WHY PUBLIC BENEFIT CORPORATIONS?

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ABSTRACT

Public Benefit Corporations ("PBCs") are a revolutionary new form of business organization that overturn the fundamental corporate principle of shareholder wealth maximization. Of the many questions that surround this new entity type, perhaps the most perplexing is why Delaware – the most influential and important state for corporate law by far – chose to adopt it. I explore this troubling question through qualitative empirical research. I find that Delaware primarily wanted to serve the needs of social entrepreneurs and financiers, but also hoped to harness the power of capitalism to remedy social ills that government has so far failed to fix. The PBC statute rather poorly implements either of these goals. The PBC statute is not a very good enforcement tool. On the other hand, the statute may prove an effective reinforcement tool, aiding sincere social entrepreneurs to pursue their various missions. Also, private ordering, such as certification by outside entities like B Lab, may fill many of the important gaps left by the law.

TABLE OF CONTENTS

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I. INTRODUCTION

Of all the social and economic challenges to the current state of Delaware corporate law, perhaps the most potentially cataclysmic is the shift in attitudes about the very purpose of corporations. Delaware corporate law holds as a core precept that the corporation's goal is to maximize shareholder value.[1] Corporations' freedom to serve the goals of other corporate constituencies (such as employees, customers, or the communities in which the companies operate) or to serve broader goals such as protecting the environment or aiding the poor is constrained by the requirement that any such efforts be primarily aimed at improving the bottom line for the benefit of the companies' shareholders.[2]

Not all observers agree that Delaware corporations must exclusively pursue profits. Progressive corporate legal scholars, such as Margaret Blair and Lynn Stout, have long asserted that corporate boards must balance the interests of different corporate constituencies, which sometimes means sacrificing profits to assist workers, lenders, or

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[1] The most recent statement of this legal principle in Delaware came in *eBay Domestic Holdings, Inc. v. Newmark*:

> The corporate form in which craigslist operates, however, is not an appropriate vehicle for purely philanthropic ends, at least not when there are other stockholders interested in realizing a return on their investment. Jim and Craig opted to form craigslist, Inc. as a *for-profit Delaware corporation* and voluntarily accepted millions of dollars from eBay as part of a transaction whereby eBay became a stockholder. Having chosen a for-profit corporate form, the craigslist directors are bound by the fiduciary duties and standards that accompany that form. Those standards include acting to promote the value of the corporation for the benefit of its stockholders. The "Inc." after the company name has to mean at least that. Thus, I cannot accept as valid for the purposes of implementing the Rights Plan a corporate policy that specifically, clearly, and admittedly seeks *not* to maximize the economic value of a for-profit Delaware corporation for the benefit of its stockholders—no matter whether those stockholders are individuals of modest means or a corporate titan of online commerce.

16 A.3d 1, 34 (Del. Ch. 2010) (internal footnote omitted); *see also* Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919) (stating, though arguably in dicta, "it is not within the lawful powers of a board of directors to shape and conduct the affairs of a corporation for the merely incidental benefit of shareholders and for the primary purpose of benefiting others, and no one will contend that, if the avowed purpose of the defendant directors was to sacrifice the interests of shareholders, it would not be the duty of the courts to interfere"); Leo E. Strine, Jr., *Our Continuing Struggle with the Idea That For-Profit Corporations Seek Profit*, 47 WAKE FOREST L. REV. 135, 151 (2012) (lambasting those who object to the view that, "as a matter of corporate law, the object of the corporation is to produce profits for the stockholders and that the social beliefs of the managers, no more than their own financial interests, cannot be their end in managing the corporation").

[2] Revlon, Inc. v. MacAndrews & Forbes Holdings, 506 A.2d 173, 176 (Del. 1986).

communities.[3] And the Delaware courts themselves have not always been clear on this point. For example, in the famous case of *Unocal Corp. v. Mesa Petroleum Co.,* the Delaware Supreme Court stated that one of the considerations a corporate board could consider when determining whether a hostile acquisition offer constituted a threat to the corporation was the offer's impact on constituencies other than shareholders, such as "creditors, customers, employees, and perhaps even the community generally."[4] The Court soon backtracked from this position, however, in *Revlon, Inc*.[5] There, the Court stated that "while concern for various corporate constituencies is proper when addressing a takeover threat, that principle is limited by the requirement that there be some rationally related benefit accruing to the stockholders."[6] Today, it seems reasonably clear that Delaware corporate law requires boards of directors to attempt to maximize shareholder profits, at least as a default rule.[7]

Entrepreneurs who want to pursue social goals to the exclusion of profits may form nonprofit corporations. But Delaware's corporate law historically provided no ready-made option for entrepreneurs who wanted to create an entity that balanced traditional profit-seeking with the pursuit of other social goals.[8] The Delaware legislature changed this with the

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[3] *See* Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VIRGINIA L. REV. 247, 252 (1999); LYNN A. STOUT, THE SHAREHOLDER VALUE MYTH: HOW PUTTING SHAREHOLDERS FIRST HARMS INVESTORS, CORPORATIONS, AND THE PUBLIC 111 (2012).

[4] 493 A.2d 946, 955 (1985).

[5] 506 A.2d at 182.

[6] *Id.* at 176.

[7] *See* Strine, *supra* note 1, at 151. It is possible that a provision in a corporations' certificate of incorporation that changed this rule would be enforced; DEL. CODE ANN. tit. 8, § 102(b)(1) (2015) (authorizing corporate charter provisions "for the management of the business and for the conduct of the affairs of the corporation, and any provision creating, defining, limiting and regulating the powers of the corporation, the directors, and the stockholders, or any class of the stockholders, or the governing body, members, or any class or group of members of a nonstock corporation; if such provisions are not contrary to the laws of this State"). While a provision changing the corporation's goal would seem to fall squarely within both "management of the business" and "conduct of the affairs," it still might run afoul of the exception for charter provisions that are "contrary to the laws of this State." No statute requires corporations to maximize shareholder value, but the principle is sufficiently strong in the common law that a court might find that charter provisions that contradict it are invalid. The opposite result, of course, is also quite possible, making the outcome of this issue difficult to predict.

[8] A Delaware limited liability company ("LLC") could likely be crafted to require balancing profits with other goals, given Delaware's emphasis on the malleability of the LLC form, but the LLC is not designed as an "off the shelf" option for this purpose. *See* Elf Atochem North America, Inc. v. Jaffari*,* 727 A.2d 286, 290-92 (Del. 1999) (stating that the Delaware Limited Liability Company Act is designed to give "maximum effect to the principle of freedom of contract" and that "only where the [operating] agreement is inconsistent with mandatory statutory provisions will the members' agreement be invalidated"); *see also* FREDERICK H. ALEXANDER, THE PUBLIC BENEFIT CORPORATION GUIDEBOOK: UNDERSTANDING AND OPTIMIZING DELAWARE'S BENEFIT CORPORATION GOVERNANCE MODEL 45-46 (2016),

adoption of a public benefit corporation statute in 2013, making it the fourteenth state to do so.[9]

In the states' competition for corporate registrations and their associated franchise taxes, Delaware is the clear winner. Whether the competition has resulted in a race to the bottom[10] or a race to the top[11] for corporate law, Delaware has found a formula that has attracted a clear majority of the major corporations in the U.S.[12] Delaware law is the gold standard.

By contrast, the benefit corporation form has often received poor reviews from corporate law experts.[13] Commentators have argued that the

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http://www.mnat.com/files/epub/ThePublicBenefitCorporationGuidebook_FrederickHAlexander.pdf (stating "[b]enefit corporations are increasingly popular structures for entrepreneurs looking to achieve both profit and social benefit, but similar goals can be accomplished in Delaware with a limited liability company").

[9] *See* DEL. CODE ANN. tit. 8, §§ 361-368 (2013). The states who adopted a benefit corporation statute prior to Delaware's were, in order: Maryland, New Jersey, Vermont, Virginia, Hawaii, California, New York, South Carolina, Louisiana, Massachusetts, Illinois, Pennsylvania, and Arkansas. *See infra* Part II. Washington, D.C. had also passed a benefit corporation statute prior to Delaware, on February 8, 2013. *See infra* note 23. The state of Washington authorized social purpose corporations, a similar form, in March of 2012, also ahead of Delaware. *See infra* note 21. It is likely, however, that a Delaware LLC could be crafted to achieve similar ends. *See supra,* note 8.

[10] Theorists who argue corporate law represents a race to the bottom claim that states compete for corporate charters (and the associated franchise taxes) by crafting their corporate law to be as favorable as possible to the managers who decide where to incorporate. *See* William Cary, *Federalism and Corporate Law: Reflections Upon Delaware*, 83 YALE L. J. 663, 664-66 (1974).

[11] The race to the top theory argues that managers will choose states with the best possible law for their shareholders. To do otherwise would suppress earnings, increase costs of capital, lower share prices, and risk hostile takeovers that would replace management. *See* Ralph K. Winter, Jr., *State Law, Shareholder Protection and the Theory of the Corporation*, 6 J. LEGAL STUD. 251, 256 (1977).

[12] *See* DELAWARE DIVISION OF CORPORATIONS, *2014 Annual Report*, https://corp.delaware.gov/Corporations_2014%20Annual%20Report.pdf (reporting that nearly two-thirds of Fortune 500 companies are incorporated in Delaware).

[13] *See, e.g.,* Sherwin Abrams, *Decisions, Decisions: Helping Clients Choose the Right Business Entity*, 101 ILL. B.J. 530, 534 (2013) (stating "[t]he L3C and benefit corporation are mere marketing devices and should never have been authorized"); J. William Callison, *Putting New Sheets on a Procrustean Bed: How Benefit Corporations Address Fiduciary Duties, the Dangers Created, and Suggestions for Change*, 2 AMER. U. BUS. L. REV. 85, 92 (2012) (arguing that the Model Statute "will ultimately discourage corporations from becoming benefit corporations and will discourage outside investment in benefit corporations and consumer validation of the benefit corporation status"); Brian Galle, *Social Enterprise: Who Needs It?,* 54 BOSTON COLLEGE L. REV. 2025, 2041 (2013) (stating "[i]t turns out, though, that the widespread legislative popularity of social enterprise has little to do with its merits. Social enterprise is the product of a race to the bottom"); David Groshoff, *Contrepreneurship? Examining Social Enterprise Legislation's Feel-Good Governance Giveaways*, 16 U. OF PENN. J. OF BUS. LAW 233, 277 (2013) (stating "[t]he material purpose and tax aims of these organizations can be achieved by existing business law structures, particularly because entities created by state law

new freedom to pursue other goals will exacerbate agency costs by interfering with the ability of the market for corporate control to police boards and executives.[14] And the very idea that balancing the needs of other constituencies, such as workers, is a worthy goal is highly controversial.[15] All of which prompts the question: why mess with

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cannot alter the federal taxation schemes relative to invested equity capital and distributions to owners"); Katz & Page, *Sustainable Business*, 62 EMORY L.J. 851, 865 (2013) (arguing that none of the enforcement mechanisms available to participants in benefit corporations are likely to prove successful); Mark Loeweinstein, *Benefit Corporations: A Challenge in Corporate Governance*, 68 BUS. LAWYER 1007, 1011 (2013) (arguing directors of benefit corporations will make suboptimal balancing decisions); Keren Raz, *Toward An Improved Legal Form for Social Enterprise*, 36 N.Y.U. REV. L. & SOC. CHANGE 283, 306 (2012) (criticizing benefit corporations for having an overly broad definition of social mission and because the beneficiaries of a company's social mission cannot sue to enforce it); Dana Brakman Reiser, *Benefit Corporations–A Sustainable Form of Organization?*, 26 WAKE FOREST L. REV. 591, 593 (2011) (the benefit corporation statute does not provide sufficient mechanisms for enforceability of both the profit-seeking and prosocial purposes); Strine, *supra* note 1, at 150 ("[benefit corporations exist in] a fictional land where you can take other people's money, use it as you wish, and ignore the best interests of those with the only right to vote. In this fictional land, I suppose a fictional accountability mechanism will exist whereby the fiduciaries, if they are a controlling interest, will be held accountable for responsibly balancing all these interests").

[14] Galle, *supra* note 13, at 2031 (internal footnotes omitted). Galle expresses this point particularly well:

> Consider next the costs of contracting. There is nothing about running a for-profit business that makes the difficulty of contracting for the production of charitable goods easier, and indeed the opposite is very likely true. Suppose the entrepreneur and her investors jointly agree that they want to divert some of the firm's revenues to the charitable activity. But how much charity will the firm do, at what quality, and at what cost? Now the investors have two worries: that the manager will do too little charity, and also that she will do too much.

Id.; *see also* Groshoff, *supra* note 13, at 277 (stating "[d]espite the ostensible social good inherent in the names ascribed to SEL-related enterprises, these organizations structurally exacerbate equity investors' ability to control corporate agents effectively, thereby leading to less disclosure of agent activity and reduced ownership control capabilities"); Strine, *supra* note 1, at 150.

[15] As Easterbrook and Fischel wrote:

> To sum up: self-interested entrepreneurs and managers, just like other investors, are driven to find the devices most likely to maximize net profits. If they do not, they pay in lower prices for corporate paper. Any one firm may deviate from the optimal measures. Over tens of years and thousands of firms, though, tendencies emerge. The firms and managers that make the choices investors prefer will prosper relative to others. Because the choices do not generally impose costs on strangers to the contracts, what is optimal for the firms and investors is optimal for society.

Easterbrook & Fischel, *The Corporate Contract,* 89 COLUMBIA L. REV. 1416, 1421 (1989); s*ee also* Stephen M. Bainbridge, *Director Primacy: The Means and Ends of Corporate Governance*, 97 NW U. L. REV. 547, 576 (2003) (stating "shareholder wealth maximization is not only the law, but also is a basic feature of corporate ideology"); Stephen M. Bainbridge, *In Defense of the Shareholder Wealth Maximization Norm*, 50 WASH. & LEE L. REV. 1423, 1427-28 (1993) (stating "[d]irectors thus cannot be loyal to both shareholders and nonshareholder success? Why risk Delaware's sterling reputation with the corporate bar and the directorate class by endorsing this untested and controversial new form of business organization? Once we understand Delaware's motives in adopting this new form, we can ask a second, perhaps more important question: will the statute meet Delaware's goals?

To explore these two issues, I will begin with a brief introduction into the history of benefit corporations. Then I will discuss Delaware's motives as revealed by their published documents and by interviews with two of the principal players involved in the benefit corporation legislation. These sources reveal that Delaware was primarily trying to induce social entrepreneurs to register their companies in the state, so to understand whether the statute will be a success. I also discuss the results of interviews I conducted of twenty-five founders or senior executives of benefit corporations about why they chose the benefit corporation form. Then I will examine the extent to which the Delaware statute meets these founders' goals. In the end, I conclude that the statute, while not ideal, does provide a useful new tool to social entrepreneurs, especially when combined with private ordering.

II. HISTORY OF BENEFIT CORPORATIONS

Benefit corporations are largely the invention of B Lab, a nonprofit organization that certifies for-profit companies as "meet[ing] rigorous standards of social and environmental performance, accountability, and transparency."[16] In 2008, B Lab began lobbying state legislatures to persuade them to pass benefit corporation statutes,[17] and it had its first success with Maryland, whose statute became effective in 2010.[18] Four states followed with benefit corporation statutes that became effective in

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constituencies. Rather, their role as stewards requires them to prefer the interests of their shareholder masters"); Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure,* 3 J. FIN. ECON. 305, 311 (1976) (arguing firms have no social responsibility because they are legal fictions, not individuals); Milton Friedman, *The Social Responsibility of Business Is to Increase Its Profits,* N.Y. TIMES, Sept. 13, 1970, § 6 (Magazine), at 33, (opining that directors who pursue their social responsibilities at the expense of corporate profits are spending shareholders' money).

[16] *See What Are B Corps?*, B LAB, http://www.bcorporation.net/what-are-b-corps.

[17] *See Our History*, B LAB, http://www.bcorporation.net/what-are-b-corps/the-non-profit-behind-b-corps/our-history.

[18] *See* Act of Apr. 13, 2010, ch. 97, 2010 MD. LAWS 980, (codified as amended at MD CODE, CORPS. & ASS'NS §§ 5-6C-01 to -08 (2012)); John Tozzi, *Maryland Passes 'Benefit Corp.' Law for Social Entrepreneurs,* BLOOMBERG BUS. WK. (Apr. 13, 2010), https://perma.cc/8MYV-QHZ8.

2011 (New Jersey, Vermont, Virginia, and Hawaii),[19] and five more in 2012 (California, New York, South Carolina, Louisiana, and Massachusetts).[20] Washington's social purpose corporation statute, a close analogue, also became effective in 2012.[21] By the time Delaware's governor signed Delaware's public benefit corporation statute on July 17, 2013,[22] statutes were also effective in Illinois, Pennsylvania, and Washington, D.C., with Arkansas's becoming effective shortly thereafter.[23]

By the time Delaware acted, in other words, the benefit corporation movement had substantial momentum, with over a dozen states having effective statutes, including major commercial states like California, New York, and Illinois. Still, not even all of these states together have the impact on corporate law that Delaware does, at least on large companies. According to the Delaware Division of Corporations, nearly two-thirds of Fortune 500 corporations are incorporated in Delaware, and in 2014, 89% of all corporations that engaged in initial public offerings chose Delaware for their state of incorporation.[24] Delaware carries so much credibility in the corporate law arena that had it chosen to reject the new form, the benefit corporation movement might well have withered and died. Transactional lawyers might have pointed to Delaware's decision as

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[19] Act of July 8, 2011, Act 209, 2011 Haw. Sess. Laws 682 (codified as amended at HAW. REV. STAT. §§ 420D-1 to -13 (2011)); Act of Mar. 1, 2011, ch. 30, 2011 N.J. Laws 324 (codified as amended at N.J. STAT. §§ 14A:18-1 to -11 (2011)); Vermont Benefit Corporations Act, No. 113, 2011 Vt. Acts & Resolves 228 (codified as amended at VT. STAT. tit. 11A, §§ 21.01-.14 (2011)); Act of Mar. 26, 2011, ch. 698, 2011 Va. Acts 1146 (codified as amended at VA. CODE §§ 13.1-782 to -791 (2011)).

[20] Act effective Jan. 1, 2012, ch. 728, § 1, 2011 Cal. Stat. 5636 (codified as amended at Cal. Corp. Code §§ 14600-31 (2012)); Benefit Corporations Law, No. 442, 2012 La. Acts 2218 (codified as amended at LA. STAT. ANN. §§ 12:1801-1832 (2012)); Massachusetts Benefit Corporation Act, ch. 238, § 52, 2012 Mass. Acts 1320 (codified as amended at MASS. GEN. LAWS ch. 156E, §§ 1-16 (2012)); Act effective Feb. 10, 2012, ch. 599, § 3, 2012 N.Y. Laws 1549 (codified as amended at N.Y. BUS. CORP. LAW §§ 1701-09 (2012)); South Carolina Benefit Corporation Act, No. 277, 2012 S.C. Acts 2265 (codified as amended at S.C. CODE ANN. §§ 33-38-110 to -600 (2012)).

[21] *See* Act effective June 7, 2012, ch. 215, 2012 Wash. Sess. Laws 1656 (codified as amended at WASH. REV. CODE §§ 23B.25.005-.150 (2012)).

[22] *See* Act of July 17, 2013, 79 Del. Laws 122 (2013-2014); *see also Governor Markell Signs Public Benefit Corporation Legislation*, DELAWARE.GOV, http://news.delaware.gov/2013/07/17/governor-markell-signs-public-benefit-corporation-legislation (last visited Oct. 6, 2017).

[23] *See* Arkansas Benefit Corporation Act, Act 1388, 2013 Ark. Acts. 5902 (codified as amended at ARK. CODE §§ 4-36-101 to -401 (2013)); Benefit Corporation Act, Pub. Law No. 97-855, 2012 Ill. Law 3916 (2012) (codified as amended at 805 ILL. COMP. STAT. 40/1-1.10 (2013)); Act effective Jan. 22, 2013, No. 2012-152, 2012 Pa. Laws 1228 (codified as amended at 15 PA. CONS. STAT §§ 3301-31 (2017)); Benefit Corporation Act of 2012, No. 19-305, 60 Stat. 2735 (2013) (codified as amended at D.C. CODE §§ 29-1301.01 to -1304.01 (2013)).

[24] *See* DELAWARE DIVISION OF CORPORATIONS, *supra* note 12.

grounds to avoid the new form, and investors and entrepreneurs might reasonably have regarded it with much greater suspicion.

Delaware's impact can be seen in the effect its blessing had on states' decisions. While it took four years for fifteen states to authorize some version of the benefit corporation before Delaware acted, it took only about half that time to double the number once Delaware passed its version.[25]

As of this writing, thirty-five states have passed some form of the benefit corporation statute, plus the District of Columbia.[26] These states cross traditional party divides, encompassing both blue states (such as California and New York) and red states (such as Louisiana and Arkansas). Similarly, the states that have not yet adopted the new form include blue states such as Maine and red states, such as Alabama, and Wyoming.[27] According to B Lab, six more states are working on enabling legislation,[28] including Iowa, which introduced legislation this year.[29]

Although benefit corporations are proving enormously popular with state legislatures, it is less clear that they are finding a receptive audience among entrepreneurs. It is not possible to be certain of the precise number of benefit corporations, since many states are not categorizing them separately. But a few scholars have attempted to count them over the past few years, and B Lab also tries to track them. Based on the data we have, the numbers are fairly anemic. There were approximately 1.1 million legal entities registered in Delaware at the end of 2014,[30] yet fewer than 300 of these were active public benefit corporations.[31] Other states have similarly small numbers. As of April of 2015, Nevada had the most, with 675, followed by Oregon with 403 and Colorado with 230.[32] New York had only 139 and California 118.[33]

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[25] *See State by State Status of Legislation*, BENEFIT CORP., http://benefitcorp.net/policymakers/state-by-state-status (last visited Oct. 9, 2017) (identifying the states that have enacted forms of benefit corporation statutes).

[26] *See id.* As of this writing, B Lab's website did not yet include Wisconsin, which enacted its benefit corporation statute in November of 2017. *See* 2017 Wisconsin Act 77.

[27] *See id.*

[28] *See id.* Note that B Lab does not count Washington's statute, although Washington's social purpose corporation is very similar to a benefit corporation. *See* WASH. REV. CODE §§ 23B.25.005-.150 (2012).

[29] *See* H.B. 62, 87th Gen. Assemb., Reg. Sess. (Iowa 2017); S.B. 221, 87th Gen. Assemb., Reg. Sess. (Iowa 2017).

[30] *See* DELAWARE DIVISION OF CORPORATIONS, *supra* note 12.

[31] *See* Ellen Berrey, *How Many Benefit Corporations are There?*, SSRN.COM (May 5, 2015) https://ssrn.com/abstract=2602781. These numbers are a minimum count due to underreporting by states.

[32] *See id*.

[33] *See id*.

While the absolute number of benefit corporations is still rather small, the growth rate is impressive. In July of 2013, when Delaware had just passed its public benefit corporation statute, there were about 251 benefit corporations in the entire country.[34] By April of 2015, the total number had grown to 2,144.[35] By January of 2016, B Lab's head of legal policy, Rick Alexander, claimed that there were over 3,000,[36] representing nearly a twelve-fold increase in just 30 months. If that rate continues, in five years there could be over 400,000 benefit corporations.

At this point, any statement about the future popularity of benefit corporations is highly speculative. Benefit corporation statutes are too new to judge their likely success. Still, while a projection of 400,000 benefit corporations in just five years is almost certainly too optimistic, there is good reason to think a meaningful demand will develop as entrepreneurs and their lawyers and investors grow more familiar with the new form. Limited liability companies' early growth was uneven as well, yet the LLC ultimately became an enormously successful form of business organization.[37]

Nationally, benefit corporations are experiencing exponential growth, despite the fact that they are new and unfamiliar. One entrepreneur I interviewed told me her lawyer (a partner at a major firm) actually threatened to fire her as a client if she insisted on using a benefit corporation for her business. Yet the entrepreneur persevered, and her lawyer ultimately acquiesced and helped her create a benefit corporation for her business. Perhaps other entrepreneurs will be similarly successful in pushing for this new form.

Like other benefit corporation statutes, Delaware's makes some changes and additions to the ordinary, for-profit corporation statute. Any features unchanged by the benefit corporation statute remain the same as in ordinary, for-profit corporations.

Delaware chose not to adopt B Lab's model statute. Since Delaware corporate law has historically been enormously influential on the other

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[34] Haskell Murray, *How Many Benefit Corporations Have Been Formed?*, SOCENT L.: BENEFIT CORP. ARCHIVES (July 23, 2013), http://socentlaw.com/2013/07/how-many-benefit-corporations-have-been-formed/. This number included Maryland benefit LLCs, but excluded any corporations in New Jersey or South Carolina for lack of data. *Id.*

[35] *See* Berrey, *supra* note 30.

[36] *See* Nicole Fallon, *Becoming a Benefit Corporation: Is it Right for Your Business?*, BUS. NEWS DAILY (Jan. 22, 2016 8:45am), http://www.businessnewsdaily.com/8734-benefit-corporation.html.

[37] *See* William J Carney, *Limited Liability Companies: Origins and Antecedents*, 66 U. COLO. L. REV. 855, 858 (1995); Bruce H. Kobayashi & Larry E. Ribstein, *Evolution and Spontaneous Uniformity: Evidence from the Evolution of the Limited Liability Company*, 34 ECON. INQUIRY 464, 472-73 (1996); Larry E. Ribstein, *Statutory Forms for Closely Held Firms: Theories and Evidence From LLCs*, 73 WASH. U. L. Q. 369, 430-31 (1995).

states, I will focus on Delaware's statute in this essay. But I will occasionally note where Delaware differs materially from B Lab's model and that contrast seems instructive.

One difference that is important to understand at the outset is the entity's title. B Lab (and most states) use the term "benefit corporation,"[38] while Delaware employs the term "public benefit corporation" (which I shall refer to as a "PBC").[39] Delaware's term may cause some confusion, as some states, such as California, use this term to refer to nonprofit corporations.[40]

III. DELAWARE'S MOTIVES

Now that we have a good sense of the historical context for Delaware's adoption of PBCs, we are ready to examine Delaware's motivations. Delaware already had a successful formula before adopting PBC legislation: it was the leading state for corporate law and the state of choice for incorporations, especially for public companies.[41] The benefit corporation is a new, largely untested idea that has been received with substantial skepticism by corporate law scholars.[42] Why then, did the Delaware Legislature feel the need to risk its credibility by adopting a benefit corporation statute?

While it is difficult to ascribe with certainty a particular purpose to a legislative process that involves so many individuals, each of whom may have had their own ideas about why PBCs would benefit Delaware, we can gain a reasonably good sense of what the state had in mind from official statements and interviews of some of the players.

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[38] *See* B Lab, *The Model Legislation*, BENEFITCORP.NET http://benefitcorp.net/attorneys/model-legislation (last visited on October 15, 2017).

[39] *See* DEL. CODE ANN. tit. 8, § 361 (2013).

[40] *See* CAL. CORP. CODE § 5110 (1980).

[41] *See generally* Lewis S. Black, Jr., DEL DEP'T OF STATE, DIV. OF CORPS., WHY CORPORATIONS CHOOSE DELAWARE (2007) (arguing, *inter alia*, that Delaware's position as the United States premier venue for incorporation is a product of the General Assembly's continued efforts to maintain the relevance of the Delaware General Corporation Law as well as the respect the Delaware Court of Chancery has earned by the corporate community at large).

[42] *See*, *e.g.*, Steven D. Solomon, *Idealism That May Leave Shareholders Wishing for Pragmatism*, N.Y. TIMES, Oct. 14, 2015, at B5 (opining that PBCs face unique hurdles including how to define fiduciary duties relating to creating a profit for shareholders versus benefitting the stated social purpose and questioning the need for PBCs when for-profit entities "make donations and support causes all the time" under existing law); David Feldman, *Benefit Corporations: Profit While Doing Good, But Worthwhile?*, DAVID FELDMAN BLOG, Sept. 16, 2014, http://www.davidfeldmanblog.com/benefit-corporations-profit-while-doing-good-but-worthwhile (opining that the lack of special tax benefits for PBCs "may [present a challenge] to draw people into the concept").

Delaware Governor Jack Markell issued a statement upon signing the bill authorizing PBCs. He said:

> We've all heard about corporations wanting to "do well" while also "doing good." With this new law, Delaware corporations will now have the ability to build those dual purposes into their governing documents. We have heard repeatedly that public benefit corporations can fill a market need. But just as important, they will also fill a societal need.[43]

Governor Markell cited two purposes for passing the PBC legislation: to allow corporations to institutionalize a social purpose, thereby helping the public, and to fill market demand for a form of business organization that permits this.

The legislators who sponsored the PBC legislation echoed similar themes. The leading sponsor of the bill in the Delaware Senate, Senator David Sokola, stated "I'm proud that Delaware now has a corporate vehicle to offer business leaders and investors that want to create value that extends well beyond owners and managers to society and the public as a whole."[44] Senator Sokola, like Governor Markell, indicated that he had two related goals in championing the PBC legislation: to offer entrepreneurs a business form they desire and to assist them in helping the broader society.

Similarly, Representative Byron Short, who co-sponsored the PBC bill, stated, "I'm happy to have co-sponsored this law which because of our State's unique role in Corporate America will make benefit corporations a viable option for entrepreneurs and investors in Delaware and throughout the nation."[45] Representative Short also seemed concerned with providing a form of business organization that entrepreneurs wanted, lending Delaware's credibility and its legal institutions to the benefit corporation form of business organization.

The official press release issued by the Governor's office upon the PBC bill's signing listed some more specific goals within the same two themes. It stated, "[t]his new corporate structure helps businesses combat short-termism, attract talent and customers, and accelerate the growth of a big investment opportunity to meet the needs of people who want to both make money and make a difference."[46] Again, we see the theme of meeting the needs of social entrepreneurs, but here there is also a hint of

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[43] *Governor Markell Signs Public Benefit Corporation Legislation*, *supra* note 22.
[44] *Id.* at 9.
[45] *Id.*
[46] *Id.*

advocacy, making the claim that PBCs will assist entrepreneurs in achieving their pecuniary goals as well as their charitable ambitions. According to the press release, PBCs will attract and retain talented employees better than traditional for-profit corporations do and will also draw customers who might not patronize an ordinary for-profit. The press release does not cite any evidence for these claims.

Delaware corporate statutes, unlike most legislation, often originate not with the legislature but with a committee of the Delaware State Bar Association: the Corporation Law Council of the Corporation Law Section ("the Council"). The PBC legislation followed this pattern.[47] I therefore interviewed Frederick "Rick" Alexander, who chaired the Council when it was considering and drafting the benefit corporation statute.[48] At the time, Mr. Alexander was a partner at Morris, Nichols, Arsht & Tunnell LLP, a leading corporate law firm in Delaware.[49] He has since become Head of Legal Policy at B Lab.[50] Mr. Alexander has also written about the history of the Council's decision to adopt benefit corporation legislation in the introduction to his book, *The Public Benefit Corporation Guidebook: Understanding and Optimizing Delaware's Benefit Corporation*.[51] Mr. Alexander spoke only for himself, not the Council, but was often able to provide his impression of the Council's views.

Mr. Alexander ultimately shared Governor Markell's two goals in adopting benefit corporation legislation, though he was quite skeptical when B Lab first approached the Council. The Council's initial view was that corporate law already functioned quite well, and that the best way to restrain corporate conduct that had a negative impact on society or the environment was through direct regulation, not by tinkering with corporate governance law.[52] The Council was eventually persuaded, however, after B Lab introduced the members to entrepreneurs, businesses, and investors who desired to organize their companies as benefit corporations.[53] The Council concluded that Delaware ought to offer businesses the flexibility to adopt social goals.[54]

Some members of the Council – and these include Mr. Alexander – also came to believe that benefit corporations could influence all

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[47] *See* ALEXANDER, *supra* note 8, at 8-9.
[48] *See id.* at 8.
[49] *See id.*
[50] *See id.* at 9.
[51] *See* ALEXANDER, *supra* note 8, *at 8-9*.
[52] *Id.* at 9.
[53] *See* Telephone Interview with Frederick H. Alexander (Mar. 15, 2016).
[54] *Id.*

corporations to operate more sustainably and responsibly.[55] Mr. Alexander was greatly influenced by the respective work of two scholars, Lynn Stout and Colin Meyer, and by institutional investors' tendency to diversify their investments by owning stock in many or even all publicly traded companies.[56] He concluded:

> I remain convinced that the for-profit corporation remains the best vehicle for raising and allocating capital (other than for certain public goods that remain the responsibility of government and NGOs). However, given the challenges that our planet and society face, I also believe we must look for a way to allow that vehicle to operate with a recognition of the interdependence of our complex globe, and the responsibility that follows. The benefit corporation provides such a path.[57]

To gain additional perspective on the Council's views, I also interviewed Council Member Professor Lawrence Hamermesh. Although, like Mr. Alexander, Professor Hamermesh spoke only for himself, and not the Council, he is a prominent scholar of corporate law and is highly respected in corporate legal circles. His views were therefore likely very influential. Professor Hamermesh was the Ruby R. Vale Professor at Widener University's Delaware Law School, where he taught corporate law, and has been a member of the Council since 1995.[58] He served as Chair of the Council from 2002-2004.[59]

Professor Hamermesh said he believed the primary purpose of passing the PBC statute was to provide another option to businesses that wanted it. He did not think there was a significant cost to providing an additional form, especially since investors who wanted a business form that permitted them to foster goals other than maximizing wealth for the owners could do so through a limited liability company. He stated:

> The public benefit corporation statute is very much in the mold of the enabling approach that characterizes all of the

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[55] *See id.*; ALEXANDER, *supra* note 8, at 9-10.

[56] *See* ALEXANDER, *supra* note 8, at 9-10, discussing COLIN MAYER, FIRM COMMITMENT: WHY THE CORPORATION IS FAILING US AND HOW TO RESTORE TRUST IN IT (2013) and LYNN STOUT, THE SHAREHOLDER VALUE MYTH: HOW PUTTING SHAREHOLDERS FIRST HARMS INVESTORS, CORPORATIONS, AND THE PUBLIC (2012).

[57] *See* ALEXANDER, *supra* note 8, at 10.

[58] WIDENER UNIVERSITY DELAWARE LAW SCHOOL BIO OF LAWRENCE A. HAMERMESH, http://delawarelaw.widener.edu/current-students/faculty-directory/faculty/112/ (last visited Oct. 14, 2017).

[59] *Id.*

> Delaware business entity statutes. This is just saying that here's another form that – if the participants want to embrace it – they can. It's got certain constraints, it is a corporation, a corporation with a somewhat different model in terms of purpose, but it's there on the shelf ready for people to take it down and use it if they want to. [60]

Professor Hamermesh believed there was demand for the new form but was not especially troubled by criticisms that investors might be reluctant to invest in an entity that diverted some of its resources to nonshareholder constituencies. He replied to this criticism by saying, "[i]f you believe investors ought to have the prerogative of choosing the form that suits them, we've built it and either they'll come or they won't."[61]

Professor Hamermesh acknowledged that Governor Markell may have also had the goal of furthering social goals by harnessing the power of private enterprise. But he told me that for him, the primary motivation was to provide a form that some investors wanted. He said, "I think what really did it for me was that I was hearing from investors who said they really want this vehicle and when you hear that it's a little hard to say, well no, we'd rather not give it to you when we're prepared to say you can take an LLC and do it anyhow."[62]

Delaware's two purposes in passing PBC legislation are intertwined. The goal of aiding society can only be met if entrepreneurs choose to adopt PBCs (and if PBCs empower entrepreneurs to aid society). Similarly, the goal of filling a market need can only be met if socially-minded entrepreneurs find the PBC legislation amenable to their purpose.

For the PBC legislation to meet Delaware's goals, then, it is critical that it fulfill the needs of social entrepreneurs. As a theoretical matter, one can imagine a wide and diverse set of motivations for social entrepreneurs to want a specialized form of business organization. Founders might select a PBC in hopes that it will help the business appeal to an important group such as customers, employees, for-profit investors, foundations, or donors, or to signal a dual purpose for some other reason ("Brand"). They might also choose a PBC because of its ability to distribute profits to owners ("Earn"), something a nonprofit cannot do; because of its regulatory simplicity as compared to a nonprofit ("Simplify"); because it might serve to push managers to adopt prosocial policies that will also help improve profitability ("Manage"); or because

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[60] *See* Telephone Interview with Lawrence Hamermesh (March 11, 2016).
[61] *Id.*
[62] *Id.*

the hybrid form may provide greater protection against hostile acquisitions ("Keep").

These are all pecuniary motives for choosing a PBC, but founders may also choose a PBC for purely idealistic motivations, because they believe that businesses should strive to do more than earn profits for their owners. Founders may believe that businesses have a moral obligation to aid their employees, communities, customers or other corporate constituencies even when doing so will reduce the company's profits. They may wish to adopt a business form that expresses these ideals and perhaps inspires others to follow their example ("Express"). Similarly, the founders may want to shield themselves from liability for adopting prosocial policies that reduce earnings, thereby encouraging such policies ("Protect") or to ensure that the company continues to embody their values even after they lose control to their heirs or to eventual buyers ("Endure").

These eight goals are not mutually exclusive. A company's founders might well want to achieve several of these goals or even all of them. Nevertheless, it seems likely (and interviews with social entrepreneurs bear out this theory) that most social entrepreneurs will have one or two of these goals primarily in mind when opting for a PBC, though some or all of the others may provide a subsidiary motivation. Delaware seems to have focused on Brand, a desire to attract and retain employees, customers and investors, and to a lesser degree on Express, a sincere desire to pursue a social mission.

To learn which of these goals loom largest in the minds of social entrepreneurs, I interviewed founders or senior executives of twenty-five benefit corporations and asked them why they chose the benefit corporation as the legal entity for their business. This was not intended as a statistically valid study. The subjects were not chosen at random but rather based on my ability or my research assistant's ability to find them and on their willingness to be interviewed.[63] The interview subjects do not represent a statistically valid sample, and their companies are registered in many different states, not just Delaware. This was a qualitative empirical study, not a quantitative one.[64] Its purpose was to gather a sense of company founders' rationale for choosing this new form.

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[63] *See* DELBERT C. MILLER AND NEIL J. SALKIND, HANDBOOK OF RESEARCH DESIGN AND SOCIAL MEASUREMENT 192 (6th ed. 2002) (stating subjects are generally not randomly selected in qualitative research).

[64] *Id.* at 143 (stating "[q]ualitative research methods are often used when the scientist is interested in obtaining detailed and rich knowledge of a specific phenomenon"). Qualitative research has been defined as follows:

> Qualitative research is a situated activity that locates the observer in the world. It consists of a set of interpretive, material practices that makes the world visible. These practices . . . turn the world into a series of

Delaware's stated goals are broadly shared by the social entrepreneurs I interviewed. The goal entrepreneurs cited most was express: an ideology or social mission, a sense that businesses should be about more than money. The majority of the entrepreneurs communicated a belief that companies should care about the welfare of their employees, the environment, and the broader impact they have on society and should sometimes sacrifice profit to pursue these other goals. Representatives of nineteen of the twenty-five companies I contacted mentioned this as one of the reasons they chose the benefit corporation form.

The vast majority of the entrepreneurs cited the Express goal in its purely communicative, non-pecuniary sense. For many, the choice of form was important mostly for its ability to express their values, often with the hope of persuading others to adopt them. Entrepreneurs wanted to demonstrate their commitment to running their companies in accordance with their ethical values and in the way they believed all companies should be run, separate and apart from any tangible benefit the form might convey.

Relatedly, nearly half the entrepreneurs cited Protect, the protection from liability benefit corporations provide to officers and directors who choose to prioritize a social mission over profit. The thrust of the entrepreneurs' concern here seemed to be permissive; that is, they wanted this protection so that they could operate their companies in accordance with their social values, free from worry that their investors would sue them for sacrificing profit for the social good. Many cited the example of Ben & Jerry's, the famously progressive ice cream maker that sold itself to Unilever, the multinational consumer goods conglomerate.[65]

The commonly told story is that Ben & Jerry's founders, Ben Cohen and Jerry Greenfield, wanted to retain ownership but felt that their duties to their public shareholders required them to sell.[66] Although some

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> representations including fieldnotes, interviews, conversations, photographs, recordings, and memos to the self. At this level, qualitative research involves an interpretive, naturalistic approach to the world. This means that qualitative researchers study things in their natural settings, attempting to make sense of, or to interpret, phenomena in terms of the meanings people bring to them.

QUALITATIVE RESEARCH PRACTICE: A GUIDE FOR SOCIAL SCIENCE STUDENTS 2-3 (Jane Ritchie & Jane Lewis eds., 2003) (quoting DENZIN AND LINCOLN, HANDBOOK OF QUALITATIVE RESEARCH 3 (2d ed. 2000)).

[65] *See, e.g.,* Constance L. Hays, *Ben & Jerry's to Unilever, With Attitude*, N.Y. TIMES, April 13, 2000, http://www.nytimes.com/2000/04/13/business/ben-jerry-s-to-unilever-with-attitude.html.

[66] *See* Jenna Lawrence, *Making the B List*, Stanford Social Innovation Review (Summer 2009), http://ssir.org/articles/entry/making_the_b_list (arguing that Cohen and Greenfield did not want to sell the company but had no choice because it was public).

have argued that Cohen and Greenfield did not have an obligation to sell the company,[67] and Unilever has arguably not only allowed Ben & Jerry's to continue to pursue its social values but has adopted some of these values itself,[68] the concern that a socially conscious company would be forced to sell itself to a buyer and abandon its social mission in the process plagues the social entrepreneurship movement. Benefit corporations offer entrepreneurs the legal authority to reject buy-out offers that would harm their social mission or non-shareholder constituencies such as employees by requiring them to balance these interests with those of shareholders.[69]

In addition to the Express motivation, the social entrepreneurs often also mentioned pecuniary rationales for choosing a benefit corporation, or at least appreciated that the form conferred pecuniary benefits even if they were not the rationale that drove the decision. In particular, they often cited versions of the Brand motivation. Over fifty percent of the entrepreneurs said that they had an easier time recruiting and/or retaining employees because of their social mission, and a similar percentage said they were better able to attract customers.

It is important to note, however, that it seems to have been the social mission itself that was instrumental in conferring these pecuniary benefits, rather than the company's status as a benefit corporation. The entrepreneurs expressed some frustration that neither audience (employees or customers) knew very much about benefit corporations and often had not even heard of the form. Once the entrepreneurs explained that being a benefit corporation meant making an enforceable, transparent commitment to the social mission, however, employees and customers reacted very favorably. The entrepreneurs frequently expressed hope that as benefit corporations became more widely known, these pecuniary benefits would come without the need to educate the target audiences.

Entrepreneurs were far less likely to claim that their company's status as a benefit corporation (or PBC) was helping them to attract outside investors. Only about a quarter of the entrepreneurs felt that their entity status was helpful in this regard, and few of these had actually secured significant capital from investors whose decision was heavily influenced by their choice of entity. Some had had conversations with investors

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[67] *See* Antony Page & Robert A. Katz, *Freezing Out Ben & Jerry: Corporate Law and the Sale of a Social Enterprise Icon*, 35 VT. L. REV. 211, 231 (2010).

[68] *See* David Gelles, *How the Social Mission of Ben & Jerry's Survived Being Gobbled Up*, N.Y. TIMES, Aug. 21, 2015, http://www.nytimes.com/2015/08/23/business/how-ben-jerrys-social-mission-survived-being-gobbled-up.html.

[69] *See* DEL. CODE ANN. tit. 8, § 365 (2013) (directing boards of PBCs to balance the interests of shareholders against the company's social mission and the interests of other corporate constituencies, and permitting companies to include a provision in their articles of incorporation protecting directors from liability for any disinterested failure to balance these interests appropriately).

where the entity status had seemed a bonus factor, while others just anticipated that it would be. On the other hand, some entrepreneurs expressed concern that investors, especially very large investors, would have hesitations about the form. These concerns did not take the shape critics have generally anticipated, that the company's mission would soak up resources and reduce investors' financial return, but rather centered on the form's unfamiliarity to investors and their counsel. The concerns, in other words, generally mirrored those investors have had with limited liability companies and had little to do with the prosocial aspects of benefit corporations or PBCs.[70]

Delaware's focus seems to have been on why entrepreneurs might choose a PBC over a traditional for-profit corporation, but for social entrepreneurs, often the strongest competitor to the PBC is actually a nonprofit corporation. Nonprofits can be complex to set up and maintain, especially for those desiring 501(c)(3) status.[71]

Benefit corporations are comparatively simple, though they do not offer the same tax advantages. Sixteen percent of the social entrepreneurs I interviewed cited this explanation for avoiding nonprofit status. A smaller percentage, alternatively, cited governance weaknesses perceived in nonprofits or concerns about the sustainability of an enterprise that depends on donations to survive. Only one entrepreneur cited both the complications of a nonprofit corporation and sustainability concerns; there was otherwise no overlap among these responses.

IV. DOES THE STATUTE MEET DELAWARE'S GOALS?

We saw in Part II that Delaware's dominant goal was to meet the needs of entrepreneurs and investors who wanted their businesses both to pursue social goals and to earn a profit. Secondarily, at least some Delaware actors also wanted to harness the power of capitalism to achieve

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[70] Entrepreneurs often incorporate, rather than form an LLC, in large part because of investors' greater familiarity with the corporate form, despite the potential tax advantages of the LLC. As Victor Fleischer has written:

> [T]he uncertainty of the LLC form increases legal costs and is an unwelcome addition to a negotiating atmosphere already laden with uncertainty and distrust. In particular, entrepreneurs who are accustomed to running corporations might resist trying out a new and unfamiliar entity. For start-ups that hope to incorporate within a few years anyway, adding an extra layer of legal costs, complexity, and uncertainty is unappealing, creating another reason why entrepreneurs and venture capital professionals prefer the C corp structure.

Victor Fleischer, *The Rational Exuberance of Structuring Venture Capital Start-Ups*, 57 TAX. L. REV. 137, 175 (2004).

[71] Corporations that qualify under 26 U.S.C. § 501(c)(3) are exempt from taxation, and donations to such entities are tax deductible to the donor.

social ends. These goals are interrelated but not synonymous. To meet the first goal, the statute must provide a form that helps entrepreneurs pursue their various ambitions. Those included protection from liability when sacrificing profits for social ends; helping to attract or retain investors, customers, and employees; and expressing entrepreneurs' ideals and inspiring others to follow them. Meeting Delaware's second goal requires legal mechanisms that encourage or even require companies to aid society. Delaware's PBC statute on its own only partially fulfills the state's two goals, but the remaining gaps might largely be filled by private ordering.

A. Meet Entrepreneurs' Needs

Delaware's primary goal in passing its PBC statute was to provide flexibility to those social entrepreneurs and investors who wanted a legal form that would permit them to pursue social goals alongside profits. Interviews with social entrepreneurs, however, revealed that their goals were multi-textured. Some entrepreneurs wanted liability protection that would enable them to choose to trade off profits for the social good when they so desired, especially in the context of a sale of the company. Others had pecuniary goals at least partially in mind, hoping that their social mission would help to attract and retain customers, employees, and/or investors. The majority's overarching ambition, though, was idealistic in nature. These social entrepreneurs wanted a legal form that expressed their values and hopefully inspired other entrepreneurs and investors to imitate their prosocial business strategies. The PBC statute does permit social entrepreneurs to achieve the Protect goal; the default rules alone, however, may prove inadequate. The statute does only a mediocre job of effecting the Brand and Express goals, but private ordering has the potential to improve matters.

1. Protect

Delaware's for-profit corporation statute does not expressly state that directors owe fiduciary duties to the corporation and can therefore suffer liability for breaching them, as by sacrificing profits for a social goal. Delaware's courts, however, have long recognized that directors owe their corporations fiduciary duties.[72] Some decades ago, the Delaware

[72] *See, e.g.*, Loft, Inc. v. Guth*,* 2 A.2d 225, 238 (Del. Ch. 1938) (stating "the directors of a corporation stand in a fiduciary relation to the corporation and its stockholders"), *aff'd*, 5 A.2d 503 (Del. 1939); Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985) (stating "[i]n carrying out their managerial roles, directors are charged with an unyielding fiduciary duty to

legislature implicitly recognized fiduciary duties' existence by passing section 102(b)(7).[73] That section permits corporations to exempt directors from personal liability for breaches of their duty of care, but not of their duties of loyalty or good faith.[74] By permitting corporations to exempt directors from liability for violating some of these duties, the statute implicitly acknowledges that these duties exist and that directors might be liable for violating them in the absence of a section 102(b)(7) provision in a corporation's certificate. The statute does not define fiduciary duties, leaving the courts free to continue to articulate their scope.[75]

Delaware's PBC statute does not define traditional fiduciary duties either, but it does state that directors must balance shareholder wealth maximization against the interests of other corporate constituencies. Section 365(a) states as follows:

> The board of directors shall manage or direct the business and affairs of the public benefit corporation in a manner that balances the pecuniary interests of the stockholders, the best interests of those materially affected by the corporation's conduct, and the specific public benefit or public benefits identified in its certificate of incorporation.[76]

The balancing requirement imposed by section 365 may be interpreted as a separate duty, but it seems most likely to be read as a modification of directors' duty of care. In a for-profit corporation, the duty of care requires directors to exercise ordinary prudence in managing the business affairs of the corporation.[77] While normally directors must take care to maximize shareholder wealth, in a PBC their duty of care morphs to pursue the interests of additional constituencies as well.[78]

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the corporation and its shareholders"), *overruled on other grounds by* Gantler v. Stephens, 965 A.2d 695 (Del. 2009).

[73] DEL. CODE ANN. tit. 8, § 102(b)(7) (2015).

[74] *Id.* Although the statute speaks separately of the duties of loyalty and good faith, the Delaware Supreme Court has held that the duty of good faith is a subset of the duty of loyalty. *See* Stone *ex rel.* AmSouth Bancorporation v. Ritter, 911 A.2d 362, 369-70 (Del. 2006).

[75] *See, e.g.,* Brehm v. Eisner, 746 A.2d 244 (Del. 2000); Broz v. Cellular Information Systems, Inc., 673 A.2d 148 (Del. 1996); *Van Gorkom*, 488 A.2d at 872; Sinclair Oil v. Levien, 280 A.2d 717 (Del. 1971); and *In re* Caremark International Derivative Litigation, 698 A.2d 959 (Del. Ch. 1996).

[76] DEL. CODE ANN. tit. 8, § 365(a) (2013).

[77] *See In re* Walt Disney Co. Deriv. Litig., 907 A.2d 693, 749 (Del. Ch. 2005) (stating "[t]he fiduciary duty of due care requires that directors of a Delaware corporation 'use that amount of care which ordinarily careful and prudent men would use in similar circumstances . . '") (quoting Graham v. Allis-Chalmers Mfg. Co., 188 A.2d 125, 130 (Del. Ch. 1963)).

[78] § 365.

The statute not only describes the duty, it also specifies what directors must do to satisfy it and avoid liability. Directors can fulfill their duty to balance the interests of the various corporate constituencies and the specific public benefit elected by informing themselves, remaining disinterested in each decision, and avoiding decisions that "no person of ordinary, sound judgment would approve."[79]

This standard resembles that of the business judgment rule, which governs liability for breaches of the duty of care in for-profit corporations, in the requirements to be informed and disinterested,[80] but seems more stringent in its substantive component. While the business judgment rule requires only that informed and disinterested directors who are acting in good faith avoid wasting corporate assets and making irrational decisions,[81] section 365(b) seems to impose liability for decisions that are merely unreasonable.[82]

So far, Delaware's PBC statute has granted directors permission to pursue other goals at the expense of profit, seemingly fulfilling the Protect goal. But at the same time, the PBC statute has potentially expanded

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[79] § 365(b).

[80] As the Delaware Supreme Court held:

> The judicial presumption accorded director and board action which underlies the business judgment rule is "of paramount significance in the context of a derivative action." As *Aronson* states, the presumption may only be invoked by directors who are found to be not only "disinterested" directors, but directors who have both adequately informed themselves before voting on the business transaction at hand *and* acted with the requisite care.

Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 367 (Del. 1993) (quoting Aronson v. Lewis, 473 A.2d, 804, 812 (Del. 1984)) (internal citations omitted).

[81] The Delaware Supreme Court has explained:

> As for the plaintiffs' contention that the directors failed to exercise "substantive due care," we should note that such a concept is foreign to the business judgment rule. Courts do not measure, weigh or quantify directors' judgments. We do not even decide if they are reasonable in this context. Due care in the decision-making context is *process* due care only. Irrationality is the outer limit of the business judgment rule. Irrationality may be the functional equivalent of the waste test or it may tend to show that the decision is not made in good faith, which is a key ingredient of the business judgment rule.

Brehm v. Eisner, 746 A.2d 244, 264 (Del. 2000) (internal citations omitted).

[82] Oddly, the statute does not impose a good faith requirement, as the business judgment rule does, though bad faith decisions would presumably also flunk the "unreasonable" test. *See* McMullin v. Beran, 765 A.2d 910, 916 (Del. 2000) (stating "[t]he business judgment rule 'is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company.'"), *quoting Aronson,* 473 A.2d at 812. Bad faith (or lack of good faith) includes two categories of behavior: subjective bad faith (an actual intent to harm the corporation), and a conscious disregard for one's responsibilities. It does not include gross negligence. *See In re Walt Disney Co. Derivative Litig.*, 906 A.2d at 64-67 (Del. 2006).

directors' liability, rather than limiting, it by not only granting permission but also imposing a *duty* to consider these other interests. This duty undermines the Protect goal but may serve other goals, such as Brand and Express, by making the selection of PBC status more meaningful. Directors threatened with liability for failing to take other corporate constituencies into account seem more likely to take care to do so. The unreasonability standard hardly seems stringent, but even a very small chance of personal liability may shape risk-averse directors' behavior, especially if they do not share all the gain for their decisions to favor profits yet bear the entire risk of liability for doing so.

This additional risk of liability can be eliminated, though, by a provision in the certificate of incorporation. The statute permits corporations to add language in the certificate that any disinterested failure to satisfy the balancing requirement will not count as a breach of the duties of loyalty or good faith and can therefore be exempted from liability with a section 102(b)(7) provision in the certificate.[83] Corporations without such a provision, however, will expose their directors to some risk of liability for making uninformed, or unreasonable balancing decisions, and corporations cannot protect their directors from liability for making interested balancing decisions.

Even these risks are limited, however, by the statute's enforcement mechanism. The Delaware corporation's statute does not expressly provide shareholders with a right to launch a claim in the corporation's name, a "derivative suit." The only mention of derivative suits in the statute comes in section 327, which establishes the contemporaneous ownership requirement: the shareholder plaintiff in a derivative action must allege in the complaint that she or he was a shareholder at the time of the contested action and remained a shareholder throughout the suit.[84]

The Delaware Chancery Court rules also regulate derivative suits without formally authorizing them. Rule 23.1 reiterates the continuous ownership rule, mandates that the plaintiff set forth in the complaint the steps taken to encourage the board to redress the concern or explain why such steps would be futile, forbids the shareholder plaintiff from receiving any compensation for serving as the lead plaintiff, and requires court approval for any settlement.[85]

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[83] *See* § 365(c).
[84] *See* DEL. CODE ANN. tit. 8, § 327 (1998).
[85] *See* DEL. CHANCERY COURT RULE 23.1.

Both the statute and the Rules, then, assume that shareholders may launch derivative actions but do not expressly authorize them to do so. That authority comes only from common law.[86]

In contrast, the PBC statute states that a shareholder or group of shareholders who owns at least 2% of the company's outstanding shares may launch a derivative action to enforce the directors' duties to balance the interests of shareholders against those of other corporate constituencies and the public interest(s) chosen by the PBC.[87] Unlike the general corporation statute, the PBC statute expressly establishes a right to bring a derivative action.

It is unclear whether the statute was meant to incorporate the other rules that govern derivative claims in traditional for-profit corporations such as the demand requirement and the contemporaneous ownership rule. The PBC statute does refer to this type of action against directors as "derivative," which may indicate an intent to import the other rules for derivative actions. On the other hand, the Delaware Legislature might have intended to create a special proceeding unique to PBCs that was exempt from these rules. Section 361 states that a PBC "shall be subject in all respects to the provisions of this chapter, except to the extent this subchapter imposes additional or different requirements, in which case such requirements shall apply."[88] But that rule just begs the question of whether the cause of action authorized by section 367 for PBCs "imposes additional or different requirements."

The legislative history is silent on the question,[89] but the fact that the statute expressly authorizes suit by a shareholder who meets the ownership requirements on the day of suit strongly suggests that the shareholder did not need to own stock on the date of the board's alleged violation.[90] The shareholder plaintiff must likely maintain ownership of at least some stock throughout the suit in order to meet the constitutional "case or controversy" requirement, but it is far from clear whether the

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[86] *See* Parfi Holding AB v. Mirror Image Internet, Inc., 954 A.2d 911, 941 n.113 (Del. Ch. 2008) (stating "[d]erivative actions are a creature of common law, not statute"); *but see* Flynn v. Bachow, 1998 Del. Ch. LEXIS 181, at *24 n.23 (stating "[t]he right to bring a derivative suit is a right created by statute within the limited partnership statutory scheme. Limited partnerships are statutory creatures not existing at common law").

[87] *See* DEL. CODE ANN. tit. 8, § 367 (2013).

[88] *Id.,* DEL. CODE ANN. tit. 8, § 361 (2013).

[89] *See* S.B. 47, 147th Gen. Assemb. (Del. 2013-2014), Act of July 17, 2013, 79 Del. Laws 122 (2013-2014).

[90] *See* § 367 (stating "[s]tockholders of a public benefit corporation owning individually or collectively, *as of the date of instituting such derivative suit*, at least 2% of the corporation's outstanding shares . . . may maintain a derivative lawsuit to enforce the requirements set forth in § 365(a) of this title.") (emphasis added).

other restrictions, most notably the demand requirement, apply to these actions.[91]

One reason to believe that the demand requirement does not apply in this context is that the defendants are necessarily the company's directors. A traditional derivative suit can be brought against the company's directors, but might also or instead target the company's officers, employees, or even a third party. For that reason, in a traditional derivative suit, the board does not always face a conflict of interest in determining whether to take action against the purported wrongdoer. The demand requirement may therefore make sense in cases where the directors are not the defendants.

In the type of derivative action authorized by section 367 in contrast, the only cause of action is for a violation of the board's balancing duties; the only possible defendants are the members of the board.[92] On the other hand, courts have also said that the mere fact that the directors approved the challenged transaction is insufficient to excuse the demand requirement, unless there is a reasonable chance that the defendant directors will suffer liability in the suit.[93]

A related question is whether § 367 actions are the *only* type of derivative suit that can be brought by a PBC shareholder. The answer here seems more straightforward. Remember that § 361 states that the ordinary corporate statutory rules apply, except to the extent the PBC subchapter imposes additional or different requirements.[94] Since the PBC statute does

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[91] *See* Gollust v. Mendell, 501 U.S. 115, 125 (1991) (requiring the plaintiff in an action arising from § 16(b) of the Securities Exchange Act of 1934 to maintain "some continuing financial stake in the litigation," even if indirect, such as an ownership stake in the issuer's parent corporation, in order to meet Article III's case-or-controversy limit on federal court jurisdiction). An analogous requirement seems to apply under Delaware law. *See* Op. of Justices*,* 413 A.2d 1245, 1247 (Del. 1980) (stating "[t]he Justices have clearly emphasized that advisory opinions are outside the mainstream of our responsibilities as judicial officers . . . ."); *see also* Worldwide Salvage v. Castle, 1987 Del. Super. LEXIS 1027, at *9 (stating "[t]he doctrine of mootness stems from the constitutional requirement that a court only has jurisdiction over actual cases and controversies").

[92] *See* DEL. CODE ANN. tit. 8, §§ 365, 367 (2013).

[93] *See* Malpiede v. Townson*,* 780 A.2d 1075, 1085 (Del. 2001) (stating "[e]xcept in egregious cases, the threat of personal liability for approving a merger transaction does not in itself provide a sufficient basis to question the disinterestedness of directors because risk of litigation is present whenever a board decides to sell the company"); Aronson v. Lewis*,* 473 A.2d 805, 815 (1984) (stating "[h]owever, the mere threat of personal liability for approving a questioned transaction, standing alone, is insufficient to challenge either the independence or disinterestedness of directors, although in rare cases a transaction may be so egregious on its face that board approval cannot meet the test of business judgment, and a substantial likelihood of director liability therefore exists"), *overruled on other grounds by* Brehm v. Eisner, 746 A.2d 244, 253-54 (Del. 2000).

[94] DEL. CODE ANN. tit. 8, § 361 (2013).

not exclude traditional derivative actions, they would seem to be permitted. Granted, the rule in section 361 applies expressly only to other statutory provisions in the corporation's chapter, and as discussed above, the authorization for derivative suits is mostly from common law. But the intent of the provision pretty clearly seems to be to make the PBC statute supplementary to ordinary corporate law, whether that law stems from a statute or court case. Also, there is some statutory reference to derivative suits in section 327, which may suffice for this purpose even for those courts inclined to apply section 361 narrowly. And there is no apparent policy justification for depriving PBC shareholders of their right to enforce directors' and officers' duties to the corporation through a derivative suit. Traditional derivative suits should remain available to PBC shareholders.

A PBC's shareholders, then, do have the power to launch a derivative action (or at least a derivative-like action) against directors who fail to balance the needs of the PBC's various constituencies. At the moment, however, only one PBCs is publicly traded.[95] Nearly all PBCs are closely held, so the shareholders and the founders are more or less synonymous, or at least substantially overlapping.[96] Presumably, the shareholders have real control over the directors, and often *are* the directors making it relatively unlikely that any of them would bring suit against themselves and their colleagues, barring some fractious internal dispute.

Other corporate constituencies, such as employees or the beneficiaries of the PBC's public purpose, have no standing to bring a suit for breach of directors' balancing duties. PBC directors have no duty to beneficiaries of the public benefit(s) pursued by the PBC, nor do they have any duty to any other beneficiary of corporate activity other than the shareholders.[97] Since shareholders are already in control of most PBCs, and other groups have no standing to sue, suits for breach of directors' balancing duties are likely to be rare, at least until we begin to see significant numbers of publicly traded PBCs.

Taken all together then, Delaware's default rules grant permission to PBCs to prioritize the interests of other constituencies over those of shareholders, meeting the Protect goal to an extent, especially in privately

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[95] Laureate Education, a public benefit corporation, went public in February, 2017. *See* Lauren Gensler, *The World's Biggest For-Profit Company, Laureate Education, Raises $490 Million In Public Debut*, FORBES, February 1, 2017, available at https://www.forbes.com/sites/laurengensler/2017/02/01/laureate-education-initial-public-offering/#19266f8c2b3d.

[96] Etsy, Inc. is registered in Delaware and began trading on Nasdaq on April 16, 2015. ETSY FAQ FOR INVESTORS, http://investors.etsy.com/phoenix.zhtml?c=253952&p=irol-faq (last visited on October 15, 2017). Etsy is certified by B Lab but has not yet become a PBC. Laureate Education, Inc. is a PBC (and certified by B Lab) and announced in October of 2015 that it planned a $1 billion initial public offering. *See* SOLOMON, *supra* note 41.

[97] § 365(b).

held PBCs where the shareholders agree on how to strike an appropriate balance. But by going further and *mandating* that directors balance the various opposing interests, the default rules fail to fully implement the Protect goal, creating at least the potential for liability for failing to fulfill their balancing duty. Private ordering, in the form of a § 102(b)(7) provision in the certificate of incorporation – tailored to PBCs so that it covers the balancing duty – may remedy this problem. Full implementation of the Protect goal, though, may undermine Brand and Express, as I will discuss below.

2. Brand

Unlike the Protect and Express motives, which are primarily rooted in an altruistic desire to help society, the Brand motive seeks pecuniary gain by leveraging the company's social mission to achieve better results with employees, customers, and investors. For social entrepreneurs to benefit in this way by choosing a PBC, the various target audiences must care enough about the company's PBC status to be willing to sacrifice other benefits to work there (in the case of employees), pay a premium price for the product or service (in the case of customers), or sacrifice some expected return or believe that their return will be higher because of the company's PBC status (in the case of investors).[98] Will sufficiently large percentages of these audiences believe that PBC status matters to make the status worthwhile?

PBCs are far too new to have generated meaningfully useful data on this question. There is some cause to think, however, that significant numbers of employees, customers, and investors may feel strongly enough about a company's prosocial behavior to be willing to pay more (or be paid less). Millennials, whose rising dominance as entrepreneurs and executives is demographically inevitable, overwhelmingly believe that a business' purpose should be greater than earning money.[99] Many millennials hold that businesses should be run to pursue a host of interests

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[98] There is some evidence that companies that focus on taking care of their employees or other corporate constituencies outperform those that do not. *See* Shawn L. Berman et. al, *Does Stakeholder Orientation Matter? The Relationship between Management Models and Firm Financial Performance*, 42 ACAD. MGMT. J. 488, 489 (describing a study that found focusing on employees and customers improved companies' performance).

[99] A recent international survey of millennials found that "[a]lmost nine in ten (87 percent) believe that 'the success of a business should be measured in terms of more than just its financial performance.'" *The 2016 Deloitte Millennial Survey*, DELOITTE, http://www2.deloitte.com/content/dam/Deloitte/global/Documents/About-Deloitte/gx-millenial-survey-2016-exec-summary.pdf (last visited Oct. 15, 2017).

in addition to shareholder value: securing well-paying and stable jobs, providing high-quality products and services to customers, nurturing communities, and protecting the environment.[100] They therefore seem likely to find benefit corporations appealing, at least in concept. More broadly, a 2014 study by Nielsen found that more than half of global online consumers would pay more for products and services provided by companies that are committed to positive social and environmental action.[101] Also, a number of the entrepreneurs I interviewed attributed their success in recruiting and retaining employees to their status as benefit corporations. And there are quite a few successful businesses (Warby Parker, Seventh Generation, Tom's Shoes etc.) that seem to be flourishing at least in part due to their prosocial brands.[102]

For purposes of this discussion, I will make the (I believe, reasonable) assumption that there is a significant market that will to some degree favor prosocial companies across all three areas: employees, customers, and investors. If PBC status is to help entrepreneurs reach that market, the status must help send a reliable signal of a company's prosocial orientation.

Companies are certainly capable of sending such a signal without adopting a special form of business organization. They do so through charitable donations, by advertising their benevolent employment and environmental policies, and by partnering with credible people and organizations to send the relevant message. For example, Walmart (whose commitment to profits can scarcely be questioned) trumpets on its website a program it calls the Shared Value Initiative:

> The work we do to help people live better extends far beyond the physical walls of our stores, making a real difference on the real issues that matter to us all. From local issues like domestic manufacturing and job creation to global issues like preserving the environment, fighting hunger, empowering

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[100] *Id.*

[101] *See* NIELSEN, *Global Consumers Are Willing to Put Their Money Where Their Heart Is When It Comes to Goods and Services from Companies Committed to Social Responsibility*, (June 17, 2014), http://www.nielsen.com/us/en/press-room/2014/global-consumers-are-willing-to-put-their-money-where-their-heart-is.html.

[102] Warby Parker, Inc. is a company that sells eyeglasses and that advertises that it gives a pair of glasses to someone in need for every pair purchased. *See* WARBY PARKER, https://www.warbyparker.com (last visited Oct. 15, 2017). Similarly, Toms Shoes, LLC says that it provides a pair of shoes for a child in need for every pair purchased by a consumer. *See* TOMS, http://www.toms.com (last visited Oct. 15, 2017). Patagonia is an outdoor clothing company that trumpets its environmental values and its fair treatment of workers. *See* PATAGONIA CORPORATE RESPONSIBILITY, http://www.patagonia.com/us/patagonia.go?assetid=67372.

> women, and providing access to healthy, affordable food, our efforts impact communities around the world and affect the lives of people we will never meet.[103]

The webpage goes on to provide links to pages that describe Walmart's efforts in greater detail and even a link to a Global Responsibility Report.[104]

Companies make prosocial claims like these quite often, but the claims may not be credited by their target audiences. The appeal of PBC status under the Brand motive is that being a PBC may generate enhanced credibility for a company's assertion that it is helping the world in a meaningful way. The Delaware statute, however, does not do a particularly good job of boosting a PBC's credibility.

PBCs lend credibility to prosocial claims by: (a) mandating that every PBC adopt a specific public benefit it will pursue; (b) requiring PBC boards of directors to pursue the company's public benefit and balance the company's other needs, such as profit, against the need to effectuate its prosocial goals and the interests of others materially affected by the corporation's activities; (c) permitting shareholders to sue directors who fail in their balancing duties; and (d) imposing certain disclosure requirements related to the company's social purpose.[105]

I will discuss the statute's public benefit requirement below, in Part B. For now, it should suffice to point out that, even if a company's stated purpose was universally acknowledged as benefitting society, merely stating the purpose achieves nothing in itself. The purpose is only meaningful to the extent the company achieves it, or at least tries to do so. If the purpose amounts to empty rhetoric, a sort of campaign promise for marketing purposes, then eventually it will cease to be credible and will lose its impact. The key question, then, is whether the remaining provisions of the PBC statute support the purpose and ensure its credibility.

As I discussed above, the balancing mandate is quite weak. In all likelihood, directors can fulfill their balancing duty by informing themselves, remaining disinterested, and avoiding unreasonable decisions. Moreover, even if directors fail in their duties, they are unlikely to suffer liability. Only shareholders have standing to sue to enforce the balancing duty, and in closely held PBCs, the shareholders are likely to be the same

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[103] WALMART SHARED VALUE INITIATIVE, https://www.sharedvalue.org/partners/funding-partners/walmart.

[104] *See* WALMART, *Global Responsibility Report*, http://corporate.walmart.com/global-responsibility/global-responsibility-report.

[105] *See* DEL. CODE ANN. tit. 8, §§ 361-368 (2013).

people as the directors. Barring a rift among the shareholders, then, there seems little chance of a lawsuit. Directors in publicly traded PBCs may face a greater threat of lawsuits for breaching their balancing duties, but publicly traded PBCs are likely to remain rare for some time yet.

Liability is not the only method of policing directors' behavior. Disclosure may also shift behavior if directors are concerned for their reputations or fear that other consequences, such as a decline in the company's stock price or in demand for the company's products, may occur if any overly profit-favoring decisions become public.

The Delaware PBC statute does impose some disclosure requirements. A Delaware PBC must provide a report to its shareholders that describes how the PBC promoted the public benefit or benefits that it has stated it will pursue.[106] The board must issue this report at least every other year.[107] This report must also describe how the company has pursued the best interests of other corporate constituencies, such as employees, communities, and the environment.[108] The report must include four types of information: (1) the goals the board set to further the chosen public benefit(s) and the interests of other corporate constituencies; (2) the standards the board chose to use to measure the company's progress in furthering those goals; (3) objective facts relevant to those standards; and (4) an analysis of the extent to which the company has succeeded in meeting its goals.[109] A PBC may impose more stringent reporting requirements in its certificate of incorporation if desired.[110]

B Lab's model statute has a similar provision, but requires somewhat more extensive disclosure and mandates that the report be issued annually.[111] The model statute also requires a benefit corporation to post the report with certain information redacted on its website and to file it with the Secretary of State, making it available to the public generally and not just to the company's shareholders.[112] Perhaps the most important distinction between Delaware's reporting requirement and B Lab's, however, is that B Lab's statute requires benefit corporations to adopt a third-party standard that meets certain criteria.[113] Delaware permits directors to create their own standard.[114] Neither statute requires an external audit or validation of the company's statements in its report.

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106 *See Id.*; DEL. CODE ANN. tit. 8, § 366(b) (2013).
107 DEL. CODE ANN. tit. 8, §§ 361-368 (2013).
108 *Id.*
109 § 366(b).
110 *Id.*, § 366(c).
111 *See* MODEL BENEFIT CORP. LEGIS. § 401 (B Lab 2017).
112 *See id.*, § 402.
113 §§ 401, 102.
114 DEL. CODE ANN. tit. 8, § 366(b) (2013).

The Delaware statute requires the board to provide disclosure only to its shareholders, and only biennially. In the typical case of a closely held PBC, where the shareholders exercise meaningful (if not total) control over the board, the disclosure is unlikely to contain information that the shareholders do not already possess. The directors are unlikely to fear their reputations will suffer if the report reveals they failed to pursue the company's stated social benefit with sufficient fervor, since only they and their affiliates will have access to the information.

B Lab's statute is superior in this respect, in that it requires that the benefit report be posted on the company's website, exposing the directors to possible reputational harm if they have failed to deliver the social benefits the company has promised in its statement of purpose. This distinction will largely vanish with publicly traded PBCs, though, since a publicly traded company has many shareholders who are not actively involved in running the company or selecting its board and since the securities laws should require public filing of the benefit report.[115]

Also, there is no enforcement mechanism built into Delaware's statute to force directors to obey their disclosure duties. Section 367, which authorizes derivative suits, permits suits only to enforce the balancing requirement. It is unclear whether shareholders could launch a common law derivative suit to enforce the disclosure duty, given the narrowness of section 367.

In sum, the PBC statute does a fairly weak job of signaling the company's prosocial behavior to employees and customers. The statute is mostly permissive, since the balancing mandate has little substantive bite and is unlikely to be effectively enforced by either the threat of liability or reputational harm. At best, adopting PBC status demonstrates the founders' desire to have the option to prioritize a social mission or the interests of non-shareholder constituencies over profit concerns.

Still, since the social mission automatically includes the welfare of employees and customers, adopting PBC status does provide a signal which may prove meaningful. Outside investors should see PBC status as posing at least some risk that the company will sacrifice profits for other interests, which can be expected to result in self-selection by investors. Investors who purchase equity in a PBC would presumably accept and perhaps even support the company's mission, making it more likely that the mission will be taken seriously by the board. Several entrepreneurs I interviewed made this point, saying that they felt benefit corporation status

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[115] *See* SEC. & EXCH. COMM'N, FORM 8-K ITEM 2.02 (2017) (public announcement or release of material, non-public information regarding results of operations or financial condition must be filed on Form 8-K).

acted as a filter to ensure they attracted only investors who shared the company's mission.

It's impossible to rule out the possibility that founders and investors will privately agree to let profit concerns trump, but PBC status will pose a risk to investors that directors will abrogate any such secret agreement without much fear of liability.[116] To the extent that risk attracts investors who sincerely share the company's prosocial goals, those goals are more likely to be pursued. Employees and customers, then, should see PBC status as some signal of an intent to favor their interests and the interest of the public benefit the company has adopted, even if the signal is muddy.

Founders who find this signal too weak can remedy the problem to some degree with private ordering. They can enhance the disclosure requirement with charter provisions that require the board to make the report available to the public and/or to measure the company's conduct against a third-party standard such as B Lab's B Impact Assessment.[117] They can ensure there is no charter provision exempting directors from liability for failing in their balancing duties. Finally, they can seek outside certification such as that provided by B Lab that goes beyond the rather sparse requirements imposed by the PBC statute. The utility of such certification depends on the requirements for certification and their enforcement. If there is sufficient demand for rigorous standards that are strictly administered, the market will presumably supply such certifications (if it does not already).[118] PBC status should be seen as a set of default terms that provide a weak signal of prosocial corporate values, with stronger signals available through private ordering to those entities that desire it.

3. Express

My interviews with social entrepreneurs indicated that, for many of them, the expressive function was the most important reason they chose to incorporate as a benefit corporation. If Delaware is to attract social entrepreneurs to PBCs, then, the statute must satisfy this need.

The name of the entity may itself aid in this regard. The name serves as an advertisement that the company aims to be about something more than making a profit for its shareholders. Even for audiences who are

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[116] Since the agreement would violate the statute's balancing duty, it would likely be held unenforceable. *See supra* note 68 and accompanying text.

[117] The B Impact Assessment is available for free. B IMPACT ASSESSMENT, http://bimpactassessment.net.

[118] For an in-depth analysis of the B Impact Assessment, see Michael B. Dorff, *Assessing the Assessment: B Lab's Efforts to Measure Companies' Benevolence*, 40 SEATTLE U. L. REV. 515 (2016) (discussing an in-depth analysis of the B Impact Assessment).

unfamiliar with PBCs, the name at a minimum, signals that this entity is something different from the usual, and the phrase "public benefit" would seem to indicate that it is something like a nonprofit. Indeed, in some states, nonprofit corporations are called public benefit corporations.[119]

The balancing duty may also be helpful in this regard. Conducting conversations about how a business decision will impact the company's various constituencies and taking those constituencies' concerns seriously will permit the founders to articulate their values regularly. Similarly, these conversations will also allow founders to vocalize their alignment with the company's social purpose. The benefit report will provide a vehicle to express these values to a potentially broader audience.

In some ways, then, the PBC statute seems targeted at the Express goal. But the statute is still quite limited. Founders who want their companies to express their values will presumably be most satisfied with an entity form that clearly advertises the company's prosocial ethos. If PBCs can too easily be used by those who want to present the appearance of creating a public benefit without the reality ("greenwash"), then the use of the form will remain suboptimal.

As discussed above, the PBC form is quite vulnerable to greenwashers, especially in closely-held companies. The balancing mandate contains only minimal substantive requirements and is unlikely to be enforced often in closely held entities. And the statute only requires the benefit report to be sent to the company's shareholders; in a closely held entity, the shareholders are likely to be in effective control of the board, and therefore, both unsurprised and undisturbed by whatever the report contains. Without more stringent protections against greenwashing, the expressive function of selecting a PBC will remain limited.

The statute's weaknesses can be addressed through private ordering to a considerable extent. By taking some of the steps outlined above, mandating broader and more extensive disclosure, leaving directors vulnerable to suits for breach of their balancing duties, seeking third-party certification of the company's prosocial behavior, founders can better express the values that will suffuse their business.

B. Foster Social Good

For at least some of those involved in passing PBC legislation in Delaware, the purpose of the new entity form was not just to attract new incorporations, but also to harness capitalist forces to solve social

[119] *See, e.g.*, CAL. CORP. CODE § 5110 (1980).

problems.[120] For the PBC form to foster social good, its requirements must facilitate the achievement of social good by the entrepreneurs who use it.

As I have discussed above, the legal form does very little to prevent founders from adopting the appearance of a prosocial organization while abandoning the substance. But for founders who are sincere in their desire to have a positive impact on society, there are some mechanisms to help them. The balancing requirement should foster discussions and reinforce the importance of the company's values.[121] Similarly, the disclosure requirement provides directors with an opportunity to self-reflect and examine whether they are running the company in a way that is consistent with their expressed social ambitions.[122] Directors worried about being sued for failing to maximize shareholder returns should be comforted by the permission the statute grants to prioritize the welfare of non-shareholder constituencies and/or the public benefit the company has adopted.[123] In other words, while the PBC statute is not a very good *enforcement* tool, it may prove an effective *reinforcement* tool.

A potentially serious problem with the PBC form, though, is that its core values are not well-defined. To evaluate the form's ability to foster the public's benefit, we need to understand what we mean by "public benefit." If the legal definition is too broad, so that it encompasses meanings that are alien to most people's conception of what a prosocial organization should be, then there is a substantial risk that the form will be abused and will cease to be useful for either the Brand or Express functions.

The Delaware legislature defined "public benefit corporation" in part as a for-profit entity "that is intended to produce a public benefit or public benefits and to operate in a responsible and sustainable manner."[124] Delaware PBCs are required to state in their certificates of incorporation the specific public benefit or benefits that they will promote.[125]

What these terms mean is less than clear. The statute does not specify *how* companies should operate in a way that is "responsible" and "sustainable." These terms remain undefined. While the statute does define "public benefit," the definition is extremely broad, encompassing

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[120] *See Governor Markell Signs Public Benefit Corporation Legislation*, *supra* note 22 (stating "[w]e have heard repeatedly that public benefit corporations can fill a market need. But just as important, they will also fill a societal need.").

[121] *See* DEL. CODE ANN. tit. 8, § 365(a) (2013).

[122] DEL. CODE ANN. tit. 8, § 366 (2013).

[123] DEL. CODE ANN. tit. 8, § 362(a) (2013) (stating "a public benefit corporation shall be managed in a manner that balances the stockholders' pecuniary interests, the best interests of those materially affected by the corporation's conduct, and the public benefit or public benefits identified in its certificate of incorporation").

[124] § 362(a).

[125] § 362(a)(1).

some positive impact on just about anyone other than shareholders (in their shareholding capacity). The statute states:

> "Public benefit" means a positive effect (or reduction of negative effects) on 1 or more categories of persons, entities, communities or interests (other than stockholders in their capacities as stockholders) including, but not limited to, effects of an artistic, charitable, cultural, economic, educational, environmental, literary, medical, religious, scientific or technological nature.[126]

To see how broad this definition is, consider a technology company that invented a new, faster smart phone. It is difficult to rule out the possibility that this contribution would count as a positive effect on a category of persons (the company's customers) of a technological nature. Yet, this hardly seems the sort of social impact most activists have in mind when they advocate for benefit corporations. Such a company would also have to be "responsible" and "sustainable," but courts might construe "responsible" narrowly to mean "compliance with all pertinent laws and regulations" and "sustainable" to mean "capable of surviving for many years."

While courts will hopefully read in meanings more in keeping with the statute's purpose than these, the statute itself provides little guidance.[127] The effect of providing a statutory purpose (and with it all the provisions designed to enforce that purpose, and therefore the utility of the entire form) will depend on whether the Delaware courts construe the statute in light of its purpose rather than its literal meaning.

This problem may not be as dire a threat as it first appears. After all, nonprofit corporations have survived a similarly amorphous definition of their permissible purposes.[128] Even the federal standard for entities who wish to qualify for tax-deductible contributions is quite broad. That standard defines the scope of qualified entities as, in relevant part:

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[126] § 362(b).

[127] B Lab's model statute is somewhat more directive in this regard. It requires benefit corporations to have a general public benefit purpose and defines this term more narrowly in relevant part as a "material positive impact on society and the environment, taken as a whole, assessed against a third-party standard." MODEL BENEFIT CORP. LEGIS. §§ 102, 201 (B LAB 2017). The official comment to this section says it is informed by §301(a), which requires directors to consider a list of constituencies that may be affected by a corporate action, as well as, additional considerations boards may weigh in making corporate decisions. *Id.* at §§ 102 cmt. regarding "General public benefit," 301.

[128] *See, e.g.*, CAL. CORP. CODE § 5111 (permitting the formation of nonprofit corporations for "any public or charitable purposes").

> Corporations, and any community chest, fund, or foundation, organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes, or to foster national or international amateur sports competition . . . or for the prevention of cruelty to children or animals . . . .[129]

Perhaps the combination of cultural norms and judicial interpretation of the PBC standard will limit permissible purposes in a way that comports with the statute's purpose.

Private ordering has the potential to ameliorate this problem as well, through third-party certification. B Lab, the dominant player in this market currently, has a complex scoring system that rates companies across a variety of dimensions.[130] The advantage of such a system is that it defines what counts as prosocial conduct in considerable detail. The disadvantage is that by imposing a particular vision of how companies should behave, it impedes entrepreneurs from experimenting with a variety of different approaches.[131]

This is perhaps a reasonable justification for the PBC statute's broad definition of "public benefit." The statute provides flexibility in a way that B Lab's third-party certification does not.

V. CONCLUSION

Throughout this essay, I have argued that the weaknesses in the PBC statute can largely be combatted through the use of private ordering, especially through the use of third-party certification. Third-party certification arguably does a better job at both the Brand and Express functions than PBC status does. One might reasonably ask, then, why entrepreneurs should bother with the new form rather than use a traditional corporation combined with third-party certification of their prosocial behavior.

One answer to this question is that third-party certification comes at the cost of narrowing the scope of permissible conceptions of prosocial corporate purposes and implementation methods. Entrepreneurs whose

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[129] 26 U.S.C. § 501(c)(3).

[130] *See* RYAN HONEYMAN ET AL., The B CORP HANDBOOK: HOW TO USE BUS. AS A FORCE FOR GOOD (2014).

[131] *See* DORFF, *supra* note 116 (arguing for the establishment of competing assessment models).

vision varies from that of the available third-party certifiers can chart their own path with a PBC, but not with certification.

Another is that PBCs are necessary for the Protect function. Certification alone provides no protection from liability for elevating social purpose over profit. This function could likely be met through a limited liability company with appropriate provisions in the operating agreement.[132] However, an LLC would not serve the same cautionary effect that a PBC does, warning investors clearly and saliently that this is an entity that may prioritize other interests over profit.[133]

A third justification for PBC status is that PBCs constitute a more durable commitment than third-party certification alone. A two-thirds vote of the outstanding shares is required to terminate the company's PBC status;[134] in contrast, terminating a relationship with a third-party certifier is an ordinary business decision that does not require a shareholder vote of any kind.[135]

Finally, PBC status may provide socially-minded entrepreneurs with leverage to use with their outside investors over time. As disputes arise over the extent to which profit should be sacrificed for social purposes, the choice of PBC status may provide rhetorical ammunition to entrepreneurs arguing the company should prioritize the public benefit. PBC status may set the terms of a relational contract between the founders and the investors that can have power far beyond any legal requirement.[136]

It is tempting for corporate legal scholars, accustomed to the hard-edged incentive-based thinking that comes with economic analysis, to react cynically to the benefit corporation movement. The new form can appear hopelessly idealistic and even naïve. The statutory provisions lend some support to this cynicism. In themselves, they seem entirely inadequate to ensure that PBCs will pursue a public benefit; they almost invite greenwashing. But there does seem to be real demand for this form among intelligent, well-educated people who are investing their human and financial capital, which should give cynics some pause. In my interviews of benefit corporation founders, I found them all to be incredibly sincere and passionate about their desire to channel capitalism's strengths into solving social problems, or at least to soften capitalism's ill effects on workers, communities, and the environment. The new form needs work, without a doubt, if it is to achieve even a fraction of its

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[132] *See* ALEXANDER, *supra* note 8, at 45-46.
[133] *See* DEL. CODE ANN. tit. 8, § 362(c) (2013).
[134] *See id.*
[135] *See* DEL. CODE ANN. tit. 8, § 141(a) (2016).
[136] *See* Ian R. McNeil, *Relational Contract Theory: Challenges and Queries*, 94 NW. U. L. REV. 877, 902-905 (2000) (discussing the founding concept of contract law as it relates to corporate legal obligations).

advocates’ ambitions. But combined with creative private ordering, PBCs have the potential to affect a transformative impact on the economy.

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