New Corporate Forms and Green Business

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ABSTRACT

You want to start a business: not just an ordinary business, producing ordinary social benefit, but a dual-mission business that will both make a profit and benefit the environment. This green business, you expect, will sometimes face trade-offs between the missions, in the sense that sometimes owners’ wealth and profit will have to be sacrificed to pursue environmental benefits. You’re optimistic, in that you hope the business will find outside investors and will scale up easily. Moreover, you don’t want to lie or even dissemble about your motives or about the business’s actions. You want to be both authentic and transparent. This Article looks at whether and how law, by means of recently enacted corporate organizational forms—benefit corporations, flexible purpose corporations and social purpose corporations—can help.

INTRODUCTION

Maryland started the trend with its enactment of the benefit corporation in April 2010.1 The bill received overwhelming support: unanimous in the Senate and 135–5 in the House.2 It was modeled on an initiative from B Lab, a Pennsylvania-based non-profit that had already pioneered a private certification program, the B Corporation,3 for socially

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2 Id.
3 Id. A certified B Corporation is any organization, including LLCs or traditional corporations, that has been “certified by the non[-]profit B Lab to meet rigorous standards of social and environmental performance, accountability, and transparency.” What Are B Corps?, CERTIFIED B CORPORATION, http://www.bcorporation.net/what-are-b-corps (last visited Jan. 31, 2013). It is like a good housekeeping seal of approval, rather than an
oriented companies. The passage of the new form was hailed by B Lab co-founder Jay Coen Gilbert as nothing short of “an inflection point in the evolution of capitalism,” and by Maryland Senator Jamie Raskin as “a great moment in evolution of commercial life in Maryland and America.”

Since then, California (January 1, 2012), Hawaii (July 8, 2011), Illinois (January 1, 2013), Massachusetts (January 1, 2013), Louisiana (August 1, 2012), New Jersey (March 1, 2011), New York (February 10, 2012), South Carolina (June 14, 2012), Vermont (July 1, 2011) and Virginia (July 1, 2011) have enacted similar forms, mostly with overwhelming bipartisan support. California has also introduced the flexible purpose corporation, which relaxes some of the statutory requirements of the benefit corporation. According to some, this form, rather than the benefit corporation, is better suited for larger publicly traded corporations that would prefer a more legally unassailable social mission. Washington State has followed this lead, with its similar social purpose corporation.

The purpose of these new kinds of corporations is to provide an organizational home, or legal architecture, suitable for hybrid, or dual-mission, businesses. These businesses are intended both to make a

See id. (claiming to be “to sustainable business what Fair Trade certification is to coffee or USDA Organic certification is to milk.”).


5 Id.


10 These legislative attempts are not the first modifications to the corporate form intended to assist dual-mission businesses. Oregon, for example, passed an amendment to its corporate code providing that a corporation’s articles could include a “provision authorizing or directing the corporation to conduct the business of the corporation in a manner that is environmentally and socially responsible.” OR. REV. STAT. ANN. § 60.047(2)(e) (West 2012). The goals were apparently “to both recruit new green businesses to Oregon and encourage existing Oregon businesses to improve the sustainability of their operations.”
profit and to create a benefit for society above and beyond what a traditional business creates,” without the problems that are perceived with either the traditional corporate form or the non-profit form. As the California assemblyman who authored his state’s legislation said, “Benefit corporations offer for-profit companies a way to do well and do right. . . . There is a way to create jobs and grow the economy while raising the bar for social and environmental responsibility.”

So far the list of benefit corporations is relatively small. Perhaps not surprisingly given that it is a relatively new form, the only ones that people are likely to recognize are the clothing manufacturer Patagonia, Inc., and perhaps Greyston Bakery, which was made famous by Ben & Jerry’s. Both became benefit corporations as soon as the form was available in their respective states, and they were the first to register. Greyston Bakery’s CEO observed, “benefit corporations are using the power of business to solve social and environmental issues and it is our goal at Greyston to set an example for other social enterprises as we embrace our new corporate status.”


Amidst all the hype it is worth analyzing how these new corporate forms might function for green businesses, those organizations that are taking voluntary actions intended to better environmental performance.\textsuperscript{18} Are they really a step forward, and if so, is the benefit or flexible purpose model likely to prove better?

This Article proceeds as follows: Part I briefly examines the perceived problems with existing forms, both for-profit and non-profit. Part II analyzes the hybrid answer for green business. Specifically, it focuses on benefit corporations and the recently enacted flexible purpose corporations. It notes the strengths and weaknesses of each form for green businesses. The Conclusion recognizes the limited role for organizational law.

I. PERCEIVED AND ACTUAL PROBLEMS OF EXISTING FORMS

Would-be founders of hybrid businesses, or social enterprise, have traditionally had the choice of non-profit or for-profit organizations. Both are perceived as having weaknesses.

Corporations. There is an ongoing debate regarding whether the traditional corporate form is suitable for double bottom line companies, including those that pursue green goals.\textsuperscript{19} Opponents of the traditional

\textsuperscript{18} Green business can be defined in several different ways. This definition is drawn from Dennis D. Hirsch, \textit{Green Business and the Importance of Reflexive Law: What Michael Porter Didn’t Say}, 62 ADMIN. L. REV. 1063, 1063 (2010). Hirsch identifies nine categories of “green business behavior.” \textit{Id.} at 1072. Hirsch explains claiming that:

[w]hen firms go \textit{green}, they exceed legal requirements by: (1) directly reducing their own regulated—or unregulated—environmental impacts in ways that will reduce regulatory risk, improve company brand, and allow firms to get out in front of anticipated regulations; (2) reducing their customers’ environmental impacts and decreasing their customers’ exposure to unhealthy substances; (3) increasing their reuse and recycling of materials used in the production process; (4) improving their energy efficiency or that of their customers; (5) improving their resource productivity or that of their customers; (6) implementing systems to identify waste reduction, pollution prevention, energy efficiency, or resource productivity opportunities throughout the company or facility; (7) collecting and disseminating more information about the firm’s environmental impacts and performance than the law requires; (8) providing more opportunities for stakeholder input into corporate environmental decision making than the law requires; and (9) financing and investing in green products and business models, such as those described above. \textit{Id.} (emphasis added).

corporate form claim that corporations are legally obliged to maximize shareholder welfare, which traditionally means maximizing profits. Typically, they cite to the venerable 1919 case of *Dodge v. Ford*, in which the Michigan Supreme Court arguably held that the Ford Motor Company nonpayment of special dividends was impermissible because the company’s motive was philanthropic. They also reference the sale in 2000 of socially and environmentally oriented Ben & Jerry’s Homemade, Inc. to the multinational Unilever, supposedly required by corporate law against the wishes of the company’s board of directors. More recently, opponents have cited the case of *eBay v. Newmark* in which the Delaware court struck down one of Craigslist’s defensive measures, a shareholder rights plan (or “poison pill”), in part because its purpose was not to advance shareholder welfare.

The argument is that assuming corporations must maximize profit, they will be unable to effectively pursue their social or environmental mission. Profit maximization would in fact prevent Kaldor-Hicks efficient transactions that would even minimally harm shareholders. (A Kaldor-Hicks transaction is one that benefits one group of stakeholders more than it harms another group of stakeholders: the winners win more than the losers lose.) Put differently, even if the transaction has a net benefit it is still impermissible if the shareholders would be the losers. In the case of a change of control transaction, only the shareholders’ interests count, meaning that if there is to be a sale it must be to the highest bidder.

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20 See Page, supra note 19, at 988. The issue is only with the corporate form. Limited Liability Companies clearly need not profit maximize. See DEL. CODE ANN. tit. 6, § 18-106(a) (West 2011) (“A limited liability company may carry on any lawful business, purpose or activity, whether or not for profit . . . .”).


23 *eBay Domestic Holdings, Inc. v. Newmark*, 16 A.3d 1 (Del. Ch. 2010).


Leaving the discussion over what corporate law actually requires with respect to shareholder wealth maximization, even if this is correct, this does not mean that there is a practical method of legal enforcement. Courts are typically extremely deferential to the business decisions of unbiased directors, and as a result operating decisions are almost never overturned. Under the business judgment rule, courts are comfortable allowing directors virtually unreviewable authority. As former Delaware Chancellor William T. Allen, Vice Chancellor Jack Jacobs, and Vice Chancellor Leo Strine put it, the business judgment rule is “an expression of a policy of non-review of a board of directors’ decision.” Although the director’s standard of conduct (how legislatures and judges hope directors will behave) may appear high, the judicial standard of review (the line between where courts will take action and where they will not) is much lower. There is a gap between these two standards that allows an enormous amount of discretion for directors that choose to pursue green goals. Thus commentators can reasonably conclude that “American corporate law permits firms to pursue . . . green practices and business plans.”

Consider Procter & Gamble (“P&G”), although there are numerous examples. P&G’s “long-term environmental sustainability vision . . . includes: [p]owering our plants with 100% renewable energy; [u]sing 100% renewable or recycled materials for all products and packaging; [h]aving zero consumer and manufacturing waste go to landfills; [and] designing products that delight consumers while maximizing our conservation of resources.”

P&G’s stated intention is to “deliver products with an improved environmental profile” and to “improve the environmental profile of our own operations.” These actions may be profit maximizing, or they may

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27 See, e.g., FRANKLIN A. GEVURTZ, CORPORATION LAW § 4.1.2, at 278–79 (2000) (“The idea underlying the [business judgment] rule is that courts should exercise restraint in holding directors liable for (or otherwise second guessing) business decisions which produce poor results or with which reasonable minds might disagree.”).
28 Id.
simply be greenwashing, but facially, at least, they look green, and shareholders have not sued the company.33

Likewise, there are virtually no judicially imposed limits on a corporation’s charitable donations. Legislators and courts have expressly permitted corporations to make these donations,34 and absent a clear conflict of interest, courts are loath to interfere. Sometimes, even if there is a conflict of interest, courts are reluctant or unable to interfere. In a notorious case involving Armand Hammer, Occidental Petroleum agreed to donate to the Armand Hammer Museum of Art and Cultural Center.35 The court noted that “[i]f the Court was a stockholder of Occidental it might vote for new directors, if it was on the Board it might vote for new management and if it was a member of the Special Committee it might vote against the Museum project” but as a judge he would likely have to allow the expenditure under the business judgment rule.36 A corporation could aggressively pursue an environmental mission in the sense that it would donate a significant percentage of its profits to an environmentally oriented charity. Would-be conflict with corporate law only occurs when the business is making operating decisions that are no longer in the interests of profit maximization.

Legally, it would be possible for an entrepreneur to form a traditional profit maximizing corporation and simultaneously form a non-profit. The two organizations could then work together, in that the corporation could donate a significant portion of its profits to the non-profit which could then fund projects to ameliorate the environment. As long as the non-profit’s use of funds was consistent with its charitable purpose, the non-profit could provide assistance,37 so that the for-profit

33 See, e.g., CAL. CORP. CODE § 207(e) (West 2012) (providing that corporations have the power to “[m]ake donations, regardless of specific corporate benefit, for the public welfare or for community fund, hospital, charitable, educational, scientific, civic, or similar.”); DEL. CODE ANN. tit. 8, § 9 (2012) (granting corporations the power to “make donations for the public welfare or for charitable, scientific, or educational purposes . . .”); MODEL BUS. CORP. ACT § 3.02(13) (2005) (“Unless its articles of incorporation provide otherwise . . . (13) to make donations for the public welfare or for charitable, scientific, or educational purposes . . .”).
34 See R. Franklin Balotti & James Hanks, Jr., Giving at the Office: A Reappraisal of Charitable Contributions by Corporations, 54 BUS. L. 965, 966 (1999) (“The present law regarding a corporation’s power to make altruistic charitable contributions (i.e., charitable contributions with no underlying business benefit) in most, if not all, American jurisdictions is one of the few rules of corporation law that permits a corporation to take action largely irrespective of corporate benefit.”).
36 Id. at *1630.
37 See Page & Katz, supra note 22, at 219.
would operate in a more environmentally friendly manner. This could, of course, be a legally complicated, Rube Goldberg–like arrangement, but conceptually it would be legal. 38

Finally, this is not a problem, or at least not so much a problem, for closely held corporations. If there is only one shareholder, or a small number of like-minded shareholders, corporations can clearly pursue whatever mission the shareholders want. 39 After all, nobody but the shareholders would even have standing to sue. Thus, closely or solely held companies with long histories that have recently become benefit corporations, like Patagonia and Greyston Bakery, 40 were not actually hampered in their pursuit of goals other than or additional to profit.

Contractarians, those who view corporations as a “nexus of contracts,” 41 should have no issue with corporations that choose to pursue dual missions as long as this goal is clearly stated ex ante. For them, profit maximization is simply a default principle that can be easily varied. 42 As two leading contractarians, Frank Easterbrook and Daniel Fischel wrote:

[W]hat is the goal of the corporation? Is it profit, and for whom? Social welfare more broadly defined? . . . Our response . . . who cares? If the New York Times is formed to publish a newspaper first and make a profit second, no one should be allowed to object. Those who came in at the beginning consented, and those who came later bought stock the price of which reflected the corporation’s tempered commitment to a profit objective. If a corporation is started with a promise to pay half of the profits to the

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38 It is perhaps not all that different from Ben & Jerry’s Homemade, Inc. and the Ben & Jerry’s Foundation, in that the foundation was the sole holder of preferred stock that held a veto right over the company’s change of control transactions. See Page & Katz, supra note 22, at 238.
40 See Lifsher, supra note 12, Greyston Bakery, supra note 17; Tozzi, supra note 39.
41 Henry N. Butler, The Contractual Theory of the Corporation, 11 GEO. MASON U. L. REV. 99, 100 (1988) (“The contractual theory views the corporation as founded in private contract, where the role of the state is limited to enforcing contracts. In this regard, a state charter merely recognizes the existence of a ‘nexus of contracts’ called a corporation.”).
42 See id. “Freedom of contract requires that parties to the ‘nexus of contracts’ must be allowed to structure their relations as they desire.” Id.
employees rather than the equity investors, that too is simply a term of the contract.43

More broadly, there is a long-standing dispute about what a corporation’s purpose ought to be.44 Dating back to at least the early 1930s, there have been those who support shareholder wealth maximization debating with those who believe that corporations should assume greater social, and more recently environmental, obligations.45 Berle and Dodd’s famous debate in the pages of the Harvard Law Review are a prominent early instance of that.46 Interestingly, both participants later reversed their views. Later, Milton Friedman in the New York Times stated that “there is one and only one social responsibility of business—to use its resources and engage in activities designed to increase its profits.”47 The debate itself has proved inconclusive with multiple iterations and no clear winner.48

Hybrid businesses are perhaps a way out of this debate, for some of the arguments in favor of shareholder wealth maximization depend on the notion that a corporation’s directors are agents of the shareholders with primary responsibilities to the shareholders.49 If the shareholders would like a corporation to pursue a green mission in addition to profit maximization there should be no dispute.50 Moreover, even if “American

43 FRANK H. EASTERBROOK & DANIEL R. FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW 35–36 (1991). See also Jonathan R. Macey, A Close Read of an Excellent Commentary on Dodge v. Ford, 3 VA. L. & BUS. REV. 177, 179 (2008) (stating that “maximizing shareholder gain is only a default rule” and that “[s]hareholders could opt out of this goal if they so desired.”).
44 See William W. Bratton & Michael L. Wachter, Shareholder Primacy’s Corporatist Origin: Adolf Berle and the “Modern Corporation,” 34 J. CORP. L. 99, 100 (2008) (“A continuing and longstanding debate has been waged in corporate law scholarship among those who favor shareholder primacy, those who favor management discretion, and those who believe that corporations have a social responsibility to other constituencies, such as the corporation’s employees, and the wider public interest.”).”)
45 See id. at 102.
46 See id. at 101.
47 Friedman, supra note 24.
49 See Friedman, supra note 24 (“the key point is that, in his capacity as a corporate executive, the manager is the agent of the individuals who own the corporation or establish the eleemosynary institution, and his primary responsibility is to them.”). In fact, a co-founder of B Lab, Andrew Kassoy, claimed that “Milton Friedman would have loved” the benefit corporation. CORP. SOC. RESP. NEWSWIRE, supra note 4.
50 Thus a business like Newground Social Investment will convert into a social purpose corporation it will largely be symbolic since there is only one shareholder. John Tozzi,
corporate law tolerates green businesses . . . [it] generally stops there, however, and neither encourages green business efforts nor particularly discourages them."\(^{51}\) Hybrid forms might actually encourage such efforts.

**Non-profits.** Non-profits have a very different shortcoming from the corporate form. The distinguishing legal feature of the non-profit is the non-distribution constraint, which is simply a "prohibition on the distribution of profits."\(^{52}\) A non-profit’s assets are locked up: there are no owners, and there is no potential for extraordinary returns.\(^{53}\) As a result, there is no equity, and non-profits have to depend upon other sources, notably donative income.\(^{54}\) Given that there are shortages of donative income, it is hard for non-profits to collect adequate amounts of capital and, thus, harder for them to grow quickly.\(^{55}\) For non-profits earning a significant amount of income, there are some legal constraints such as the unrelated business income tax.\(^{56}\) Moreover, because there is no equity it is harder to introduce incentive-based compensation.\(^{57}\) Put differently, there are no stock options in the non-profit world. In addition, the public is likely to view it as unseemly if the employees of non-profits receive high compensation.\(^{58}\)

II. **THE HYBRID ANSWER FOR GREEN BUSINESS**

New hybrid forms attempt to resolve the apparent shortcomings of traditional organizational forms by combining features of both the for-profit and non-profit world. These new hybrid forms include the community interest company in the United Kingdom, the low-profit limited liability company, or L3C, the benefit LLC, the benefit corporation, and the closely related flexible purpose corporation and social purpose

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\(^{51}\) Sneirson, *supra* note 30, 491–92.

\(^{52}\) See Hansmann, *supra* note 48, at 501.

\(^{53}\) See id. at 521.

\(^{54}\) See id. at 502.

\(^{55}\) See id. at 549.


\(^{57}\) See DAN PALOTTA, UNCHARITABLE: HOW RESTRAINTS ON NONPROFITS UNDERMINE THEIR POTENTIAL 119 (2009).

\(^{58}\) Coaches of college football and basketball teams may be an exception to this rule. For a compilation of salaries for college football coaches, see College Football Coach Salary Database, 2006–2011, USA Today (Nov. 17, 2011), http://usatoday30.usatoday.com/sports/football/story/2011-11-17/cover-college-football-coaches-salaries-rise/51242232/1.
corporation.\textsuperscript{59} This Article will look specifically at the benefit corporation and compare and contrast it to the flexible or social purpose corporation.

The benefit corporation has been enacted in eleven states (California, Hawaii, Illinois, Louisiana, Maryland, Massachusetts, New Jersey, New York, South Carolina, Vermont, Virginia)\textsuperscript{60} and proposed in at least fourteen more,\textsuperscript{61} while other states have not been able to pass the proposed legislation.\textsuperscript{62} There are significant differences in the various enactments and six major differences from the traditional corporation: purpose, fiduciary duties, reporting, third-party standards, enforceability or derivative suits, and what can be broadly characterized as governance procedures.\textsuperscript{63}

In addition to the benefit corporation, there are two other corporate forms that have been introduced for dual-mission businesses. These include the social purpose corporation in Washington,\textsuperscript{64} and the flexible purpose corporation in California that was introduced simultaneously with, and as an alternative to, its benefit corporation.\textsuperscript{65} Both are similar to each other, but differ from benefit corporations in terms of their stated purpose, use of a third-party standard, use of benefit enforcement proceedings, and grant to shareholders of dissenters rights.\textsuperscript{66}

\begin{itemize}
\item \textsuperscript{63}See Reiser, \textit{supra} note 59, at 600, 604–06.
\item \textsuperscript{64} See H. B. 2239, 62d Leg., Reg. Sess. (Wash. 2012).
\item \textsuperscript{65} See CAL. CORP. CODE § 2602 (West 2012).
\item \textsuperscript{66} Memorandum from The Volunteer Legal Services Program of the Bar Association of San Francisco (2012), available at http://www.sfbar.org/forms/vlsp/benefit-corp-memo%20.pdf;
All of the above corporate forms are primarily governed by the respective state’s preexisting corporate law. Similarly, they must include the new designation in their name, note that it will be governed by the particular chapter of the corporate code, and state its general public benefit, social purpose or special purpose, or specific benefit. No doubt in the interests of full disclosure to potentially unwary investors, a social purpose corporation must also include in its articles language stating “[t]he 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.”

Much, however, of what is required for a benefit corporation is optional for the social purpose corporation, and in some cases the social purpose corporation is even given additional latitude. For example, it may require directors to consider the impacts of a decision on the social purpose corporation’s purpose; an assessment provided to shareholders based on a third-party standard; and a supermajority vote for any corporate action, including those for which shareholder approval is not otherwise required. In addition, the corporation’s existence may be limited to a specified date and it is also permitted to designate specific social purposes.

*Purpose.* All benefit corporations must have a “general public benefit” that is generally defined as “a material positive impact on society and the environment taken as a whole, as measured by a third-party standard, from the business and operations of a benefit corporation.”


67 See H. B. 2239 § 2, 62d Leg., Reg. Sess. (Wash. 2012) (“Except as otherwise expressly stated in this [social purpose corporation] chapter . . . references in this title to the term ‘corporation’ shall be read to include social purpose corporations organized under this chapter.”); CAL. CORP. CODE § 2501 (West 2012).

68 California is similar. See CAL. CORP. CODE § 2602 (West 2012).

69 WASH. REV. CODE § 23B.25.040 (2012). In California, if the business is related to banking, insurers, professional corporations or close corporations, other provisions are also required. See CAL. CORP. CODE § 2501 (West 2012).

70 WASH. REV. CODE § 23B.25.040.2(a)−(e) (2012).

71 WASH. REV. CODE § 23B.25.040.2(d)−(e) (2012).

Several states, however, require instead that the general benefit must result from activities that advance specific public benefits.\textsuperscript{73}

Benefit corporations may also specify in their articles (or in some cases bylaws)\textsuperscript{74} one or several “specific public benefits,” which is generally one related to underprivileged populations, health improvements, environment, education, arts, science, or the increase of capital to organizations intended to provide public benefits.\textsuperscript{75} All but one state has also included a catch-all provision that captures the conferring of “any other particular benefit on society or the environment.”\textsuperscript{76} Massachusetts, for example, is fairly typical. Its statute provides that:

“Specific public benefit”, [includes] any of the following:
(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) promoting the preservation and conservation of the environment; (4) improving human health; (5) promoting the arts, sciences, access to and advancement of knowledge; (6) increasing or facilitating the flow of capital and assets to entities with a general public benefit purpose; or (7) conferring any other particular benefit on society or the environment.\textsuperscript{77}

Hawaii’s law is even more specific, adding provisions related to the use of patents, the upholding of fair labor standards nationally and

\textsuperscript{73} See, e.g., Maryland, Md. CODE ANN., CORPS. & ASS’NS § 5-6C-01 (West 2011) (“activities that promote a combination of specific public benefits”); New Jersey, N.J. STAT. ANN. § 14A:18-1 (West 2011); New York, N.Y. BUS. CORP. LAW § 1702(b) (McKinney 2012) (explaining the definition of “public benefit”); Vermont, Vt. STAT. ANN. tit. 11A, § 21.08 (West 2011) (“The articles of incorporation . . . may identify one or more specific public benefits . . .”).

\textsuperscript{74} VA. CODE ANN. § 13.1-787(a) (2011).

\textsuperscript{75} Virginia adds religious purpose to that list. VA. CODE ANN. § 13.1-782 (2011).

\textsuperscript{76} N.Y. BUS. CORP. LAW § 1702(e) (Consol. 2012). Louisiana is the only state that does not include a catchall provision. See LA. REV. STAT. ANN. § 12:1803 (2012). Some states use different language, like Vermont. Vt. STAT. ANN. tit. 11A, § 21.03 (2011) (“[T]he accomplishment of any other identifiable benefit for society or the environment.”).

\textsuperscript{77} MASS. GEN. LAWS ch. 156e, § 10(a)(2) (2012).
internationally, the creation and retention of good jobs, and the enhancement of environmental protection.

With respect to the specific public benefit relating to the environment, particular language ranges from merely “preserving the environment,” “preserving or improving the environment,” to “preserving the environment, promoting positive impacts on the environment, or reducing negative impacts on the environment.” Given the catch-all provision—any particular or identifiable benefit for the environment—it is not clear that specific language related to the environment makes any real difference.

A social purpose corporation’s mission is phrased differently from that of a benefit corporation’s express purpose of a “material positive impact on society and the environment.” Instead, a social purpose corporation:

[must be] organized to carry out [its specified] business purpose in 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 (3) the environment.

A flexible purpose corporation must pursue a special purpose which is either “[o]ne or more charitable or public purpose activities that a nonprofit public benefit corporation is authorized to carry out” or “[t]he purpose of promoting positive short-term or long-term effects of, or minimizing adverse short-term or long-term effects of, the flexible purpose corporation’s activities upon any of the following: (i) [t]he flexible purpose

78 HAW. REV. STAT. § 420D.5(b) (West 2011) (“Creating and retaining good jobs within the State as well as throughout the United States . . .”).
79 Id. (“Upholding fair labor standards nationally and internationally; provided for purposes of this paragraph, ‘fair labor standards’ shall be construed to prohibit child labor, forced or compulsory labor, discrimination in employment, restrictions on freedom of association, and denial of the right to collective bargaining . . .”).
80 Id. (“Enhancing environmental protection nationally and internationally . . .”).
81 MD. CODE ANN., CORPS. & ASS’NS § 5-6C-01(d) (West 2011).
84 CLARK & VRANKA, supra note 72, at 15.
corporation’s employees, suppliers, customers, and creditors. (ii) the community and society. (iii) the environment.”

For green businesses, the specific purpose or public benefit is not an issue. Any plausible environmental goal would be sufficient. A concern, however, is that the environmental purpose chosen might be trivial, or might be something that the company was already doing. As one commentator on California’s version noted, a company can use its “carbon emissions abatement presently pursued, [could be] an excuse for reincorporating as a flexible purpose corporation for the benefit of being known as doing good.” This low bar avoids problems in determining what kind of green benefits are sufficient or who the decision makers should be.

There could, however, be problems, at least conceptually, with the benefit corporation’s general public benefit. A benefit corporation must create a material positive impact on society and the environment. Presumably, creating a material positive impact on the environment alone would be insufficient (i.e., the argument that a material positive impact on the environment would necessarily also be a material positive impact on society would be unavailing), and the environmental and social benefits could be in conflict. A business that chooses to privilege the environment over social concerns might find itself violating this provision. Thus a company like Guayaki, which has an environmental mission of preserving the Amazon rainforest, might pay its U.S. workers below the poverty rate.

It should also be noted that one up-front cost that is increased with these new forms is that a hybrid corporation must define its social benefit and purpose in advance for the articles of incorporation. This requires sufficient agreement among the founders and could be time-consuming. It might also prove futile if the business or business context do not develop as expected. Granted, clear articulation of the mission may also have benefits. This contrasts with a traditional corporation.

87 W. Derrick Britt et al., Everything You Ever Wanted to Know About the Flexible Purpose Corporation (and Then Some), BUS. FORGOOD (Feb. 23, 2011), http://www.businessforgood.co/2011/03/frequently-asked-questions-proposed.html.
88 Id. (internal quotations omitted).
89 CLARK & VRANKA, supra note 72, at 1.
92 See Reiser, supra note 59.
where the articles of incorporation typically merely state the corporation is being formed for any lawful business purpose.93

Fiduciary duties. As with a traditional corporation, directors will have the fiduciary duties of loyalty and care.94 Legislatures do not intend any changes to the duty of loyalty, which, of course, is intended to capture conflict of interest situations.95 The duty of care, however, is altered, in that directors of benefit corporations have an affirmative duty to consider certain other interests besides those of shareholders, and they are also permitted to consider almost any non-shareholder interest.96

Massachusetts, for example, requires that the board of directors, board committees and the individual director consider the effects of any action on shareholders, employees, customers (as beneficiaries of the public benefit corporations’s purpose), the community and societal factors, the local, regional and global environment, the benefit corporation’s short-term and long-term interests, the accomplishment of the benefit corporation’s purposes, and whether remaining independent may be in the best interests of the corporation.97

A. In discharging the duties of their respective positions and in considering the best interests of the benefit corporation, the board of directors, committees of the board and individual directors of a benefit corporation:

1. shall consider the effects of any action upon:
   i. the shareholders of the benefit corporation;
   ii. the employees and workforce of the benefit corporation, its subsidiaries and its suppliers;
   iii. the interest of customers or clients as beneficiaries of the general public benefit or specific public benefit purposes of the benefit corporation;
   iv. community and societal factors, including those of each community in which offices or facilities of the benefit corporation, its subsidiaries or its suppliers are located;
   v. the local, regional and global environment;
   vi. the short-term and long-term interests of the benefit corporation, including benefits that may accrue to the benefit corporation from its long-term plans and the possibility that these interests may be best served by the continued independence of the benefit corporation; and

93 See CLARK & VRANKA, supra note 72, at 16.
94 See id. at 8.
95 See Reiser, supra note 59, at 601.
96 See id. at 599.
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This last bullet point is clearly intended to allow directors to refuse an unwanted takeover bid. Other states have addressed this in different ways, such as silence, \(^{98}\) or permissively allowing directors to consider “[t]he resources, intent, and conduct of any person seeking to acquire control of the [benefit] corporation.” \(^{99}\)

In case the list of mandatory concerns is insufficient, directors also have the option of considering state, regional and national economic interests, or “other pertinent factors or the interests of any other group that they deem appropriate.” \(^{100}\)

Directors need use “sound and reasonable judgment” for their decision-making, and need not prioritize any particular interest unless the articles have stated that there will be prioritization. \(^{101}\) Some states have not included this prioritization language. \(^{102}\)

There are other minor differences among the states, however, given that all include permissive language, like the provision quoted above, and none would necessarily be dispositive with respect to the actual decision reached (just as with judicial multifactored tests), it is unlikely that these differences will prove significant.

For a flexible purpose corporation, fiduciary duties are also more flexible, in that a director or officer may consider the corporation’s social purpose, but need not. \(^{103}\) Directors are essentially protected by the

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\(^{98}\) See MD. CODE ANN., CORPS. & ASS’NS § 5-6C-07 (West 2011).

\(^{99}\) HAW. REV. STAT. § 420D.6 (West 2011).

\(^{100}\) MASS. GEN. LAWS ch. 156E, § 10(a)(2) (West 2011) (Directors “may consider: (i) the interests of the economy of the state, the region and the country . . . ; or (ii) other pertinent factors or the interests of any other group that they deem appropriate.”).

\(^{101}\) (b) Directors shall consider the factors in clause (1) of subsection (a) using sound and reasonable judgment in determining corporate actions and the best interests of the benefit corporation. Directors shall not be required to give priority to the interests of a particular person or group referred to in clauses (1) or (2) of said subsection (a) over the interests of any other person or group unless the benefit corporation has stated in its articles its intention to give priority to certain interests related to its accomplishment of its general public benefit purpose or of a specific public benefit purpose identified in its articles.

\(^{102}\) See MD. CODE ANN., CORPS. & ASS’NS § 5-6C-07 (West 2011).

\(^{103}\) See MD. CODE ANN., CORPS. & ASS’NS § 2602(2)(B)(ii) (West 2011).
business judgment rule in the same way as directors of traditional corporations, but are also expressly protected from liability with respect to those decisions that balance profit-making and the pursuit of the mission.

A criticism of both types of hybrid corporation is that the legislation provides little guidance on how directors should make decisions. In other words, after considering the effect on the various enumerated stakeholders, and optionally considering anything else deemed relevant, how is the director supposed to prioritize? In some cases, the various potential effects of an action will be completely incommensurate. How, for example, would one compare the impairment of a scenic view with lost jobs? Or, to cite a recent example, the increase in food-borne illnesses with the reduction of the use of plastic grocery bags? The result is a lack of accountability.

**Reporting.** Benefit corporations are required to prepare and release an “annual benefit report.” The report must describe ways the benefit corporation pursued both the general public benefit and any specific public benefit, the extent to which either kind of public benefit was created, and circumstances that hindered the creation of benefits. The report must also assess the benefit corporation’s social and environmental performance, in accordance with the consistent application of the third party’s standard along with an explanation for any inconsistent

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104 Under CAL. CORP. CODE § 2700(a), a director must act “in good faith, in a manner the director believes to be in the best interests of the flexible purpose corporation and its shareholders, and with that care, including reasonable inquiry, as an ordinarily prudent person in a like position would use under similar circumstances.” CAL. CORP. CODE § 2700(a) (West 2012). There is no significant difference between this standard and that set forth in CAL. CORP. CODE § 309(a) for traditional corporations. See id. § 309(a).

105 See id. § 309(c)–(d) (West 2012).


A few states have added additional disclosure requirements, such as Vermont, that require the listing of specific actions the benefit corporation could take to improve its performance. New Jersey provides for disclosure of the directors’ compensation and the identity of five percent or greater shareholders, and California requires a description of the process and rationale for the use of the third-party standard and information that might affect the credibility of the standard.

This report must then be made available to shareholders and posted on a publicly accessible portion of the benefit corporation’s website. Most states allow benefit corporations to remove old benefit reports from their website. Some states also require the benefit corporation to file the report with a relevant state agency.

Those states which require a benefit director, discussed under corporate governance, also require that the report includes her statement regarding whether the benefit corporation complied in all material respects with the state’s act and in accordance with its benefit purpose.

A flexible purpose corporation must also produce a “social purpose report” (in Washington) or a “special purpose current report” (in...
California) that is substantially similar to an annual benefit report, except that it is not based on third-party standards and there is no statement by a benefit director.\footnote{121} In California, shareholders can also waive the special purpose current reports if there are fewer than one hundred shareholders and waivers by two thirds of the shares.\footnote{122}

These reports are in many ways similar to corporate social responsibility reporting, albeit with more specifically required elements.

\footnote{121} \textsc{Cal. Corp. Code} § 3501(b)(1)–(5). California requires some additional details. In particular the articles shall include:

1. Identification and discussion of the short-term and long-term objectives of the flexible purpose corporation relating to its special purpose or purposes, and an identification and explanation of any changes made in those special purpose objectives during the fiscal year.

2. Identification and discussion of the material actions taken by the flexible purpose corporation during the fiscal year to achieve its special purpose objectives, the impact of those actions, including the causal relationships between the actions and the reported outcomes, and the extent to which those actions achieved the special purpose objectives for the fiscal year.

3. Identification and discussion of material actions, including the intended impact of those actions, that the flexible purpose corporation expects to take in the short term and long term with respect to achievement of its special purpose objectives.

4. A description of the process for selecting, and an identification and description of, the financial, operating, and other measures used by the flexible purpose corporation during the fiscal year for evaluating its performance in achieving its special purpose objectives, including an explanation of why the flexible purpose corporation selected those measures and identification and discussion of the nature and rationale for any material changes in those measures made during the fiscal year.

5. Identification and discussion of any material operating and capital expenditures incurred by the flexible purpose corporation during the fiscal year in furtherance of achieving the special purpose objectives, a good faith estimate of any additional material operating or capital expenditures the flexible purpose corporation expects to incur over the next three fiscal years in order to achieve its special purpose objectives, and other material expenditures of resources incurred by the flexible purpose corporation during the fiscal year, including employee time, in furtherance of achieving the special purpose objectives, including a discussion of the extent to which that capital or use of other resources serves purposes other than and in addition to furthering the achievement of the special purpose objectives.

\footnote{122} \textsc{Cal. Corp. Code} § 3502(h) (West 2012).
Corporations can already publish annual benefit reports, and are already required to disclose some environmental related information.123

There may in fact be a “growing trend of traditional financial reporting and sustainability issues intersecting”124 and moreover there is likely “significant progress in CSR reporting in the last couple of years both in terms of quality and quantity.”125 That said, companies pick and choose what they wish to disclose, resulting in incommensurate reports126 and the fear of greenwashing.127 Forbes, for example, noted that “[t]oday’s consumer landscape is saturated with marketing campaigns that promise customers green(er) services or products but are challenged to deliver substantiated data that empowers, educates and connects with buyers [sic] values.”128
Although there are several organizations that have or are trying to develop CSR reporting standards, and some expect that there will “be a convergence around a smaller subset of CSR reporting standards,” this could easily take ten to fifteen years, if it happens at all.129 The annual benefit report will not necessarily change this, except to the degree that a few third-party standard setters require it.130

There is also a tension between permitting flexibility in reporting and requiring conformity, which makes comparisons between businesses easier. There is a reason the Securities and Exchange Commission spells out requirements for financial reporting.

Patagonia’s experience may be illustrative. It published an audited corporate social responsibility report in 2004, based on the Global Reporting Initiative, an organization that develops and disseminates reporting guidelines.131 Patagonia decided the report was inauthentic and did not reflect the company well.132 Patagonia’s director of environmental analysis stated, “It was as boring as all the other reports out there—it felt like a marketing statement.”133 The CEO, Yvon Chouinard, was harsher, calling it “absolute bullshit.”134 Since then, Patagonia has produced the “Footprint Chronicles” which they believe is more honest and accurate, and helps to reduce their adverse social and environmental impacts.135 The company also notes that they “know that when we can reduce or eliminate a harm, other businesses will be eager to follow suit.”136

There are other potential advantages with the benefit report. As one blog notes, with Patagonia’s enhanced disclosure, “Life is going to be tougher and more uncomfortable for more clothing companies thanks to Patagonia’s increasing disclosure.”137 Moreover, some make a business case for disclosure, above and beyond the potential marketing advantages.138

129 Tschiggfrie, supra note 126.
130 See Reiser, supra note 59, at 600–01.
133 Id.
134 See id.
136 Id.
The European Commission “by disclosing social, environmental and governance information, enterprises often find that they can better identify and manage issues that influence their business success. Good disclosure of non-financial information enables investors to contribute to a more efficient allocation of capital and better achieve longer-term investment goals.”

**Third-party standards.** In order to judge whether a benefit corporation is achieving its general public benefit, statutes require the use of a third-party standard. This third-party standard must be developed by a party that is independent of the benefit corporation. It must be “comprehensive in its assessment of the effect of the business and its operations upon the interests listed that the board shall and may consider when making decisions,” such as information relevant to the criteria selected, the relative weights of the criteria, the revisions process, the standard setting body, including its owners, leadership, and the process by which the leadership changes. B Lab is the most prominent standard setter, but other organizations like Green Seal and Green America are intended to be eligible as standard setters for green businesses. In contrast, flexible purpose and social purpose corporations, like other corporations, may engage third parties to set standards, but are not required to do so.

Some have also noted that there may be a conflict of interest, in that B Lab, an early proponent of benefit corporations, is likely the most important third-party standard provider. It has apparently developed a standard that is available to interested corporations starting at $25,000 per year. Proponents of the flexible purpose corporation have also argued

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139 Id.
140 See CLARK & VRANKA, supra note 72, at 1.
141 See id. at 18.
142 HAW. REV. STAT. § 414D.12 (West 2010).
143 See About Green Seal, GREEN SEAL, http://www.greenseal.org/AboutGreenSeal.aspx (last visited Jan. 10, 2013) (“We develop life cycle-based sustainability standards for products, services and companies and offer third-party certification for those that meet the criteria in the standard.”).
144 See What We Do, GREEN AM., http://www.greenamerica.org/about/whatwedo/ (last visited Jan. 31, 2013) (“Promoting green and fair trade business principles while building the market for businesses adhering to these principles.”).
145 See CLARK & VRANKA, supra note 72, at 3, 24.
146 See id. at App. C, 8.
147 See Andre, supra note 107, at 140.
that the use of third-party standards could in fact stifle innovation in the future, or could “devolve into a ‘back-door’ means for regulating certain products or pursuing other controversial public policy objectives and, ultimately, would lead any discussion of such a legislative proposal into the turmoil of special interests.”

Enforceability/derivative suits. Corporate directors can be sued for their breach of fiduciary duties of care and loyalty. Based on a somewhat murky division, depending primarily on the kind of harm caused by the breach, these suits may either be direct on the part of the shareholders or derivative on the part of the corporation. Several states have introduced an analogous procedure, the benefit enforcement proceeding, as a means of ensuring that directors and officers perform their duties, including the pursuit of the general and specific public benefit.

These lawsuits may generally be brought derivatively by a shareholder, or a director, although some states also permit the benefit corporation itself to bring an action, or any person specified in the articles or bylaws. Just as derivative suits for the breach of the duty of care are very difficult for the plaintiff to win, benefit enforcement proceedings are likely to be the same. States include provisions that reduce the chance of liability. For example, Virginia bars personal liability for the failure of the benefit corporation to create a public benefit, or as long as the director has performed in compliance with the obligations set forth for a traditional corporation, i.e., to act “in accordance with [the director’s] good faith business judgment of the best interests of the corporation.”

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149 See Britt et al., supra note 87.
151 Id.
157 The Virginia Code provides that:

[i]n any proceeding brought by or in the right of a benefit corporation or brought by or on behalf of the shareholders of a benefit corporation, a director is not personally liable for monetary damages for: 1. Any action
Moreover benefit corporations, just like traditional corporations, can include an exculpation clause in their articles.\(^{158}\)

**Governance Procedures.** There are two changes that some states have introduced that address the benefit corporation’s governance procedures: benefit directors and supermajority votes.\(^{159}\)

The board of a benefit corporation in most states must include one “benefit director,” who must be independent.\(^{160}\) In addition to the rights and responsibilities of the other director, the benefit director prepares the statement regarding the benefit corporation’s performance referenced above.\(^{161}\) Many states have chosen not to introduce the use of benefit directors.\(^{162}\)

In order to change a benefit corporation’s purpose, typically a two-thirds supermajority of the votes of each class of shareholders is required.\(^{163}\) Other states are silent on the question.\(^{164}\) In any case, a benefit corporation could, in any state, impose a higher requirement for this kind of change.

A change, and for certain change of control transactions that would materially affect the social mission, requires the approval of two-thirds of the votes.\(^{165}\) Shareholders of social purpose and flexible purpose corporations are also given dissenters rights—essentially a put, i.e., the right

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\(^{158}\) Exculpatory clauses, of which Delaware General Corporate Law § 102(b)(7) is the most prominent, allow for early dismissal of certain kinds of fiduciary duty claims. See DEL. CODE ANN. tit. 8, § 102(b)(7) (2012).


\(^{160}\) See Munch, *supra* note 159.

\(^{161}\) See VT. STAT. ANN. tit. 11A, § 21.09(d) (referencing traditional corporation standards for directors).


\(^{163}\) See Munch, *supra* note 159.


to sell, at fair value—in the event that the corporation’s purpose materially changes or it ceases to be a social purpose corporation.166

A two-thirds supermajority vote does not do much to protect a green business. The widespread fear that a green business will sell out to a conventional profit-maximizing company remain largely unaddressed. A business, regardless of form, will not be sold in situations where 1) the directors and shareholders do not want to sell, or 2) where directors want to sell but shareholders do not. Likewise the green business will be sold if both directors and shareholders want to sell (though the benefit corporation requires a modest supermajority). The difference between fifty percent plus one and sixty six and two-thirds percent plus one will rarely be significant.

CONCLUSIONS

a. Modest benefits but modest costs
b. Consider other mission maintenance mechanisms:
   longer terms for directors, stock with vetoes, delayed acquisitions (would lower the takeover premium), caps
c. Recognize limited role for law

There may also be concerns regarding financing. Just as angel or venture capitalists may be uncomfortable with the LLC in comparison to the corporation, even if there are tax advantages, they may be uncomfortable with a hybrid corporate form. In particular, directors of hybrid organizations are seen to have more discretion.167 Of course, there are some investors who may be attracted to the form as they want to invest in socially oriented businesses.168

There are three main arguments made against these new forms: they are unnecessary, potentially dangerous, and perhaps ineffective. The forms are considered unnecessary, because whatever the new forms can do, the old forms could do as well.

They are considered dangerous because of their potential misuse. Consumers may believe that a benefit corporation is in fact pursuing a more noble agenda than a traditional corporation. If in fact it is not, the

166 See, e.g., CAL. CORP. CODE § 3000 (West 2012).
167 See Reiser, supra note 59.
consumer will, in some sense, have been defrauded. The question is simply whether there is too great a risk of greenwashing with these new forms. Obviously, fraud can be committed with any organizational form—witness all the piercing the corporate veil legislation\textsuperscript{169}—so the issue would be whether the new forms substantially increase that risk.

There are, of course, several general advantages to these new forms. Even if it is possible to duplicate the structure of a benefit or flexible purpose corporation with the traditional corporation, using an off-the-rack standard form will reduce transaction costs. Moreover, the use of the state-sponsored form may serve a valuable signaling function to all stakeholders. It is also possible the form may help shape preferences, in that it expands the choices that an entrepreneur has. Finally, it may allow greater authenticity and transparency among employees.

Overall, the new organizational forms are likely a modest improvement for those who support green business. They may conceivably increase the number of green businesses. Perhaps the biggest issue is that little has been done to ensure that resources will remain dedicated to the green mission. Lawmakers and other entrepreneurs should consider different ways of encouraging sticking to missions. There are several legal ways this could be done. For example, the supermajority necessary to convert a benefit corporation to a traditional corporation could be raised, certain parties could be given veto rights by way of preferred stock, boards of directors could be elected for longer periods, and beneficiaries could be given additional representation.