

[378] *Id.* § 2503.1. Additionally, FPCs may engage in a wide range of business activities, commercial or industrial banking, the trust business, or the title insurance business, subject to the applicable provisions of the California Financial Code. *Id.* § 2510.

[379] *Id.* § 2602(a).

[380] *Id.* § 2602(b)(1).

[381] CAL. CORP. CODE § 2602(b)(2)(A) (West 2011).

[382] *Id.* § 2602(b)(2)(B)(i)–(iii).

[383] *Id.* § 2603(a)(3).

[384] *Id.* § 2603(a)(4).

[385] *Id.* § 2603(a)(6).

[386] *Id.* § 2603(a)(5).

[387] CAL. CORP. CODE § 2603(a)(10) (West 2011).

[388] *See id.* § 2603(a)(10)(A)–(B).

[389] *Id.* § 2603(a)(10)(C).

Thus, the corporate purpose provisions of the FPC's authorization statute requires the founders to select at least one charitable, social, or environmental purpose.[390] The FPC, like the L3C, may be created for primarily charitable purposes. The main difference, however, is that where the L3C is designed to receive PRIs from foundations, the FPC is designed to raise equity capital.[391] Note that nowhere in the FPC statute will one find the term "low-profit," nor is there a prohibition or cap on dividends, thus making it more appealing to a broader group of investors. In other words, an FPC created for a charitable or environmental purpose[392] would arguably qualify for a PRI under the proposed IRS regulations discussed above, but it may also raise equity capital from socially responsible investors. Thus, the FPC represents a truly blended corporate form, where the articles of incorporation enshrine both profit motive and social and environmental benefits as corporate purposes.

With respect to fiduciary duties, FPC directors are generally obligated to perform their duties in good faith and with reasonable care "in a manner the director believes to be in the best interests of the flexible purpose corporation and its shareholders."[393] In discharging those duties, directors may consider and give weight to factors the director deems relevant, including the "short-term and long-term prospects of the flexible purpose corporation, the best interests of the flexible purpose corporation and its shareholders," and the social or environmental interests set forth in the articles of incorporation.[394] Directors are insulated from liability based upon any alleged failure to act,[395] and stakeholders are explicitly denied a right of action against directors.[396]

However, creditors and shareholders are given some limited rights of action against the FPC and its directors, although the extent of liability in these cases may be capped or subject to indemnification by the FPC. Section 2701 provides limited rights of action for creditors or shareholders of the FPC.[397] A director may also be liable to creditors for distributing assets

390 *Id.* § 2602(b)(2)(A), (B)(i)–(iii).

391 *See* SUSAN H. MAC CORMAC, NEW CORPORATE Forms: FLEXIBLE PURPOSE CORPORATIONS, BENEFIT CORPORATIONS, AND L3CS, (Berkeley Ctr. for Law, Bus. & Econ., Berkeley, Cal., Nov. 8, 2011), *available at* http://www.law.berkeley.edu/files/bclbe/Berkeley_Handout_1182011_-_1.pdf.

392 CAL. CORP. CODE § 2602(b)(2)(A) (West 2011).

393 *Id.* § 2700(a).

394 *Id.* § 2700(c).

395 *Id.* § 2700(d).

396 *Id.* § 2700(f).

397 *Id.* § 2701(a). For example, a director may be liable to shareholders for making any distribution to the shareholders contrary to sections 500 to 503 of the California Corporate Code. *Id.* § 2701(c)(1).

to shareholders after the institution of dissolution proceedings.[398] Moreover, directors who abstain from voting are deemed to have approved the decision and do not escape liability for the aforementioned actions.[399] However, even the minimal FPC director liability can effectively be circumvented by virtue of capping damages and indemnification provisions.[400]

Accountability of the FPC to its blended corporate purposes is addressed in its unique reporting requirements. FPC's are required to issue "annual reports,"[401] which must be sent to the shareholders and also be made publicly available on the FPC's website.[402] The statute requires the annual reports to include an end-of-year balance sheet and a management discussion and analysis (MD&A) of issues such as the short-term and long-term objectives of the FPC relating to its specific purpose(s) and the effectiveness of the material actions taken to achieve those purposes.[403] In addition to this annual reporting requirement, FPCs are also required to issue a "special purpose current report" to the shareholders and the public within forty-five days of a material action or expenditure related to the FPCs specific purposes.[404] These special purpose reports are designed to ensure FPCs transparency to the shareholders and the public by identifying and discussing all material expenditures made in furtherance of the FPC's special purposes.

The FPC model, however, is not without problems. The corporate purpose categories are certainly flexible, but they may be so broadly drafted that they risk losing all meaning. This problem is exacerbated by the two-level reporting structure, which imposes added costs on the FPC without requiring that the reports be assessed against an independent third-party standard. As discussed above, this leaves open the possibility of manipulating reported data to the FPC's advantage while its directors simultaneously benefit from expansive liability protections.[405] This point is driven home when one considers that the board of directors is given sole discretion to determine what information to include in the annual and special purpose reports.[406]

---

[398] CAL. CORP. CODE § 2701(c)(2) (West 2011).

[399] *Id.* § 2701(b).

[400] Damages obtained from directors in these actions are capped at the amount of the illegal distribution, or the fair market value of the property at the time of the illegal distribution, plus interest. *Id.* § 2701(d). Furthermore, a FPC may elect to indemnify any director from any and all claims pursuant to section 2702(b). *Id.* § 2702(b).

[401] *Id.* § 3500.

[402] CAL. CORP. CODE § 3500(b) (West 2011).

[403] *Id.* § 3500(b)(1)–(5).

[404] *Id.* § 3501.

[405] *See, e.g.*, *id.* § 3502(a) (conferring discretion on both management and the board when providing the information required by section 3501).

[406] *Id.*

The broad limitations on liability also present the problem of accountability to the FPC's stated social or environmental purposes. As R. Todd Johnson, energy practice leader at Jones Day's Silicon Valley office, has noted, the FPC "seeks to unleash directors from the risk of liability, permitting them to experiment more broadly with the right mix of doing well and doing good, without concerns of personal or corporate suits."[407] However, it is unclear whether this experiment will serve the needs of the social enterprise movement. Curiously, the FPC employs a combination of unchecked directorial power and lack of standardized and independent reporting requirements, which have historically been poor bedfellows for social and environmental progress. The FPC's lack of accountability and specificity may, in turn, create the impression amongst socially responsible investors that FPCs lack legitimacy. In sum, the FPC may live up to its name as a genuinely "flexible" purpose corporation in the context of director liability and blended corporate purpose, but the potential for abuse, along with onerous reporting requirements, does little to contribute to the development of social enterprise law.

D. Social Purpose Corporations

On March 30, 2012, three months after its introduction,[408] Washington Governor Chris Gregoire signed Substitute House Bill 2239 (SHB 2239) into law, which authorized the creation of yet another entity, the social purpose corporation (SPC).[409] SPCs, much like FPCs, must include a corporate purpose statement in their articles of incorporation. All SPCs must be organized as follows: "[I]n a manner intended to promote positive short-term or long-term effects of, or minimize adverse short-term or long-term effects of, the corporation's activities upon any or all of (1) the corporation's employees, suppliers, or customers; (2) the local, state, national, or world community; or

---

[407] R. Todd Johnson, *The Benefit Corporation: A Step in the Right Direction, but ...*, BUS. FOR GOOD (June 12, 2010, 12:01 PM), http://businessforgood.blogspot.com/2010/06/benefit-corporation-step-in-right.html.

[408] House Bill 2239 (HB 2239) was introduced into the Washington State House of Representatives on January 10, 2012. A companion bill, Senate Bill 6230 (SB 6230), was introduced on February 15, 2012 in the Washington State Senate. Both bills were quickly voted through their respective houses. On February 13, 2012, HB 2239 passed in the House with a vote of 62 yeas, 31 nays, and 5 excused; on March 2, 2012, SB 6230 passed in the Senate with a vote of 34 yeas, 14 nays, and 1 excused. *See H.B. 2239 Establishing Social Purpose Corporations: History of the Bill*, WASH. ST. LEG., http://apps.leg.wa.gov/billinfo/summary.aspx?bill=2239&year=2011 (last updated Mar. 5, 2013).

[409] *See* S.H.B. 2239, § 1, 62d Leg., Reg. Sess. (Wash. 2012), *available at* http://apps.leg.wa.gov/documents/billdocs/2011-12/Pdf/Bills/House%20Passed%20Legislature/2239-S.PL.pdf.

(3) the environment."[410] This language is similar to the FPC requirement; however, the category of "charitable purposes" is notably absent. SPCs are also given the option to select one or more "specific social purposes," although the bill does not provide a list of examples of such purposes.[411]

Existing organizations may convert to SPC status,[412] provided they amend their articles of incorporation to include the following: (i) a statement that the corporation is a social purpose corporation; (ii) a statement setting forth the general social purpose and specific social purposes, if any; and (iii) the following mission statement: "The mission of this social purpose corporation *is not necessarily compatible with and may be contrary to maximizing profits and earnings for shareholders*, or maximizing shareholder value in any sale, merger, acquisition, or other similar actions of the corporation."[413] These requirements, along with the mandate that a SPC include the term "social purpose corporation" or "SPC" in its name,[414] serve to put any potential investors on notice that the SPC is an entity that may subrogate shareholder value in favor of social or environmental interests. In contrast with the L3C, where charitable purpose arguably overrides profit maximization, the SPC takes a more flexible approach by giving directors the discretion to choose social and environmental purposes over profits in all circumstances.

The statute also includes provisions designed to ensure that SPCs retain their general and specific social purposes. For example, in the event an amendment to the articles of incorporation is proposed that would materially alter one or more of the SPC's social purposes, the bill requires a minimum of a two-thirds majority to pass the amendment.[415] The same applies to situations in which the SPC is involved in a merger or transaction in which it is not the surviving corporation or one that will dispose of all or substantially all of its assets.[416] In the event such votes succeed, the shareholders of an SPC are entitled to dissent and obtain a fair market buyout of their shares.[417]

SPC directors also enjoy limited liability. Directors are shielded from liability against derivative actions for failure to maximize shareholder value

---

[410] *Id.* § 3.

[411] *Id.* § 4.

[412] *Id.* § 14 (permitting any corporation that is not a SPC to become a SPC, subject to conditions set forth in § 14(1)(a)–(c)).

[413] *Id.* §§ 5(1)(b)–(e), 14(3) (emphasis added) (internal quotation marks omitted).

[414] *Id.* § 5(1)(a).

[415] S.H.B. 2239, § 10, 62d Leg., Reg. Sess. (Wash. 2012), *available at* http://apps.leg.wa.gov/documents/billdocs/2011-12/Pdf/Bills/House%20Passed%20Legislature/2239-S.PL.pdf (providing in addition that an SPC may require a greater vote in its articles of incorporation).

[416] *Id.* §§ 11–12.

[417] *Id.* § 13(2)–(3).

by virtue of the mission statement discussed above.[418] The statute gives directors the discretion to "consider and give weight to one or more of the social purposes of the corporation as the director deems relevant,"[419] and it provides that any directorial action or failure to act "shall be deemed to be in the best interests of the corporation" so long as the director reasonably believes the action "is intended to promote one or more of the social purposes of the corporation."[420] The statute also denies stakeholders a right of action against directors and officers of SPCs.[421]

Transparency of SPCs is addressed by requiring them to submit a "social purpose report" to the shareholders and to make the report publicly available on its website.[422] The social purpose report is required to include a "narrative discussion" regarding the social purposes of the SPC, including its efforts to promote its social purpose.[423] Additionally, the report may include a discussion of the SPC's short-term and long-term objectives, any "material actions taken by the corporation during the fiscal year to achieve its social purpose or purposes," and "[a] description of the financial, operating, or other measures" employed by the SPC for evaluating its social performance.[424] Washington Superior Courts are vested with the authority to order a social purpose report be furnished to the shareholders if appropriate notice has been given and the SPC has failed to issue a report for at least two consecutive fiscal years.[425]

While the intent behind the social purpose reporting requirement is laudable, the bill does not require that these reports be assessed against independent third-party standards. As a result, SPCs, like FPCs, are held to no higher a standard than CR reporting, leaving investors in the familiar situation of relying on voluntarily disclosed, unregulated reports assessed against unstandardized methodologies.[426] This risks leaving SPCs and FPCs unaccountable for their blended value goals. However, the SPC's distinctly anti-*Revlon*, anti-shareholder wealth maximization mission statement is a notable development in social enterprise law. Stronger reporting requirements can be found in benefit corporation statutes, the topic of the next Section.

---

[418] *See id*. § 6.
[419] *Id.* § 6(2).
[420] *Id.* § 6(3).
[421] S.H.B. 2239, § 6(4)–(5), 62d Leg., Reg. Sess. (Wash. 2012), *available at* http://apps.leg.wa.gov/documents/billdocs/2011-12/Pdf/Bills/House%20Passed%20Legislature/2239-S.PL.pdf.
[422] *Id.* § 16(1).
[423] *Id.* § 16(2).
[424] *Id.*
[425] *Id.* § 16(5).
[426] *See supra* Part II.B.

E. Benefit Corporations

1. Distinguishing "B Corporations" from Benefit Corporations

The benefit corporation has been called the "most ascendant social enterprise innovation today."[427] Like other emerging entities, benefit corporations aim to accommodate both social and financial goals by increasing the board's discretion to take social and environmental goals into account when making business decisions.[428] At the time of this writing, benefit corporations have been enacted in twelve states and the District of Columbia,[429] and legislation is currently under consideration in several more jurisdictions.[430]

The success of the benefit corporation is due in large part to the lobbying efforts of B Labs, a nonprofit organization dedicated to supporting business vehicles for "entrepreneurs and investors seeking to use business to solve social and environmental problems."[431] In addition to supporting benefit corporation legislation, B Labs has created its own private certification for "B Corporations."[432] As of March 2013, B Labs has certified 693 B Corporations spanning across sixty industries.[433]

There is a crucial distinction between "B Corporations" and benefit corporations. B Labs certifies existing organizations that wish to brand themselves as "B Corporations."[434] In contrast, benefit corporations are new corporate entities authorized under state corporate law.

---

[427] Munch, *supra* note 78, at 171.

[428] William H. Clark, Jr. & Larry Vranka, The Need and Rationale for the Benefit Cor poration: Why It Is the Legal Form That Best Addresses the Needs of Social Entrepreneurs, Investors, and, Ultimately, the Public 1 (Jan. 26, 2012), *available at* http://benefitcorp.net/storage/documents/The_Need_and_Rationale_for_Benefit_Corporations_April_2012.pdf.

[429] California, Hawaii, Illinois, Louisiana, Maryland, Massachusetts, New Jersey, New York, Pennsylvania, South Carolina, Vermont, and Virginia have all passed Benefit Corporation legislation. *See State by State Legislative Status*, BENEFIT CORP INFO. CENTER, http://www.benefitcorp.net/state-by-state-legislative-status (last visited Mar. 23, 2013).

[430] Legislatures in Alabama, Arizona, Arkansas, Connecticut, Florida, Iowa, Montana, Nevada, New Mexico, North Carolina, Oregon, Rhode Island, and West Virginia are considering bills to authorize benefit corporations. *See id.* The District of Columbia introduced benefit corporation legislation on November 15, 2011. *See id.*; *Benefit Corporation Act of 2011*, COUNCIL OF D.C., http://dcclims1.dccouncil.us/lims/legislation.aspx?LegNo=B19-0584 (last visited Mar. 23, 2013).

[431] *The Nonprofit Behind B* Corps, B CORP., http://www.bcorporation.net/what-are-b-corps/the-non-profit-behind-b-corps (last visited Mar. 23, 2013).

[432] Fei, *supra* note 24, at 41.

[433] B CORPORATION, http://www.bcorporation.net (last visited Mar. 23, 2013).

[434] Fei, *supra* note 24, at 41–42.

Organizations seeking a "B Corporation" certification must first take a "B Impact Assessment," pass an assessment review,[435] submit required documentation and adopt B Labs' amendments to their articles of incorporation,[436] and pay B Labs a certification fee.[437] Once the process is complete, B Labs certifies that the corporation is a "B Corporation," at which point it is subject to B Labs's private regulatory regime that includes randomly selected on-site reviews.[438] Additionally, B Corporations are required to prepare an annual public interest report that evaluates its progress in meeting its stated goals.[439]

Because it is self-imposed and privately regulated, B Corporation certification does not offer any special tax treatment.[440] Moreover, it fails to grant stakeholders a right of action against the B Corporation to enforce the mandate that directors consider stakeholder interests when making business decisions.[441] Dana Brakman Reiser opines that shareholders who invest in a B Corporation because of its social and environmental commitments could serve as a proxy for stakeholder constituencies, but ultimately concludes that B Corporation certification "realistically offers only moral, rather than legal, assurances to non-shareholder constituencies and social interests."[442] Therefore, Reiser argues, its most important aspect is its branding value.[443] Because B Corporations are subject to a private regulatory system, their branding value will be determined by the effectiveness of the regulation. The extent to which the B Corporation brand succeeds with benefit corporations and the other entities discussed *infra,* however, remains to be seen.

---

[435] *How to Become a B Corp*, B CORP., http://www.bcorporation.net/become-a-b-corp/how-to-become-a-b-corp (last visited Mar. 23, 2013).

[436] *See Protect Your Mission*, B CORP., http://www.bcorporation.net/become-a-b-corp/how-to-become-a-b-corp/protect-your-mission (last visited Mar. 23, 2013) (providing a link to a portion of the site that contains step-by-step instructions, depending on an entity's current legal form); *cf.* Steven J. Haymore, Note, *Public(ly Oriented) Companies: B Corporations and the Delaware Stakeholder Provision Dilemma*, 64 VAND. L. REV. 1331, 1323 (2011) (arguing that B Corporations' future may depend on the compatibility of B Labs' stakeholder charter provision with Delaware corporate law).

[437] *Make It Official*, B CORP., http://www.bcorporation.net/become-a-b-corp/how-to-become-a-b-corp/120 (last visited Mar. 23, 2013).

[438] *Id.*

[439] *Id.*

[440] Reiser, *supra* note 265, at 637.

[441] *Id.* at 640–41.

[442] *Id.* at 641–42.

[443] *See id.* at 643; *see also* Kelley, *supra* note 7, at 367 ("[T]he primary benefit of the B designation will be to create a brand for corporations that are truly and fundamentally committed to socially beneficial outcomes.").

2. *The Benefit Corporation at a Glance*

Thus far, California,[444] Hawaii,[445] Illionois,[446] Louisiana,[447] Maryland,[448] Massachusetts,[449] New Jersey,[450] New York,[451] Pennsylvania,[452] South Carolina,[453] Vermont,[454] Virginia,[455] and the District of Columbia[456] have enacted benefit corporation legislation. All benefit corporation statutes are structured around four main headings: (1) general provisions, (2) corporate purpose, (3) accountability, and (4) transparency.[457] This Section identifies three fundamental aspects of benefit corporations and then highlights some notable features specific to certain jurisdictions.

a. Corporate Purpose: Creating General and Specific Public Benefits

Every benefit corporation statute requires that the articles of incorporation include language explaining that the benefit corporation "shall have the purpose of creating a general public benefit"[458] and permits benefit corporations to specify one or more "specific public benefits."[459] "General public benefit" is defined as a "material positive impact on society and the environment," measured "against a third-party standard, from the business and

---

[444] *See generally* CAL. CORP. CODE §§ 14600–14631 (West 2012).

[445] *See generally* HAW. REV. STAT. §§ 420D-1 to -13 (2012). Hawaii's statute uses the term "sustainable business corporation" instead of the "benefit corporation." *Id.* § 420D-2. Unlike the other emerging corporate entities discussed in Parts III.B and III.C, above, however, this appears to be a distinction without a difference.

[446] S.B. 2897, 97th Gen. Assemb., Reg. Sess. (Ill. 2012) (effective Jan. 1, 2013).

[447] *See generally* Benefit Corporations, LA. REV. STAT. ANN. §§ 12:1801–1832 (2012).

[448] *See generally* MD. CODE ANN., CORPS. & ASS'NS §§ 5-6C-01 to 5-6C-08 (LexisNexis 2012).

[449] MASS. GEN. LAWS ch. 238, § 52 (2012).

[450] N.J. STAT. ANN. §§ 14A:18-1 to -11 (West 2012).

[451] N.Y. BUS. CORP. LAW §§ 1701–1709 (McKinney 2012).

[452] 15 PA. CONS. STAT. § 3301–3331 (2012).

[453] *See* H. 4766, 119th Leg., Reg. Sess. (2012) (amending Title 33 of the 1976 Code by adding Chapter 38, entitled "South Carolina Benefit Corporation Act").

[454] *See generally* VT. STAT. ANN. tit. 11A, §§ 21.01–21.14 (2012).

[455] *See generally* VA. CODE ANN. §§ 13.1-782 to -791 (2012).

[456] D.C. CODE § 29-1301 to -1304 (2013). The District of Columbia approved Bill No. B19-584 in December 2012 and the bill was sent to the Mayor. The Mayoral Review End Date is February 11, 2013, at which point the bill is subject to the thirty-day period of Congressional review as provided by the District of Columbia Home Rule Act, D.C. CODE § 1-206.02(c)(1) (2012). Thus, the tentative effective date of the D.C. Benefit Corporation Act of 2011 is March 13, 2013. *See Legislation*, COUNCIL OF THE DISTRICT OF COLUMBIA, http://dcclims1.dccouncil.us/lims/searchbylegislation.aspx (last visited Mar. 23, 2013).

[457] *See, e.g.*, CAL. CORP. CODE §§ 14600–14631 (West 2012).

[458] *See, e.g.*, N.J. STAT. ANN. § 14A:18-5(a) (West 2012).

[459] *Id.* § 14A:18-5(b).

operations of a benefit corporation."[460] While the exact meaning of this definition has not been addressed by the courts, a notable inclusion is the reference to a third-party standard, which attempts to address concerns regarding reporting accountability and methodology.

All benefit corporation statutes also define the term "specific public benefit" by listing the following examples:

> (1) Providing low-income or underserved individuals or communities with beneficial products or services;
> (2) Promoting economic opportunity for individuals or communities beyond the creation of jobs in the normal course of business;
> (3) Preserving or improving the environment;
> (4) Improving human health;
> (5) Promoting the arts, sciences, or advancement of knowledge;
> (6) Increasing the flow of capital to entities with a public benefit purpose; and
> (7) Conferring any other particular benefit on society or the environment.[461]

These examples provide much-needed specificity to both directors and investors, and their wide range reflects the expansive American view of social enterprise. Indeed, each list ends with a catch-all provision[462] that encourages the innovation of new or more specific public benefits. More importantly, as William Clark and Elizabeth Babson note, in treating general and specific public benefits separately, the statutes ensure that benefit corporations "can pursue any specific mission, but that the company as a whole is also working toward general public benefit."[463]

The statutes also contain provisions designed to ensure benefit corporations retain their unique corporate purpose. For example, the Vermont statute requires that the board of directors provide a statement of reasons why it is proposing a merger or sale in which the surviving corporation is not a benefit corporation.[464] Furthermore, many statutes require that a merger or sale must be approved by, at minimum, a two-thirds vote, or a greater voting

---

[460] N.Y. BUS. CORP. LAW § 1702(b) (McKinney 2012). Note, however, that the definition of "general public benefit" contained in the New Jersey statute does not include a reference to a "third-party standard," although it does require that the annual benefit report be prepared in accordance with a third-party standard. *See* N.J. STAT. ANN. § 14A:18-11(2).

[461] VA. CODE ANN. § 13.1-782 (2012). The Louisiana statute contains slightly different language regarding specific environmental benefits, to wit: "[p]reserving the environment, promoting positive impacts on the environment, or reducing negative impacts on the environment." Benefit Corporations, LA. REV. STAT. ANN. § 12:1803(A)(10)(c) (2012).

[462] *Id.* § 13.1-782(7).

[463] Clark & Babson, *supra* note 14, at 841 (noting that this ostensibly ensures that benefit corporations are not, for example, seeking to reduce waste while increasing carbon emissions).

[464] VT. STAT. ANN. tit. 11A, § 21.06(a)(1) (2012).

share as required by the articles of incorporation.[465] The same two-thirds voting requirement is also applicable to amendments to the corporate purposes contained in the articles of incorporation, even where the benefit corporation would retain its social enterprise status.[466] These provisions do not rise to the level of "asset locks," as it is still possible to overcome these protections and transfer a benefit corporation's assets to a for-profit organization. However, these heightened requirements may deter potential hostile takeovers or mergers that would separate a benefit corporation's assets from its stated social or environmental purposes.

b. Accountability: The Duty to Consider Stakeholder Interests

All benefit corporation statutes also impose an additional duty on directors. In addition to the traditional duty to create value for shareholders, directors of benefit corporations are also under a duty to consider the effects of their business decisions upon stakeholder groups.[467] These stakeholders include the following:

> (2) The employees and workforce of the benefit corporations and its subsidiaries and suppliers;
> (3) The interests of customers of the benefit corporation as beneficiaries of the general or specific public benefit purposes of the benefit corporation;
> (4) Community and societal considerations, including those of any community in which offices or facilities of the benefit corporation or its subsidiaries or suppliers are located;
> (5) The local and global environment;
> (6) The short-term and long-term interests of the benefit corporation ...; and
> (7) The ability of the benefit corporation to accomplish its general, and any specific, public benefit purpose.[468]

While this list is instructive, it does not provide directors with any particular hierarchy by which to evaluate each of these interests.[469] In fact, most

[465] *Id.* § 21.06(a)(2).
[466] *See, e.g.*, CAL. CORP. CODE § 14610(d) (West 2012).
[467] *See, e.g.*, *id.* § 14620(b).
[468] CAL. CORP. CODE § 14620(b)(2)–(7). Note however that the Hawaii statute only requires that directors consider the effects of any action on the shareholders and the "accomplishment of general and specific public benefits" of the sustainable business corporation, and gives directors the discretion for, but does not require, consideration of the six groups of stakeholder interest. *See* HAW. REV. STAT. § 420D-6(1)(2)(A)–(H) (2012). Additionally, the phrase "the short-term and long-term interests of the benefit corporation" is not included among the list in the Maryland statute. *See* MD. CODE ANN., CORPS. & ASS'NS § 5-6C-07 (LexisNexis 2012).
[469] This has been criticized by some commentators as inviting conflicts and confusion as to how directors should make business decisions. *See* Cummings, *supra* note 26, at 606.

benefit corporation statutes explicitly provide that directors are not required to give priority to any particular group over any other, unless otherwise stated in the articles of incorporation,[470] leaving directors a large degree of flexibility in this respect. Additionally, directors of benefit corporations are shielded from liability to the stakeholders whose interests they are obliged to consider. Most benefit corporation statutes provide that directors have no fiduciary duties to stakeholders, and in this regard they are similar to those of the aforementioned FPC and SPC.[471] However, shareholders of benefit corporations are given an expanded right of action to enforce this additional duty to consider stakeholder interests.[472]

Thus, the benefit corporation relies on shareholders to act as proxies for stakeholder groups to ensure compliance with the stated social and environmental purposes of the organization.[473] Additionally, the statutes permit benefit corporations to privilege one or more specific public benefits above others,[474] and to grant specific stakeholder groups with a right of action designed to ensure that the directors fulfill their duty to consider stakeholder interests.

c. Transparency: The Annual Benefit Report

The third fundamental element of benefit corporation statutes is the annual benefit report (ABR). In all states, benefit corporations are required to submit an ABR to each shareholder[475] and, in most cases, to make the

---

[470] *See, e.g.*, CAL. CORP. CODE § 14620(d); N.Y. BUS. CORP. LAW § 1707(a)(3) (McKinney 2012).

[471] *See, e.g.*, N.Y. BUS. CORP. LAW § 1707(c); VT. STAT. ANN. tit. 11A, § 21.09(e) (2012).

[472] *See, e.g.*, VT. STAT. ANN. tit. 11A, § 21.13 (giving shareholders a right of action to pursue benefit enforcement proceedings, including claims that directors violated their statutory standard of conduct, which includes giving sufficient consideration to stakeholder interests).

[473] Robert A. Wexler & David A. Levitt, *Using New Hybrid Legal Forms: Three Case Studies, Four Important Questions, and a Bunch of Analysis*, 69 EXEMPT ORG. TAX REV. 64, 70 (2012), http://www.adlercolvin.com/pdf/hybrid.pdf ("[A]n alternative corporate form makes sense if the founders want the corporation's board to be free to consider, on a regular and unlimited basis, a social or charitable mission, without concern about failure to maximize profits.").

[474] *See* J. Haskell Murray, *Choose Your Own Master: Social Enterprise, Certifications and Benefit Corporation Statutes*, 2 AM. U. BUS. L. REV. (forthcoming 2013) (manuscript at 30), *available at* https://papers.ssrn.com/sol3/Delivery.cfm/SSRN_ID2115548_code1725837.pdf?abstractid=2085000&mirid=1 (noting however, that directors may not pursue a special purpose at the expense of the general public purpose).

[475] *See* CAL. CORP. CODE § 14630; HAW. REV. STAT. § 420D-11 (2012); N.J. STAT. ANN. § 14A:18-11 (West 2012); N.Y. BUS. CORP. LAW § 1708; MD. CODE ANN., CORPS. & ASS'NS § 5-6C-08 (LexisNexis 2012); VA. CODE ANN. § 13.1-791 (2012); VT. STAT. ANN. tit. 11A, § 21.14.

most recent ABR publicly available on its website.[476] The ABR must be measured against some independent, third party standard[477] chosen by the board. In general, ABRs must include a narrative description of: (1) the ways in which the benefit corporation pursued both its general and any specific public benefits during the year, (2) any circumstances that have hindered the creation of general or specific public benefits, and (3) an assessment of the social and environmental performance of the benefit corporation.[478]

The independent standard plays an important role in adding legitimacy to the benefit corporation's stated purposes. The drafters took great care to define "third party standard" to prevent the inherent conflict of interests that arise when corporations promulgate their own standards or use malleable industry-friendly standards. The New York statute uses the most common definition of "third-party standard," to wit:

> [A] recognized standard for defining, reporting and assessing general public benefit that is:
> (1) developed by a person that is independent of the benefit corporation; and
> (2) transparent because the following information about the standard is publicly available:
> (A) the factors considered when measuring the performance of a business;
> (B) the relative weightings of those factors; and
> (C) the identity of the persons who developed and control changes to the standard and the process by which those changes are made.[479]

Thus, the third-party standard requirement goes to great lengths to ensure that the standard-setters are truly independent of the benefit corporation and its interests.

However, some commentators have criticized this approach, emphasizing that the statutes lack verification requirements and rely on self-reporting.[480] Some have argued that this "presents a clear opportunity for selective reporting, if not outright misconduct."[481] Steven Munch suggests that future legislation should outline specific penalties for directors who "provide false

---

[476] *See, e.g.*, N.J. STAT. ANN. § 14A:18-11(c); VA. CODE ANN. § 13.1-791(C).

[477] *See supra* note 460 and accompanying text.

[478] *See, e.g.*, MD. CODE ANN., CORPS. & ASS'NS § 5-6C-08(a).

[479] N.Y. BUS. CORP. LAW § 1702(g). The statutes in Vermont, Virginia, Maryland, and New Jersey contain the same definition.

[480] Gupta, *supra* note 366, at 224 (questioning whether the third-party evaluations are rigorous enough and whether self-evaluations pose risks of dishonest reporting); *see also* Cummings, *supra* note 26, at 580, 611–13. The Vermont statute stands alone in vesting benefit directors with the authority to retain an independent third party to audit the annual benefit report or conduct social and environmental performance assessments. VT. STAT. ANN. tit. 11A, § 21.10(c)(2).

[481] Munch, *supra* note 78, at 194.

or misleading information on the company's social performance."[482] William H. Clark, Jr., one of the drafters of benefit corporation legislation, counters with several reasons for not mandating verification of ABRs. First, he notes that doing so would impose additional costs on benefit corporations.[483] Second, he argues that for-profit corporations are not required to have audited financial reports, and by analogy, benefit corporations should not be required to have audited ABRs.[484] Clark addresses Munch's concerns by noting that directors of benefit corporations are already subject to suit for fraud if they report false or misleading information in their benefit reports.[485] He also argues that discretionary verification should remain available to certain benefit corporations who wish to distinguish themselves and attract greater confidence in their social and environmental claims.[486]

Clark offers persuasive arguments against mandatory verification, but that is not the only critique leveled at benefit corporations' reporting requirements. For instance, the statutes do not provide any baseline for social or environmental performance, nor do they prescribe any particular methodology or require a specific valuation metric against which a benefit corporation's social and environmental performance should be assessed. Clark responds by noting that unlike financial metrics, reliable industry standards for measuring social and environmental performance do not exist, but "[p]resumably, armed with the information included in the annual benefit report and the statutory requirements with respect to a third-party standard, market forces will shape the landscape of third-party standards utilized by benefit corporations."[487] Although this approach stands in stark contrast to CR reporting, the effectiveness of this particular mixture of third-party standards without verification or baselines remains to be seen.

d. Variations in the Statutes

In his dissenting opinion in *New State Ice Co. v. Liebmann*,[488] Justice Louis Brandeis famously observed that "[i]t is one of the happy incidents of the federal system that a single courageous State may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country."[489] Legislatures in several states have served as

---

[482] *Id.*
[483] Clark & Babson, *supra* note 14, at 846.
[484] *Id.* at 847.
[485] *Id.*
[486] *Id.*
[487] *Id.* at 846.
[488] 285 U.S. 262, 280 (1932) (Brandeis, J., dissenting).
[489] *Id.* at 311.

laboratories for benefit corporation legislation, and it comes as no surprise that states continue to build upon previous legislation by introducing unique provisions for their respective corporate codes. In an effort to provide a deeper understanding of this quickly developing legal landscape, this Section identifies several variations and unique features of benefit corporation statutes.

The Benefit Director. Eight states—Hawaii, Illinois, Louisiana, New Jersey, Massachusetts, Pennsylvania, South Carolina, and Vermont—and the District of Columbia have adopted the requirement that benefit corporations designate an independent "benefit director" to sit on the board.[490] These provisions largely mirror each other.[491] In general, the benefit director has all the "powers, duties, rights, and immunities of the other directors of the benefit corporation,"[492] and is elected and may be removed by the same procedures applicable to other directors.[493] The benefit director's primary responsibility is preparing the ABR.[494] All nine jurisdictions require benefit directors to include statements in the ABR addressing whether the benefit corporation fulfilled its general and specific goals, whether the directors and officers acted in accordance with their duty to consider stakeholder interests, and, if the benefit corporation failed in either of these two respects, a description of those failures.[495] Much like the other directors, benefit directors are shielded from personal liability "for any act or omission taken in his or her official capacity."[496]

Benefit Officers. The same nine jurisdictions also permit the selection of a "benefit officer."[497] Unlike benefit directors, however, the selection of a

[490] *See* HAW. REV. STAT. § 420D-7 (2012); LA. REV. STAT. ANN. § 12:1822(A) (2012); N.J. STAT. ANN. § 14A:18-7 (West 2012); S.C. CODE ANN. § 33-38-410(A) (2012); VT. STAT. ANN. tit. 11A, § 21.10 (2012).

[491] *See, e.g.*, HAW. REV. STAT. § 420D-7; D.C. CODE § 29-1303.2 (2013).

[492] *See, e.g.*, LA. REV. STAT. ANN. § 12:1822.

[493] *See* HAW. REV. STAT. § 420D-7(b); LA. REV. STAT. ANN. § 12:1822(B); N.J. STAT. ANN. § 14A:18-7(b); S.C. CODE ANN. § 33-38-410(A); VT. STAT. ANN. tit. 11A, § 21.10(b).

[494] *See* HAW. REV. STAT. § 420D-7(c); LA. REV. STAT. ANN. § 12:1822(C); N.J. STAT. ANN. § 14A:18-7; S.C. CODE ANN. § 33-38-410(C); VT. STAT. ANN. tit. 11A, § 21.10(c)(1).

[495] *See, e.g.*, N.J. STAT. ANN. § 14A:18-7(c); VT. STAT. ANN. tit. 11A, § 21.10(c)(3)–(4).

[496] *See, e.g.*, N.J. STAT. ANN. § 14A:18-7(e); VT. STAT. ANN. tit. 11A, § 21.10(f). These statutes contain the usual exceptions for "intentional misconduct," "a knowing violation of [the] law," and "self-dealing." N.J. STAT. ANN. § 14A:18-7(e); VT. STAT. ANN. tit. 11A, § 21.10(f); S.B. 2897, 97th Gen. Assemb., Reg. Sess. (Ill. 2012) (effective Jan. 1, 2013); MASS. GEN. LAWS ch. 238, § 52.11(a) (2012); 15 PA. CONS. STAT. § 3322(a) (2012).

[497] HAW. REV. STAT. § 420D-9(a); LA. REV. STAT. ANN. § 12:1824(A); N.J. STAT. ANN. § 14A:18-9; S.C. CODE ANN. § 33-38-430(A); VT. STAT. ANN. tit. 11A, § 21.12; S.B. 2897, 97th Gen. Assemb., Reg. Sess. (Ill. 2012) (effective Jan. 1, 2013); MASS. GEN. LAWS ch. 238, § 52.11(a); 15 PA. CONS. STAT. § 3322(a).

benefit officer is left to the board's discretion.[498] Benefit corporations may have an independent benefit officer specifically charged with the management of the benefit corporation relating to the creation of the general or specific public benefits.[499] In almost all cases, when a benefit officer is selected, he or she bears the statutory responsibility for preparing the ABR.[500]

The California and Virginia statutes do not expressly authorize the benefit officer position. However, in most cases,[501] regardless of designation, officers of benefit corporations enjoy the same duties, rights, privileges, and immunities as directors. For example, the Virginia statute contains a general provision stating that officers "shall have no liability" for actions taken that the officer believes, in his "good faith business judgment," agree with the general or specific public benefits of the corporation and are consistent with any third-party standards then in effect.[502] Other states, like California, Vermont, and New Jersey, include more detailed officer liability provisions. These states require each officer of a benefit corporation to consider both shareholder and stakeholder interests when (1) "[t]he officer has discretion to act with respect to a matter" or (2) it reasonably appears that the matter "may have a material effect" on the creation of general or specific public benefits or any stakeholder interests.[503] Thus officers, as well as directors, are under an additional duty to consider stakeholder interests, but they are shielded from liability in decision-making circumstances.[504]

---

[498] *See, e.g.*, VT. STAT. ANN. tit. 11A, § 21.12 ("A benefit corporation *may* have an officer designated the 'benefit officer' ...." (emphasis added)).

[499] *See, e.g.*, HAW. REV. STAT. § 420D-9(a)–(b).

[500] *See id.*; LA. REV. STAT. ANN. § 12:1824(B)(2); N.J. STAT. ANN. § 14A:18-9; S.C. CODE ANN. § 33-38-430(B)(3).

[501] The Maryland statute does not acknowledge or address the issue of officers of benefit corporations.

[502] VA. CODE ANN. § 13.1-789 (2012). One might term this approach the "third-party business judgment" standard insofar as its conjunctive language appears to cloak officers' decisions under the veil of the business judgment rule, so long as those decisions are consistent with third-party standards. *Id.* ("An officer of a benefit corporation shall have no liability for actions [that] ... are consistent with (i) the general public benefit ... *and* (ii) the requirements of any third-party standard then in effect.") (emphasis added)).

[503] CAL. CORP. CODE § 14622(a)(1)–(2) (West 2012); N.J. STAT. ANN. § 14A:18-8(a)–(b); VT. STAT. ANN. tit. 11A, § 21.11.

[504] CAL. CORP. CODE § 14622(b) (providing that an officer's consideration of stakeholder interests shall not constitute a violation of the officer's duties); *id.* § 14622(c) (shielding officers from liability for money damages for any action taken under this section or failure to create a general or specific public benefit); *id.* § 14622(d) (explicitly denying a right of action to stakeholders or beneficiaries of the public benefits against officers of benefit corporations).

The Benefit Enforcement Proceeding. Nine states—California, Louisiana, Illinois, Massachusetts, New Jersey, Pennsylvania, South Carolina, Virginia, and Vermont—and the District of Columbia provide for a special right of action against benefit corporations—namely, a benefit enforcement proceeding (BEP).[505] A BEP is a limited right of action available to shareholders, directors, or any other persons that may be specified in the articles of incorporation.[506] In most cases, standing to bring a BEP is also granted to persons or groups who own at least 5%[507] of the equity interest in a benefit corporation's parent corporation.[508] In most states, BEPs are limited to claims against directors or officers for failure to pursue the general or specific public benefit purpose of the corporation or violation of a duty or standard of conduct.[509] California adds "failure of the benefit corporation to deliver or post an annual benefit report as required by Section 14630" to this list of preapproved BEP claims.[510]

The New York and Maryland statutes do not create any special right of action against benefit corporations. While these statutes fail to mention BEPs, benefit corporations incorporated in these jurisdictions are still subject to the provisions of their respective corporate codes.[511] Therefore, shareholders have standing to bring derivative suits alleging breach of fiduciary duties or violations of standards of conduct.[512] Because directors of benefit corporations are under an additional duty to consider stakeholder interests, shareholders

---

[505] CAL. CORP. CODE § 14623; LA. REV. STAT. ANN. § 12:1825(B); N.J. STAT. ANN. § 14A:18-10(b); S.C. CODE ANN. § 33-38-440(C) (2012); VT. STAT. ANN. tit. 11A, § 21.13(b); S.B. 2897, 97th Gen. Assemb., Reg. Sess. (Ill. 2012) (effective Jan. 1, 2013); MASS. GEN. LAWS ch. 238, § 52.11(a) (2012); 15 PA. CONS. STAT. § 3322(a) (2012).

[506] *See, e.g.*, N.J. STAT. ANN. § 14A:18-10(b)(2)(a) to (b)(2)(d); VT. STAT. ANN. tit. 11A, § 21.13(b)(1)–(4).

[507] *Compare* N.J. STAT. ANN. § 14A:18-10(b)(2)(c), *and* VT. STAT. ANN. tit. 11A, § 21.13(b)(3), *with* CAL. CORP. CODE § 14623(b)(2)(C), *and* S.C. CODE ANN. § 33-38-440(C)(2)(c). The former require a 10% equity interest in the parent corporation, while the latter require only a 5% interest to trigger the right to a BEP.

[508] *See, e.g.*, N.J. STAT. ANN. § 14A:18-10(b)(2)(c); VT. STAT. ANN. tit. 11A, § 21.13(b)(3).

[509] *See, e.g.*, N.J. STAT. ANN. § 14A:18-1; VA. CODE ANN. § 13.1-782 (2012); VT. STAT. ANN. tit. 11A, § 21.13(c).

[510] CAL. CORP. CODE § 14601(b)(3). Hawaii's statute is less clear. It does not set forth any special right of action against Benefit Corporations, but rather provides in general terms that shareholders and directors have the right to bring derivative claims "to enforce corporate purposes and the standards for directors ... [and] to enforce the general or specific public benefit purposes" of the corporation. HAW. REV. STAT. § 420D-10 (2012). Thus, while not explicitly providing for a BEP, the Hawaii statute appears to infer the existence of a limited right of action available only to directors and shareholders.

[511] *See, e.g.*, MD. CODE ANN., CORPS. & ASS'NS § 5-6C-02 (LexisNexis 2012); N.Y. BUS. CORP. LAW § 1701 (McKinney 2012).

[512] *See, e.g.*, MD. CODE ANN., CORPS. & ASS'NS § 2-405.1; N.Y. BUS. CORP. LAW § 720.

in states that do not provide for a special right of action vis-à-vis a BEP may still pursue a traditional derivative action alleging a violation of that duty.[513]

Public Comment. The public comment requirement is unique to the Hawaiian statute. Before publishing its final ABR, a Hawaiian "sustainable business corporation" is required to "post a draft of its benefit report on the public section of its website, or make it otherwise available to the public, for a sixty-day public comment period."[514] Directors of benefit corporations are required to consider stakeholder interests in business decisions, but only those incorporated under the laws of Hawaii are required to include stakeholders and the general public in the drafting of the ABR.

Forfeiture of Social Enterprise Corporate Status. The potential forfeiture of benefit corporation status is a feature unique to the New Jersey statute. Benefit corporations registered in New Jersey are required to submit a copy of their ABR, along with a $70.00 filing fee, to the Department of the Treasury on an annual basis.[515] In the event a benefit corporation fails to file an ABR for two consecutive years,[516] the Department of the Treasury is granted the authority to file a statement that the benefit corporation has forfeited its status and is no longer subject to the act.[517] However, the forfeiture can be remedied by filing an ABR with the Department of the Treasury, triggering automatic reinstatement of benefit corporation status.[518] Nevertheless, potential loss of operating power and benefit corporation status pose significant deterrents to potential violators.

F. Conclusion

The four new entities discussed in this Part constitute the first generation of entities in the social enterprise revolution in U.S. corporate law. They remain, by and large, untested corporate forms with high aspirations and varying approaches to finding an effective blend of corporate purposes. The success of the L3C may depend in large part on the effectiveness of the recently proposed IRS regulations to allay tax risks with respect to PRIs. The FPC offers the interesting option of serving either charitable or

---

[513] Clark & Babson, *supra* note 14, at 850 (emphasizing that while BEPs grant shareholders an expanded right of action, the duty to consider stakeholder interests does not require a particular outcome of the directors' decision-making).

[514] HAW. REV. STAT. § 420D-11(b). Note, however, that the Hawaiian "sustainable business corporation," while bearing a different name than the benefit corporation, appears to be a distinction without a difference as the statute mirrors other benefit corporation statutes.

[515] N.J. STAT. ANN. § 14A:18-11(d)(1) (West 2012).

[516] *Id.* § 14A:18-11(d)(2).

[517] *Id.*

[518] *Id.*

blended-value purposes, but vague drafting and unprecedented grants of limited liability may risk doing more harm than good to the social enterprise movement. The SPC, with its introduction of the anti-*Revlon* declaration, is a significant step away from shareholder wealth maximization. However, the lack of third-party standards for reporting requirements remains a legitimate accountability concern for the SPC form. Finally, there is the benefit corporation. It offers the most specific list of public benefits and a catch-all provision enabling entrepreneurs to pursue a limitless number of specific social and environmental benefits, while still requiring the overall pursuit of a general public benefit. Benefit directors and other officers enjoy limited liability, but they are under a duty to consider stakeholder interests when making business decisions, which is made enforceable through the BEP. All ABRs must meet minimum content requirements and must be assessed against independent, third-party standards measuring social and environmental performance.

In light of the above analysis, the benefit corporation emerges as the most promising corporate entity. On paper, it appears to combine an appropriate mixture of specifically defined social or environment corporate purposes, transparency, accountability, flexibility, and limited liability for social entrepreneurs.[519] This might explain why, on the morning of January 3, 2012, several CEOs, including Yvon Chouinard of Patagonia,[520] lined up outside the Secretary of State's office to file their reincorporation papers and become benefit corporations.[521] The next Part will first address some critiques

---

[519] *See* Clark & Babson, *supra* note 14, at 851 (concluding that the benefit corporation "is the most comprehensive, yet flexible legal entity devised to address the needs of entrepreneurs and investors, and ultimately, the general public").

[520] Marc Lifsher, *Firms File for Do-Good Status*, L.A. TIMES, Jan. 4, 2012, at B1, B4. Yvon Chouinard explained: "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." *Id.* at B4. Patagonia, already well known for its environmental commitments, was the first major company to adopt the benefit corporation form in California. *Firms with Benefits: A New Sort of Caring, Sharing Company Gathers Momentum*, ECONOMIST (Jan. 7, 2012), http://www.economist.com/node/21542432. Following Patagonia, Sun Light & Power and King Arthur Flour became benefit corporations, demonstrating the entity's adoption across industry lines. *See About Us*, SUN LIGHT & POWER, http://sunlightandpower.com/about/#136 (last visited Mar. 23, 2013); *see also About: Social Responsibility*, KING ARTHUR FLOUR, http://www.kingarthurflour.com/about/social-responsibility.html (last visited Mar. 23, 2013).

[521] Lifsher, *supra* note 522, at B1; *see also* Alex Goldmark, *Twelve California Companies Seize the Moment to Become Benefit Corporations*, GOOD (Jan. 3, 2012, 12:00 PM), http://www.good.is/post/eighteen-california-companies-seize-the-moment-to-become-benefit-corporations/.

of the benefit corporation, and then make the case for the benefit corporation as the most appropriate vehicle for the social enterprise movement.

IV. The Case for the Benefit Corporation

A. Responding to the "Social Business" Critique

Perhaps the most outspoken critic of blended value approaches to social enterprise is, surprisingly, Muhammad Yunus, the father of the microcredit industry. Yunus became a Nobel Peace Prize laureate in 2006 for his work advancing a "social business" model aimed at alleviating poverty.[522] He goes to great lengths to distinguish his term "social business" as a specific subset of the broader social enterprise movement.[523]

Yunus presents three arguments against the blended value approaches gaining momentum in the U.K. and the United States. First, Yunus makes a moral argument, contending that it is inherently immoral to make a profit from the poor, and that this constitutes "benefiting from the suffering of our fellow human beings."[524] Yunus uses examples from his experience in the microcredit arena[525] and, admittedly, within the confines of this limited context, his moral argument is very strong.

However, the argument fails to hold water when applied to social enterprises engaging in other social or environmental goals. Take, for example, Solar Works, a California benefit corporation that provides full-service solar panel design and installation.[526] Alternatively, consider Clay.com, a New York benefit corporation that provides a social marketplace of second-hand items that raises money for local communities.[527] Neither of these benefit corporations directly addresses poverty, but both still strive to achieve specific environmental or social benefits in their respective communities. These examples show how Yunus's definition of social business narrows its focus to traditionally charitable issues—namely, poverty—and reflects how social business is much more akin to European social cooperatives than American social enterprise entities.

---

[522] *The Nobel Peace Prize 2006*, NOBELPRIZE.ORG (Oct. 13, 2006), http://www.nobelprize.org/nobel_prizes/peace/laureates/2006/press.html.

[523] YUNUS, *supra* note 2, at 12 (emphasizing that social business is a "new category" of business).

[524] *Id.* at 13.

[525] *Id.* at 13–14.

[526] *See* SOLARWORKS, http://www.solarworksca.com (last visited Mar. 23, 2013).

[527] CLAY, http://www.clay.com (last visited Mar. 23, 2013).

Yunus also contends that "[i]n times of stress, profit will always trump the other 'bottom lines.'"[528] He argues that blended-value approaches create confusion for board members over how to balance those goals,[529] and that where confusion arises, profits will almost always win over social goals, which will "fade in importance."[530] In contrast, he explains that there is no balancing of contradictory objectives involved in a social business because every business decision is measured by whether it will enable the business "to provide the greatest possible benefit to society,"[531] and in this sense it is guided by its primarily charitable purpose.

Instead of avoiding tension between profit and purpose, most emerging entities invite this conflict with open arms and attempt to insulate those making holistic business decisions from personal liability.[532] This is a much different approach to Yunus's social business model, but the fact that these entities require consideration of non-shareholder interests is a significant step away from the single bottom-line, shareholder-centric model of corporate governance. Furthermore, Yunus's argument overlooks the possibility that certain entities, like benefit corporations, permit the founders to enshrine the primacy of one or more stakeholder interests above others, thus giving directors a more tangible yardstick by which to measure their decisions.

Lastly, Yunus makes a systemic argument, contending that social business is necessary to create "a clearly defined alternative ... in order to change mindsets, reshape economic structures, and encourage new forms of thinking."[533] This argument is compelling,[534] but the momentous economic restructuring it envisions will not occur overnight. It may be that the eventual success of Yunus's social business model is necessarily dependent on the organic development of smaller, incremental shifts towards stakeholder-inclusive governance models. The imposition of an enforceable duty to consider stakeholder interests, for example, represents a significant step in this direction. In this sense, blended value entities like the benefit corporation may represent stepping stones to Yunus's social business.[535]

---

[528] YUNUS, *supra* note 2, at 14 (arguing that in practice, CEOs tend to "lean—perhaps unconsciously—in favor of profit, and exaggerate the social benefits being created").

[529] *Id.* ("The idea of a 'mixed' company offers no clear guidance ....").

[530] *Id.*

[531] *Id.* at 15.

[532] Clark & Babson, *supra* note 14, at 840–41, 848–49.

[533] YUNUS, *supra* note 2, at 16.

[534] *Id.* ("Social business is about totally delinking from the old framework of business—not accommodating new objectives within the existing framework.").

[535] *Id.* at 1. ("[Type I social business] is a non-loss, non-dividend company devoted to solving a social problem and owned by investors who reinvest all profits in expanding and improving the business.").

B. The Valuation Problem

Some commentators highlight the problem of valuing a corporation's social and environmental impacts, observing that a failure to agree upon metrics for such impacts stifles the growth of investments in social enterprise.[536] These critiques continue to be made despite the fact that several organizations, in addition to B Labs, *infra*, have promulgated assessment tools.[537] For example: the Center for Sustainable Organization's (CSO) Social Footprint,[538] the Roberts Enterprise Development Fund's Ongoing Assessment of Social ImpactS (OASIS);[539] New Profit, Inc.'s Balance Scorecard;[540] the Social Return On Investment (SROI);[541] the ISO2600;[542] and, most prominently, the Global Reporting Initiative's (GRI) G3 Guidelines.[543]

This is an area in which the failures of CR reporting can creep into the new ground being broken by social enterprise entities. CSI's Social Footprint is one of the few assessment tools that attempts to provide a mathematical calculation of "anthro capital" to generate a value representing a social bottom line.[544] This is a promising development, but by no means a silver bullet. The reality is that the financial industry possesses myriad tools for measuring a company's financial value, but has only begun to explore different methods for valuing a corporation's social and environmental impacts and benefits. Social enterprise's biggest challenge will be to fashion new and innovative metrics for measuring social and environmental benefits.[545]

---

536 Snyder, *supra* note 103, at 586 ("There have been recent efforts to quantify social impact. Examination of such efforts affirms initial intuitions and illustrates that given the nature of the issues, the reports are inherently ambiguous.").

537 *See generally List of Standards*, BENEFIT CORP INFO. CENTER, http://benefitcorp.net/selecting-a-third-party-standard/list-of-standards (last visited Mar. 23, 2013).

538 *The Social Footprint Method*, CENTER FOR SUSTAINABLE ORGS., http://www.sustainableorganizations.org/the-social-footprint.html (last visited Mar. 23, 2013); *see also* Snyder, *supra* note 103, at 586.

539 *See generally* Fay Twersky & BTW Consultants, *An Information OASIS: The Design and Implementation of Comprehensive and Customized Client Information and Tracking Systems*, REDF (2002), http://www.redf.org/learn-from-redf/publications/121.

540 Rob Wherry, *The Matchmaker*, FORBES, Dec. 23, 2002, http://www.forbes.com/forbes/2002/1223/338_print.html ("The key to New Profit is its scorecard, which rates a nonprofit on a series of financial and other sorts of benchmarks.").

541 *See The SROI Guide*, THE SROI NETWORK, http://www.thesroinetwork.org/sroi-analysis/the-sroi-guide (last visited Mar. 23, 2013).

542 *See ISO 26000—Social Responsibility*, ISO (2010), http://www.iso.org/iso/iso_catalogue/management_and_leadership_standards/social_responsibility/iso26000.

543 *See G3 Guidelines*, GLOBAL REPORTING INITIATIVE, https://www.globalreporting.org/reporting/latest-guidelines/g3-guidelines/Pages/default.aspx (last visited Mar. 23, 2013); *see also* Snyder, *supra* note 103, at 586–91 (providing an overview of the GRI G3 Guidelines).

544 *The Social Footprint Method*, *supra* note 538; *see also* Snyder, *supra* note 103, at 592.

545 *See* Doeringer, *supra* note 254, at 323 (suggesting increasing investments in research and development of valuation metrics that accurately account for the impact of social enterprise).

C. Benefit Corporations Going Forward

This Article has argued that, in comparison to the other emerging corporate entities currently available to social entrepreneurs, the benefit corporation most effectively blends profit with social and environmental goals, and accountability with flexibility. But the benefit corporation's strongest competition going forward may not be the new entities discussed above, but rather[546] the already popular and notoriously flexible limited liability company (LLC).[547] Proponents of the LLC, like Anne E. Conaway, argue that the LLC can better accommodate the blended-value goals that benefit corporations seek to achieve.[548] They contend that the benefit corporation imposes additional costs in comparison to LLCs.[549] For example, in states that require independent benefit directors to sit on the board, the benefit corporation is obliged to search for and pay a salary to that individual.[550] Additionally, LLC proponents emphasize that benefit corporation statutes muddy the waters of fiduciary duties, and that a carefully tailored LLC agreement can more specifically delineate directors' fiduciary duties to an organization and its members.[551] Lastly, the LLC generally qualifies as a "pass through" entity for federal income tax purposes, whereas the benefit corporation offers no relief from the traditional corporate entity tax.[552]

These are perhaps the most compelling arguments against the benefit corporation, and addressing them substantively should be the polestar for future drafting and policy decisions. The following offers some suggestions in the hopes of sparking a conversation about the future of the benefit corporation and its role in the social enterprise movement.

1. Statutory Reform

There are several areas in which state legislatures can improve upon the first generation of statutes currently on the books. Lawmakers can require

---

[546] Thomas Earl Geu, *Understanding the Limited Liability Company: A Basic Comparative Primer (Part One)*, 37 S.D. L. REV. 44, 45 (1991) ("[The LLC] is a *hybrid form of business* created by combining the organizational and tax attributes of partnerships and corporations ...." (emphasis added)).

[547] Anne E. Conaway, *The Global Use of the Delaware Limited Liability Company for Socially-Driven Purposes*, 38 WM. MITCHELL L. REV. 772, 780 (2012) ("The thesis of this article is that, presently, the Delaware LLC provides global investors maximum internal efficiency, as well as asset protection at a decreased agency cost, for businesses operating solely within or outside the United States for socially-driven purposes.").

[548] *Id.* at 801.

[549] Reiser, *supra* note 17, at 608.

[550] *See* N.J. STAT. ANN. § 14A:18-7 (West 2012); VT. STAT. ANN. tit. 11A, § 21.10 (2012).

[551] *See* Conaway, *supra* note 547, at 801–02, 816.

[552] *See* Geu, *supra* note 546, at 45.

that the independent, third-party reporting standard produce some metric for measuring an organization's social and environmental impacts. Permitting benefit corporations to select third-party standards such as the GRI Guidelines or other standards that lack qualitative methodology does nothing more than require what 95% of the world's largest corporations already engage in—public relations moonlighting as corporate social responsibility. If states are willing to hand over the enforcement reins to third-party standard setters, they should at minimum require that those standards use some objective calculus to give numerical values to a benefit corporation's social and environmental benefits. Doing so would produce two results for benefit corporations: first, it would effectively address methodological shortcomings of CR reporting; second, it would prevent a race to the bottom amongst third-party standard setters. Most important, it would encourage the creation of new valuation metrics and force those already engaged in standard setting to pursue more robust methodologies. Once acceptable methodologies are in place, lawmakers might set minimum requirements for social and environmental performance that benefit corporations must meet in order to maintain their corporate status.

To the extent that lawmakers are uncomfortable with turning over the lion's share of regulatory authority to independent third parties, they might also consider adopting a public participation provision like that in the Hawaiian statute. Costs associated with permitting public comment are marginal, and yet this simple step opens a dialogue between communities served by benefit corporations, and it may strengthen ties with stakeholder groups whose interests benefit corporations are under a duty to consider. While requiring a period for public comment may provide another layer of enforcement, the effectiveness of this approach relies on the ABR being assessed against objective third-party standards in the first place.

New Jersey's forfeiture of social enterprise status provision[553] offers additional regulation of the ABR. However, this approach requires a greater degree of government oversight and involvement than other benefit corporation statutes that leave enforcement to the shareholders by way of the BEP.[554] Theoretically, the threat of derivative suits for failure to prepare an ABR is sufficient to ensure that such reports are distributed and made public. However, to prevent unscrupulous business practices that seek to use the good will of the benefit corporation brand to defraud consumers, a simple forfeiture of status provision may provide a necessary regulatory floor.

The author suggests that future benefit corporation statutes adopt an element of the SPC statute—namely, the anti-*Revlon* "mission statement"

[553] N.J. STAT. ANN. § 14A:18-11(d)(1).
[554] *See, e.g.*, VA. CODE ANN. § 13.1-782 (2012).

providing: "The mission of this social purpose corporation *is not necessarily compatible with and may be contrary to maximizing profits and earnings for shareholders*, or maximizing shareholder value in any sale, merger, acquisition, or other similar actions of the corporation," to supplement the benefit corporation's purpose of "creating a general public benefit," and to make clear that—in all business decisions—directors are free to choose not to maximize profits.

Finally, some commentators have suggested that requiring only one benefit director on the board is insufficient, particularly in larger organizations.[555] Steven Munch suggests that future legislation "require benefit corporations to enlist additional benefit directors as they grow and, once they reach a certain size, to organize full benefit committees as part of their boards."[556]

2. Tax Credits

Another method to foster the growth of benefit corporations, and social enterprise in general, is to provide tax credits for these organizations. As several commentators have pointed out, benefit corporations and other social enterprise entities receive no preferential tax treatment,[557] and they argue that tax credits offer a practical counterweight to the added burden borne by the entities' commitment to socially and environmental responsible business practices.[558] Because benefit corporation directors are given the discretion to de-prioritize shareholder wealth maximization, they may very well reap a lower return on investment.[559] Tax credits could prove especially helpful for start-ups seeking seed-stage funding.

Some local jurisdictions have already enacted such tax credits. The city of Philadelphia recently introduced a Sustainable Business Tax Credit, effective through 2017.[560] Certified B Corporations located in Philadelphia are eligible

---

[555] Munch, *supra* note 78, at 193.

[556] *Id.*

[557] *See, e.g.*, Ajulo Othow, *Benefits Corporations: A New Way to Balance Values and Profits*, RAPPAPORT BRIEFING (Sept. 8, 2012), http://rappaportbriefing.net/2012/09/08/benefits-corporations-a-new-way-to-balance-values-and-profits/ ("Benefits [sic] corporations also differ from non-profit organizations whose operators and donors rely on significant tax advantages to encourage giving to fund their programs. Benefits corporations have no such tax advantages; they must instead maintain a viable *for*-profit model to stay in business.").

[558] *See* Munch, *supra* note 78, at 188 (noting that this approach has caused mixed reactions in the United States).

[559] *See id.*

[560] City of Philadelphia Bus. Servs., *Credits, Grants, & Other Incentives*, CITY OF PHILADELPHIA, https://business.phila.gov/pages/taxcreditsotherincentives.aspx (last visited Mar. 23, 2013). There have also been rumors that Portland, Oregon, and Washington, D.C., will grant tax breaks to certified B Corporations; *see also* Gupta, *supra* note 366, at 225.

to be classified as sustainable businesses and receive a tax credit of $4000.[561] Other government incentives for benefit corporations are also being proposed. For example, in San Francisco, Bill No. 120082 would amend the San Francisco Administrative Code to give California benefit corporations additional points in the system the city uses for bidding contracts.[562] While prospects of federal tax relief for benefit corporations remain uncertain, state and local governments can take steps to foster social enterprise in their areas by adopting tax credits or preferred government contract status.

CONCLUSION

This Article has illustrated the effects of the global social enterprise movement on corporate law in Europe and the United States. In doing so, the Article has drawn a stark contrast between the European and American approaches, and it has emphasized that the emerging entities associated with these approaches lie along a surprisingly broad spectrum, from social cooperatives that operate like traditional charities to for-profit FPC's with unprecedented protection for directors and their business judgment. The Article argues that the benefit corporation is the most promising entity for social entrepreneurs. While benefit corporations may be the most desirable of this first generation of social enterprises, whether they provide sufficient benefits to overcome the strong preference for LLCs remains debatable. Likewise, the uncertainty surrounding the ability of third-party standards to prevent selective reporting and foster accurate valuation metrics for social and environmental performance continues to impede progress.

Despite these problems, one cannot overlook the consistent growth in investments in social enterprise. Increased financial support and the continued experimentation with a growing list of entities designed specifically for social entrepreneurs are necessary for continued progress. Indeed, these trends should give social entrepreneurs reason to hope for a future that includes a thriving economic sector offering accurate valuation metrics and efficient corporate entities that allow business to be used as a tool for social and environmental good.

---

[561] City of Philadelphia Business Services, *supra* note 560. However, no more than twenty-five sustainable businesses may receive the tax credit in any one tax year. *Id.*

[562] Mark Hrywna, *Benefit Corporations in California Meets Chill in San Francisco*, NONPROFIT TIMES (Mar. 23, 2012), http://www.thenonprofittimes.com/article/detail/benefit-corporation-in-california-meets-chill-in-san-francisco-4497.