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## More Burden than Benefit? Analysis of the Benefit Corporation Movement in California

Sarah Thornsberry

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# **MORE BURDEN THAN BENEFIT? ANALYSIS OF THE BENEFIT CORPORATION MOVEMENT IN CALIFORNIA**

SARAH THORNSBERRY

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## ABSTRACT

The benefit corporation movement has been associated with the separate camps of social entrepreneurship, nonprofit organizations, and for-profit corporations, while trying to establish itself as a community of businesses that pursue not only profit, but also environmental and social good. This article examines the legal attributes of benefit corporation legislation and articulates why incorporating as a benefit corporation can be an excellent business decision. Lastly, the article looks at how the movement can further expand in California.

## I. INTRODUCTION

A couple sits in a chic restaurant, examines the menu before them and before ordering, inquires about their meal:

**Nance:** If you could just tell us a little bit more about [the chicken].

**Waitress:** It's a heritage-breed, woodland-raised chicken that's been fed a diet of sheep's milk, soy, and hazelnuts.

**Peter:** And it's local? It is local?

**Nance:** Is that USDA organic? Or Oregon organic? Or Portland organic?

**Peter:** These hazelnuts, are they local?

**Nance:** How big is the area where the chickens are able to roam free?

*The waitress retrieves a binder of papers and a picture of a chicken . . .*

**Waitress:** Alright, here is the chicken you will be enjoying tonight . . . his name was Collin, here are his papers.

**Peter:** He looks like a happy little guy who runs around . . . do you know if he had a lot of friends—other chickens as friends?

**Waitress:** I don't know that I can speak to that level of intimate knowledge about him.

**Nance:** Who are these people raising Collin?

**Peter:** And you have a good relationship with this farm? It's not some guy on a yacht, who lives in Miami, just saying that he's organic?

**Nance:** It just, it tears at the core of my being, the idea of someone just cashing

in on the trend of being organic . . . .<sup>1</sup>

This *Portlandia* episode is a parody of “social consumerism” taken to the extreme.<sup>2</sup> However, social consumerism is on the rise in the United States, with a younger generation becoming more aware of how their purchases can have a social impact and increasingly willing to pay a higher price tag for socially-responsible companies’ products and services.<sup>3</sup> The socially-conscious consumer is a global phenomenon,<sup>4</sup> and in America, it has taken root.<sup>5</sup> A leading marketing firm has coined the term “New Consumer” to describe people “uniting deeply-held principles with everyday pragmatism, a sense of purpose with more active participation to help create solutions that can improve their own lives while creating a more sustainable economy that can benefit all.”<sup>6</sup> How can businesses capitalize on this consumer trend and still remain competitive in the arenas of quality and price?

One answer has been for businesses to utilize corporate social responsibility (CSR), a term that describes the measures taken by a corporation to assist in social and economic development.<sup>7</sup> However, since CSR encompasses self-prescribed commitments rather than upheld standards, it can

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<sup>1</sup> Melissa Locker, *Portlandia: Is It Local?*, INDEPENDENT FILM CHANNEL (Jan. 21, 2011), <http://www.ifc.com/fix/2011/01/portlandia-is-it-local> (some dialogue omitted).

<sup>2</sup> *Portlandia* is a comedy series airing on the Independent Film Channel that features “life in hipster enclaves, and the self-consciousness that makes hipsters desperately disavow the label.” Margaret Talbot, *Stumptown Girl*, THE NEW YORKER (Jan. 2, 2012), [http://www.newyorker.com/reporting/2012/01/02/120102fa\\_fact\\_talbot?currentPage=all](http://www.newyorker.com/reporting/2012/01/02/120102fa_fact_talbot?currentPage=all).

<sup>3</sup> *Nielsen Identifies Attributes of the Global, Socially-Conscious Consumer*, NIELSEN (Mar. 27, 2012), <http://www.nielsen.com/us/en/insights/press-room/2012/nielsen-identifies-attributes-of-the-global--socially-conscious-.html>.

<sup>4</sup> *Id.* Consumers living in the Asia-Pacific, Middle East, Africa, and Latin America have self-identified with this movement. *Id.*

<sup>5</sup> Raphael Bemporad, *How Conscious Consumers Are Redefining Value in a New Economy*, CASE FOUNDATION (Apr. 23, 2009), <http://casefoundation.org/blog/how-conscious-consumers-are-redefining-value-new-economy-8701>. The 2009 BBMG Conscious Consumer Report revealed that “nearly seven in ten Americans agree (67%) that ‘even in tough economic times, it is important to purchase products with social and environmental benefits,’ and half (51%) say they are ‘willing to pay more’ for them.” *Id.*; see also RAPHAEL BEMPORAD & MITCH BARANOWSKI, BBMG, CONSCIOUS CONSUMERS ARE CHANGING THE RULES OF MARKETING. ARE YOU READY? 1 (Nov. 2007), available at [http://www.greenamerica.org/PDF/summary\\_2008chi-conscious-consumers.pdf](http://www.greenamerica.org/PDF/summary_2008chi-conscious-consumers.pdf) (finding that in 2007 “nearly nine in ten Americans . . . are more likely to buy from companies that manufacture energy efficient products (90%), promote health and safety benefits (88%), support fair labor and trade practices (87%) and commit to environmentally-friendly practices (87%), if products are of equal quality and price.”).

<sup>6</sup> BBMG, UNLEASHED: HOW NEW CONSUMERS WILL REVOLUTIONIZE BRANDS AND SCALE SUSTAINABILITY 5–6 (Mar. 2011), available at <http://www.sustainableindustries.com/resources/unleashed-how-new-consumers-will-revolutionize-brands-and-scale-sustainability>.

<sup>7</sup> Antony Page & Robert A. Katz, *Is Social Enterprise the New Corporate Social Responsibility?*, 34 SEATTLE U. L. REV. 1351, 1351 n.1 (2011).



be easily construed by companies wanting to leverage its inherent marketing power to conscious consumers.<sup>8</sup> In an action called “green-washing,” or “faux CSR,” businesses cast their social actions in an unrealistic light.<sup>9</sup> In a world where half of the one hundred largest economic entities are private corporations,<sup>10</sup> this trust factor with corporations is an issue to address. Critics question the authenticity of corporations’ cause-marketing campaigns.<sup>11</sup> Popular books, such as New York Times bestseller, *The Omnivore’s Dilemma*,<sup>12</sup> and national leaders have addressed the lack of supply chain transparency. For example, in September 2012, President Obama committed to increase supply chain transparency in governmental contracts to help eradicate human trafficking.<sup>13</sup> In California, recent legislation requires high-profit companies to share their supply chain sourcing with consumers when it is requested.<sup>14</sup> When it comes to trusting corporations’ actions, Americans are becoming wary, and thus, increasingly rely upon third-party evaluations when making decisions if a company “does good things for people and the planet.”<sup>15</sup> “[T]he accuracy of CSR information is important for efficient securities markets and informed

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<sup>8</sup> Miriam A. Cherry & Judd F. Sneirson, *Beyond Profit: Rethinking Corporate Social Responsibility and Greenwashing After the BP Oil Disaster*, 85 TUL. L. REV. 983, 985 (2011) (discussing “the disconnect between how BP portrayed itself in the public sphere and how it actually behaved when its image was not at stake”).

<sup>9</sup> *Id.* at 986.

<sup>10</sup> Ben Schreckinger, *Virtue Inc. Can the New “Benefit Corporation” Charters Give Companies a Conscience?*, THE BOS. GLOBE (Nov. 25, 2012), <http://www.bostonglobe.com/ideas/2012/11/25/virtue-inc/sMNhJRcOIgZ0rqpLTALrN/story.html>.

<sup>11</sup> *Id.*; see also Dr. Ioannis Ioannou, *Can We Really Trust Today’s Businesses?*, BLOOMBERG BUSINESSWEEK (Aug. 14, 2012), <http://www.businessweek.com/articles/2012-08-14/can-we-really-trust-today-s-businesses>.

<sup>12</sup> MICHAEL POLLAN, *THE OMNIVORE’S DILEMMA: A NATURAL HISTORY OF FOUR MEALS* (2006).

<sup>13</sup> Press Release, Office of the Press Sec’y at The White House, Fact Sheet: Executive Order Strengthening Protections Against Trafficking in Persons in Federal Contracts (Sept. 25, 2012), *available at* <http://www.whitehouse.gov/the-press-office/2012/09/25/fact-sheet-executive-order-strengthening-protections-against-trafficking>.

<sup>14</sup> S.B. 657, 2009–2010 Leg. Sess. (Cal. 2010), *available at* <http://www.state.gov/documents/organization/164934.pdf>. This bill enacts the California Transparency in Supply Chains Act of 2010, which stipulates that as of January 1, 2012, retail sellers and manufacturers having \$100,000,000 or more in annual worldwide gross receipts and doing business in the state to “disclose their efforts to eradicate slavery and human trafficking from their direct supply chains for tangible goods offered for sale . . . .” *Id.* The Act’s stated purpose is to eliminate consumers who “inadvertently promote sanctioning these crimes through the purchase of goods and products that have been tainted in the supply chain.” *Id.* With the Act, consumers are now able to distinguish which companies make a concentrated effort to combat human trafficking in their practices and help eradicate such slavery with their purchasing decisions.

<sup>15</sup> Bemporad & Baranowski, *supra* note 5, at 3. When making decisions, socially conscious consumers use the media (53%), certification seals and labels on the products (52%), and the Internet (41%), compared to relying on advertisements (30%). *Id.*

consumer choice,”<sup>16</sup> especially when consumers are seeking brands that deliver on “Triple Value Proposition.”<sup>17</sup>

This Article examines how a new player in the corporate legal field, the benefit corporation, is meeting the outcry for companies that not only espouse to “doing good,” but are also kept accountable for such social actions. Part II breaks down some terms arising out of the conscious consumerism movement, examines differences between popular benefit corporation entities, and analyzes how California has adopted the model legislation for the legal entity into its corporate code. Part III examines how benefit corporations stack-up against other corporate entities in supporting businesses that desire to pursue the triple-bottom line. Part IV evaluates if the legislation is even necessary in light of other corporate law precedent. Part V outlines arguments for the benefit corporation legal entity in California. Finally, Part VI presents ideas on how benefit corporations will impact California’s economy and how the state can continue encouraging entrepreneurship through supporting the benefit corporation community.

## II. BACKGROUND & BENEFIT CORPORATION FORMATION

### *A. The Social Entrepreneurship Backdrop*

In combining business acumen with profit generation to not only make money, but also positively impact society, the benefit corporation model is gaining popularity among businessmen and social entrepreneurs.<sup>18</sup> Some of the most notable businesses that are either pursuing or already have become a benefit corporation include: Etsy, Ben & Jerry’s, King Arthur Flour, and Patagonia.<sup>19</sup> The movement of social entrepreneurship is known for the “triple bottom line” business plan, pursuing not only economic prosperity, but also environmental quality and social good.<sup>20</sup> A benefit corporation legal entity also

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<sup>16</sup> Cherry & Sneirson, *supra* note 8, at 986.

<sup>17</sup> BBMG, *supra* note 6, at 22. These “New Consumers” are estimated to make up 30% of the U.S. population. *Id.* at 8. The “Triple Value Proposition” unites “practical benefits (e.g., cost savings, durability and style), social and environmental benefits (e.g., local, fair trade and biodegradable) and tribal benefits (e.g., connecting them to a community of people who share their values and aspirations).” *Id.* at 22.

<sup>18</sup> Steven Munch, *Improving the Benefit Corporation: How Traditional Governance Mechanisms Can Enhance the Innovative New Business Form*, 7 NW. J. L. & SOC. POL’Y 170, 170–71 (2012) (“While they plan to tackle social problems with business-like ideas and discipline, they also hope for some freedom from the pursuit of profit maximization.”).

<sup>19</sup> *Find a B Corp*, B CORPORATION, <http://www.bcorporation.net/community/directory> (last visited Sept. 30, 2013).

<sup>20</sup> Christen Clarke, *California’s Flexible Purpose Corporation: A Step Forward, A Step Back, or No Step At All?*, 5 J. BUS. ENTREPRENEURSHIP & L. 301, 308 (2012) (noting that this is also

pursues these three goals, while simultaneously meeting the needs of consumers advocating more transparency and higher standards of accountability among businesses.<sup>21</sup>

However, is a benefit corporation a social enterprise? A social enterprise is defined as “(1) an organization that serves first and foremost a social mission, (2) through the use of sophisticated business models . . . (3) pursuing multiple financing options, and (4) facing novel governance challenges when balancing the interests of donors and investors.”<sup>22</sup> When using this definition, and examining a social enterprise’s main purpose to “create social benefits from those whose lives it touches,”<sup>23</sup> it appears that the benefit corporation movement has separated itself from being placed *solely* in the social enterprise box. Benefit corporations will sometimes fit within the social enterprise categorization; however, not all benefit corporations can be categorized as a social enterprise. While general social purpose is woven into its articles of incorporation, the ability to pursue profit is still strongly within a benefit corporation’s focus.<sup>24</sup> While “[t]he general public understands traditional charity, as well as for-profit business . . . [it] does not yet fully understand companies that balance both financial and social gain.”<sup>25</sup> In explaining benefit corporations, it is important for them to be distinguished from social entrepreneurship, yet not separated from the movement’s energy to commit to best business practices that entail more than a singular focus on profit.

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commonly defined as people, planet, and profit); *see also Triple Bottom Line*, THE ECONOMIST (Nov. 17, 2009), <http://www.economist.com/node/14301663> (adapted from TIM HINDLE, THE ECONOMIST GUIDE TO MANAGEMENT IDEAS AND GURUS (2008)). The Triple Bottom Line consists of:

[T]he traditional measure of corporate profit—the “bottom line” of the profit and loss account. The second is the bottom line of a company’s “people account”—a measure in some shape or form of how socially responsible an organisation [sic] has been throughout its operations. The third is the bottom line of the company’s “planet” account—a measure of how environmentally responsible it has been.

*Id.*

<sup>21</sup> Anurag Gupta, *L3Cs and B Corps: New Corporate Forms Fertilizing the Field Between Traditional For-Profit and Nonprofit Corporations*, 8 N.Y.U. J.L. & BUS. 203, 221–22 (2011).

<sup>22</sup> Keren G. Raz, *Toward an Improved Legal Form for Social Enterprise*, 36 N.Y.U. REV. L. & SOC. CHANGE 283, 287–88 (2012).

<sup>23</sup> *Id.* at 289.

<sup>24</sup> *Id.* at 290. The idea of the public giving donations to Patagonia is a strange one, whereas the idea of the public donating to a project such as the social enterprise Ghana Sustainable Aid Project, that has founded a portable internet café in a Ghanaian village, is more palatable. *Id.*

<sup>25</sup> *Id.* at 300.

*B. Benefit Corporation v. B Corp*

Going forward, there must also be an understanding of the difference between a benefit corporation and a B Corporation (B Corp). A benefit corporation relates to a business that has undergone the changes in its articles of incorporation, modified its decision-making structure, and agreed to the other stipulations of California's Corporate Code for incorporation.<sup>26</sup> However, being a legal benefit corporation does not mean that the business is also automatically certified as a B Corp.<sup>27</sup> Stated differently, the B Corp label is not a requirement for the legal status.<sup>28</sup> A benefit corporation can fully and legally function without it.<sup>29</sup>

To become a B Corp, a company must work directly with the renowned non-profit organization that spearheaded benefit corporation legislation, B Lab.<sup>30</sup> To attain the B Corp label, an entity must go through an interviewing and certification process, which includes a comprehensive analysis of "its governance, suppliers, employees, and social and environmental impacts."<sup>31</sup> A company must attain an 80/200 score in a self-analysis, which is then verified by B Lab, to become eligible for the label.<sup>32</sup> B Lab charges an annual \$500 fee for companies with annual sales under \$2 million.<sup>33</sup> The B Lab requirements differ by state depending upon whether the state has a constituency statute.<sup>34</sup> In California, where no constituency statute exists, current corporations must become a legal benefit corporation entity within two years of B Corp certification.<sup>35</sup> Limited Liability Companies ("LLCs") and low-profit limited liability companies ("L3Cs") must amend their governing documents to adopt

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<sup>26</sup> *What is the Difference Between a B Corporation and a Benefit Corporation?*, B REVOLUTION CONSULTING, INC. (June 21, 2012), <http://www.brevolutionconsulting.com/becoming-a-b-part-1-what-is-the-difference-between-a-b-corporation-and-a-benefit-corporation>.

<sup>27</sup> *Id.*

<sup>28</sup> *Id.*

<sup>29</sup> *Id.*

<sup>30</sup> *Id.*

<sup>31</sup> *Id.*

<sup>32</sup> *Id.*; see also Dirk Sampsel, *The ABC's of B Corporations: Getting a Balanced Profit/Impact Strategy*, CSRWIRE (Aug. 30, 2013, 8:55 AM), <http://www.csrwire.com/blog/posts/996-the-abcs-of-b-corporations-getting-a-balanced-profit-impact-strategy> (noting that these impact metrics provide "a concrete set of measureable, manageable performance variables that can be used to structure performance objectives and incentives").

<sup>33</sup> *What is the Difference Between a B Corporation and a Benefit Corporation?*, *supra* note 25.

<sup>34</sup> *Legal Roadmap*, B CORP., <http://www.bcorporation.net/become-a-b-corp/how-to-become-a-b-corp/legal-roadmap/corporation-legal-roadmap> (last visited Nov. 15, 2013).

<sup>35</sup> B LAB, INC., TERM SHEET FOR B CORPORATIONS IN STATES THAT DO NOT HAVE CONSTITUENCY STATUTES (2012), available at [http://bcorp.nonprofitsoapbox.com/storage/documents/term\\_sheet\\_non-constituencybenefit\\_3.pdf](http://bcorp.nonprofitsoapbox.com/storage/documents/term_sheet_non-constituencybenefit_3.pdf) (for corporations in states that do not have constituency statutes where Benefit Corporation is available).

the B Corp legal framework within ninety days of certification or adopt the benefit corporation legal status within one year.<sup>36</sup> A sole proprietorship, because it is not formally organized as a business and has no corporate governing documents, can attain the B Corp certification without adopting the legal entity status.<sup>37</sup> The certified B Corp must complete a B Impact Assessment™ once every two years to maintain its status, and within that two year period, may be chosen as one of the 20% randomly selected B Corps to undergo an on-site audit.<sup>38</sup>

The B Corp status is an asset to companies for three main reasons: marketing, consumer trust, and performance improvement. One survey found that 52% of consumers rely on certification seals when buying products.<sup>39</sup> With the B Corp label attached to its brand, businesses can leverage their marketing power to reach such consumers that share their values, especially as entities like Method and Seventh Generation build notoriety for the label's branding power.<sup>40</sup> Since the B Corp label backs up this marketing power with third-party accountability, consumers can trust the label and the company.<sup>41</sup> In addition, with the B Corp label, benefit corporations are given free publicity through featured articles about B Lab and the burgeoning movement.<sup>42</sup> B Corps are offered discounted service partnerships, networking opportunities, and can more easily attract talent with their visible commitment to the triple bottom line.<sup>43</sup> Also, by using the B Impact Assessment tool, businesses can compare themselves against an average score of other businesses who have used the tool and identify ways to improve.<sup>44</sup>

Without acquiring the B Corp label in conjunction with legally incorporating as a benefit corporation, it may be hard for businesses, at this point and time, to generate the same sort of marketing benefits. However, as notoriety of the benefit corporation movement builds, the time may be

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<sup>36</sup> B LAB, INC., TERM SHEET FOR B CORPORATIONS IN STATES WITH CONSTITUENCY STATUTES, LLCs, AND PARTNERSHIPS (2012), available at [http://www.bcorporation.net/sites/all/themes/adaptivetheme/bcorp/pdfs/term\\_sheet\\_constituency\\_states\\_llcs\\_llps\\_3.pdf](http://www.bcorporation.net/sites/all/themes/adaptivetheme/bcorp/pdfs/term_sheet_constituency_states_llcs_llps_3.pdf).

<sup>37</sup> *Legal Roadmap*, *supra* note 34.

<sup>38</sup> B LAB, INC., *supra* note 35.

<sup>39</sup> BEMPORAD & BARANOWSKI, *supra* note 5, at 1.

<sup>40</sup> *What is the Difference Between a B Corporation and a Benefit Corporation?*, *supra* note 26.

<sup>41</sup> Dirk Sampsele, *What Do B Corporations and Benefit Corporations Actually Do?*, CSRWIRE (Mar. 1, 2013, 9:00 AM), <http://www.csrwire.com/blog/posts/741-what-do-b-corporations-and-benefit-corporations-actually-do>.

<sup>42</sup> *Id.*

<sup>43</sup> *Become a B Corporation: The Business Case*, B REVOLUTION CONSULTING, INC. (2012), <http://www.brevolutionconsulting.com/articles/become-a-b-corporation-the-business-case>.

<sup>44</sup> *Benchmark Performance*, B CORP. (2012), <http://www.bcorporation.net/become-a-b-corp/why-become-a-b-corp/benchmark-performance>; *Compare Your Impact*, B CORP. (2012), <http://bimpactassessment.net/how-it-works/compare-your-impact>.

approaching when a company will not need the additional label.

### *C. California's Adoption of Benefit Corporation Legislation*

As of September 2013, twenty states have passed legislation to integrate the benefit corporation within their corporate codes, and such legislation has been introduced in fifteen other states.<sup>45</sup> Notably, in July 2013, Delaware, which is arguably “the most important state for businesses that seek access to venture capital, private equity, and public capital markets,”<sup>46</sup> signed the legislation into law.<sup>47</sup> The model provision requirements of a benefit corporation include: stating an express purpose in the articles of incorporation to incorporate as a benefit corporation, committing to a general public benefit purpose,<sup>48</sup> requiring the board of directors to consider the effect its decision will have on the business’s stakeholders when pursuing the corporation’s “best interests,”<sup>49</sup> and ensuring accountability through a required annual benefit report which includes a “review of its social and environmental performance prepared ‘in accordance with a third party standard.’”<sup>50</sup>

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<sup>45</sup> *State-by-State Legislative Status*, B CORP., <http://benefitcorp.net/state-by-state-legislative-status> (last visited Sept. 30, 2013). The twenty states that have enacted such legislation include: Arizona, Arkansas, California, Colorado, Delaware, Hawaii, Illinois, Louisiana, Maryland, Massachusetts, Nevada, New Jersey, New York, Oregon, Pennsylvania, Rhode Island, South Carolina, Vermont, Virginia, and Washington, D.C. *Id.* Legislation has been introduced in Alabama, Connecticut, Florida, Georgia, Idaho, Iowa, Kansas, Kentucky, Minnesota, Montana, New Hampshire, Ohio, Utah, West Virginia, and Wisconsin. *Id.*

<sup>46</sup> Jay Coen Gilbert, Bart Houlahan & Andrew Kassoy, *Today Marks a Tipping Point in the Evolution of Capitalism*, FORBES (July 17, 2013, 9:30 AM), <http://www.forbes.com/sites/skollworldforum/2013/07/17/today-marks-a-tipping-point-in-the-evolution-of-capitalism> (noting that Delaware is “home to 1 million businesses, including 50% of all publicly-traded companies and 64% of the Fortune 500”).

<sup>47</sup> *Id.*

<sup>48</sup> Munch, *supra* note 18, at 186; *see also* MODEL BENEFIT CORP. LEGISLATION § 201 (B Lab, Inc. 2013), *available at* <http://benefitcorp.net/attorneys/model-legislation>. In addition to the requirement of a general public benefit purpose, a benefit corporation is allowed to tack on specific public benefit purposes, but is not required to do so. *Id.* § 201(a)–(b). With this general purpose, a business becomes “constitutionally committed to being socially responsible.” Page & Katz, *supra* note 7, at 1376.

<sup>49</sup> MODEL BENEFIT CORP. LEGISLATION § 301(a) (B Lab, Inc. 2013), *available at* <http://benefitcorp.net/attorneys/model-legislation>. Seven interests are listed that the committees of the board and individual directors “shall consider” when making decisions: (1) the shareholders, (2) the employees and work force, (3) the interests of customers as beneficiaries of the general public benefit or specific public benefit purposes of the corporation, (4) the community and societal factors, including those of each community in which offices or facilities are located, (5) the local and global environment, (6) the short-term and long-term interests of the corporation itself, and (7) the ability of the corporation to accomplish its general public benefit purpose and any specific public benefit purpose. *Id.*

<sup>50</sup> Munch, *supra* note 18, at 186. *See* GREYSTON BAKERY, BENEFIT CORPORATION REPORT (2012), *available at* <http://www.greystonbakery.com/wp-content/uploads/2013/01/greyston-annual>

A general public benefit purpose is required, compared to a specific benefit purpose, because a benefit corporation is committed to the idea of comprehensive consideration of multiple stakeholders in decision-making.<sup>51</sup> This prevents the pursuit of one narrowly-focused purpose while forsaking all other stakeholders.<sup>52</sup>

The model provision ensures exoneration of a director from *personal* liability both for actions performed in compliance with the state's corporate law dictating directors' duties, and actions that cause the failure of the benefit corporation to pursue or create general public benefit.<sup>53</sup> Furthermore, "the director does not have a duty to a person that is a beneficiary of the general public benefit purpose or a specific public benefit purpose."<sup>54</sup> When making decisions, directors are not required to "give priority to the interests of a particular person or group . . . over the interests of any other person or group unless the benefit corporation has stated in its articles its intention to give priority to certain interests related to . . . its general public benefit purpose."<sup>55</sup>

The model provision creates a new role of "benefit director," an independent individual who is tasked with preparing the annual benefit report and offering his opinion on the directors' compliance with their responsibilities in the detailed decision-making process.<sup>56</sup> Also, in furthering accountability, the model provision lays out the "right of action" limitations and standing for

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[2012 ks 05.pdf](#), for an example of a benefit report.

<sup>51</sup> DAN OSUSKY, ASSESSING IMPACT: A GUIDE TO THIRD PARTY STANDARDS FOR BENEFIT CORPORATIONS 1, 4 (2012), *available at* <http://www.brevolutionconsulting.com/assets/Assessing-Impact-A-Guide-to-Third-Party-Standards-for-Benefit-Corporations.pdf>.

<sup>52</sup> *Id.*

<sup>53</sup> MODEL BENEFIT CORP. LEGISLATION § 301(c) (B Lab, Inc. 2013), *available at* <http://benefitcorp.net/attorneys/model-legislation>.

<sup>54</sup> *Id.* § 301(d).

<sup>55</sup> *Id.* § 301(a)(3).

<sup>56</sup> *Id.* § 302. Some academics have expressed concern that this annual benefit report is still not rigorous enough to ensure that abuse is absent and there is no skewed reporting. Gupta, *supra* note 21, at 203, 224–25. Addressing these concerns, others have stressed that, "to be effective in the context of social goals, external accountability must align both with individuals' intrinsic motivation and institutions' internal accountability framework." Briana Cummings, *Benefit Corporations: How to Enforce a Mandate to Promote the Public Interest*, 112 COLUM. L. REV. 578, 617 (2012). Cummings goes on to advocate that third-party accountability is important and should be used externally through an "institutional intermediary," who would foster "professional accountability by pooling knowledge between members of an industry and 'develop[ ] a community of practice to sustain . . . inquiry and learning.'" *Id.* at 622. One proposal for this institutional intermediary is the development of the internal role of an "organizational catalyst," an individual with "high status, high social and intellectual capital, sufficient resources, 'direct lines of communication . . . [to] chief executives,' and who is otherwise strategically placed within the organization to mobilize learning and change by communicating with peers in their cultural/professional language." *Id.* at 624. By "mobiliz[ing] change by developing experiments, analyzing their effects, and reporting on them to the external regulator," the organizational catalysts "contribute to adaptive learning and to both external and internal accountability." *Id.*

proceedings against the benefit corporation; it notes, “except in a benefit enforcement proceeding,<sup>57</sup> no person may bring an action or assert a claim against a benefit corporation or its directors or officers with respect to: (1) failure to pursue or create a general public benefit . . . or (2) violation of an obligation, duty, or standard of conduct . . . .”<sup>58</sup> It derives standing for a benefit enforcement proceeding only to the benefit corporation itself, or derivatively by shareholders, directors, people that own beneficially, or of record, five percent or more of outstanding equity interests in “an entity in which the benefit corporation is a subsidiary,”<sup>59</sup> or other persons as specified in the benefit corporation’s articles of incorporation or bylaws.<sup>60</sup>

These model provisions were modified per the enacting twenty states’ legislative documents.<sup>61</sup> In California, the model legislation was changed to exclude the requirement of the role of a benefit director.<sup>62</sup> In addition, California added provisions to give dissenter stakeholders rights upon amendment of articles for election of status as a benefit corporation,<sup>63</sup> or upon termination of the status of a benefit corporation.<sup>64</sup> California has also expanded the definition of a benefit enforcement proceeding to allow a claim or action if a benefit corporation fails to deliver or post the required annual benefit report.<sup>65</sup> In addition, California stipulates that the reorganization of a benefit corporation “would have the effect of terminating the status of a corporation as a benefit corporation, [and] the reorganization shall not be effective unless the

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<sup>57</sup> MODEL BENEFIT CORP. LEGISLATION § 102 (B Lab, Inc. 2013), *available at* <http://benefitcorp.net/attorneys/model-legislation>. The Model code defines a benefit enforcement proceeding as: “[a]ny claim or action for: (1) failure of a benefit corporation to pursue or create general public benefit or a specific public benefit purpose set forth in its articles; or (2) violation of any obligation, duty, or standard of conduct under this [chapter].” *Id.*

<sup>58</sup> *See id.* § 305(a)(1)(i)-(ii).

<sup>59</sup> *Id.* § 305(c).

<sup>60</sup> *Id.*

<sup>61</sup> *Model Legislation, B CORP.* (2012), <http://benefitcorp.net/legislators/model-legislation>. The Model Legislation “reflects the expressed needs of business leaders and investors interested in using the power of business to solve social and environmental problems, and has been conformed to local corporate codes by local corporate attorneys.” *Id.*

<sup>62</sup> CAL. CORP. CODE §§ 14600–14631 (Deering 2012); *see also State-by-State Analysis, BENEFIT CORP.*, [http://benefitcorp.net/storage/State\\_by\\_State\\_Analysis.pdf](http://benefitcorp.net/storage/State_by_State_Analysis.pdf). Compare California to the laws in Hawaii, New Jersey, and Vermont which keep the role of “benefit director” intact. *Id.*

<sup>63</sup> *Id.* § 14603(a) (explaining that, “[I]f the amendment is adopted, a shareholder of the corporation may, by complying with Chapter 13 (commencing with Section 1300) of Division 1, require the corporation to purchase at their fair market value the shares owned by the shareholder which are dissenting shares as defined in subdivision (b) of Section 1300 in accordance with the procedures in that chapter, as if the adoption of the amendment were a reorganization to which that chapter applies.”).

<sup>64</sup> *Id.* § 14603(a), 14604(a).

<sup>65</sup> *Id.* § 14601(b)(3).



reorganization is approved by at least the minimum status vote.”<sup>66</sup>

### III. COMPARISON OF BENEFIT CORPORATIONS TO OTHER LEGAL ENTITIES

Californian innovators have a long history of challenging the “status quo” of business.<sup>67</sup> Take for example the Skoll Foundation founded by the first president of eBay, the Omidyar Foundation established by the founder of Ebay, and Google.org, the philanthropic, for-profit branch of the world-renowned online search engine.<sup>68</sup> In founding such organizations that support social good, these leaders have publicly commented on the shift in societal thinking that needs to take place to merge profit maximization with long-term goals of sustainability and community development.<sup>69</sup>

However, in California where there are multiple hybrid business entity forms to choose from, is the benefit corporation legislation necessary? An entity doing business in California can incorporate as an LLC, low-profit limited liability company, flexible purpose corporation, non-profit, or a regular for-profit corporation—any of which can support social good in some capacity. Each has its unique challenges in helping businesses that are pursuing the triple bottom line.

#### *A. Limited Liability Company*

An LLC is considered a hybrid entity that merges the benefits of the single taxation of partnerships with the limited liability of a corporation.<sup>70</sup> The ability to limit fiduciary duties through an LLC’s articles of incorporation, and gain more flexibility in its management structure compared to a publicly traded corporation, has made this legal entity attractive to entrepreneurs.<sup>71</sup> An LLC

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<sup>66</sup> *Id.* § 14604(b).

<sup>67</sup> Patrick Hanlon, *California Dreamin’: The New State of Innovation*, FORBES (Sept. 12, 2013, 12:42 PM), <http://www.forbes.com/sites/patrickhanlon/2013/09/12/california-dreamin-the-new-state-of-innovation>.

<sup>68</sup> Jay Milbrandt, *A New Form of Business Entity is Needed to Promote Social Entrepreneurship: The Not-For-Loss Corporation*, 1 J. BUS. ENTREPRENEURSHIP & L. 421, 422 (2008). The Skoll Foundation “seeks to advance systemic change in communities around the world through social entrepreneurship.” *Id.*

<sup>69</sup> *Id.* at 423–25. “I don’t see why we ought to make an artificial distinction that says for-profit is all about making money and only nonprofit is about helping people.” *Id.* at 423 (quoting Pierre Omidyar).

<sup>70</sup> Clarke, *supra* note 20, at 305–06.

<sup>71</sup> *Id.* at 306 n.48 (quoting Celia R. Taylor, *Carpe Crisis: Capitalizing on the Breakdown of Capitalism to Consider the Creation of Social Businesses*, 54 N.Y.L. SCH. L. REV. 743, 751–52 (2009/2010)).

“can create a mission of social good instead of maximizing profits,”<sup>72</sup> and can “receive funding from non-profit, grant-making organizations.”<sup>73</sup> The parties to an LLC have the freedom of contract to bargain for whatever business provisions and internal structure they desire, with no mandate that the LLC must express its purpose or objectives in its certificates of formation.<sup>74</sup> However, no accountability structure exists to assist consumers in finding out if the LLC is following through on its social missions.

### *B. Low-Profit Limited Liability Company*

The L3C was created as a separate entity from the LLC for companies that wanted to wholeheartedly pursue a “socially beneficial purpose,”<sup>75</sup> while attracting diversified capital in the form of program-related investments (“PRIs”) from foundations.<sup>76</sup> PRIs meet foundations’ requirements under the IRS to dispose of “5% or more of their assets each year toward furthering their charitable activities.”<sup>77</sup> To qualify with the IRS as tax-exempt, a PRI “must meet the following requirements: (1) the primary purpose of the investment is to accomplish a charitable or educational purpose; (2) no significant purpose is the production of income or asset appreciation; and (3) no purpose is to promote a prohibited political or legislative purpose.”<sup>78</sup> Advocates for the L3C entity believe that the funding flexibility of an L3C to receive PRIs, grants, and private investments would expand the horizon of available capital for organizations existing for charitable purpose.<sup>79</sup>

The underlying idea of L3C formation, to gain foundations’ investment confidences, has been somewhat curtailed by the IRS’s refusal to grant an overarching blessing of PRIs as definitively tax-free.<sup>80</sup> Like an LLC, a L3C is

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<sup>72</sup> *Id.* at 306.

<sup>73</sup> *Id.* at 309.

<sup>74</sup> Ann E. Conaway, *The Global Use of the Delaware Limited Liability Company for Socially-Driven Purposes*, 38 WM. MITCHELL L. REV. 772, 811, 813 (2012). Please note that this is referring to an LLC under Delaware statutes. This may change according to the state where the entity has filed its documents of formation.

<sup>75</sup> Clarke, *supra* note 20, at 311.

<sup>76</sup> *Id.* PRIs allow “foundations to make contributions that are not taxed by the IRS, and they allow the foundation an opportunity to make a return on its investment.” *Id.*

<sup>77</sup> Jaclyn Cherry, *Charitable Organizations and Commercial Activity: A New Era Will the Social Entrepreneurship Movement Force Change?* 5 J. BUS. ENTREPRENEURSHIP & L. 345, 350 (2012).

<sup>78</sup> Clarke, *supra* note 20, at 311.

<sup>79</sup> Raz, *supra* note 22, at 298–99.

<sup>80</sup> Clarke, *supra* note 20, at 311. The IRS did, in a private letter ruling in 2006, state that a foundation’s investment in businesses that had been rejected traditional financing and the majority of the owners or controllers of the business were part of the disadvantaged community where the businesses were located. Conaway, *supra* note 75, at 805. This was an LLC that got PRI approval

not itself taxed, but rather the tax burden falls upon the shareholders “according to their respective share of the L3C’s income.”<sup>81</sup> To become a legal entity, the L3C must exist to pursue a charitable or educational purpose,<sup>82</sup> and not have a “significant purpose” in producing income nor in having a goal for any political or legislative purpose.<sup>83</sup> Critics of the L3C entity argue that the same purpose can be accomplished by an LLC, without such an extra designation.<sup>84</sup> Like the LLC, the L3C has “no clear mechanism” by which investors or consumers can ensure that the L3C is operating under its expressed purpose(s).<sup>85</sup> If an L3C starts to act outside of its charitable mission, its status can be revoked and converted to an LLC.<sup>86</sup>

### C. Flexible Purpose Corporation

In California, a separate hybrid entity has been created called a “flexible purpose corporation” (“FPC”).<sup>87</sup> Akin to the motives that have propelled the benefit corporation movement forward, the FPC was created after concerns were raised about the “lack of a ‘mission anchor’ when control changes hands” in the most vulnerable times for a company—during the early stages of high investor power, when a company is more vulnerable to being steered toward pure profit generation, and during the merger stages of new leadership.<sup>88</sup> Similarly, both legal entities require the company to write the social benefit pursuit promise into the DNA of its articles of incorporation, while affording the entities the freedom to pursue profit at the same time.<sup>89</sup>

Even if California were to have a constituency statute, which legally gives businesses the “option to consider nonshareholder interests,” the option is permissive rather than mandatory.<sup>90</sup> Both benefit corporations and FPCs make these stakeholder interests *mandatory* to consider in decision-making, but neither give the beneficiaries the standing to sue.<sup>91</sup> However, the FPC differs

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and the authors point out that “[w]hat is necessary is that the investment matches the mission and objectives of the foundation and the operating agreement reflects that mission.” *Id.*

<sup>81</sup> Clarke, *supra* note 20, at 312.

<sup>82</sup> Conaway, *supra* note 75, at 803. Such charitable purpose must fall under those delineated by the IRS as “religious, scientific, educational, literary, or charitable.” *Id.*

<sup>83</sup> Clarke, *supra* note 20, at 312.

<sup>84</sup> Conaway, *supra* note 75, at 782–83.

<sup>85</sup> *Id.* at 804.

<sup>86</sup> Cherry, *supra* note 78, at 351–52.

<sup>87</sup> CAL. CORP. CODE §§ 2500–3503 (Deering 2012).

<sup>88</sup> Clarke, *supra* note 20, at 317.

<sup>89</sup> *Id.* at 318; *see supra* text accompanying note 49.

<sup>90</sup> Clarke, *supra* note 20, at 322.

<sup>91</sup> *Id.* at 326.

from the benefit corporation in two main ways: (1) rather than call for a general public benefit, the FPC is only required to include a specific public benefit in its articles of incorporation,<sup>92</sup> and (2) the FPC, while still having the annual reporting requirements like the benefit corporation, is not held to a third-party standard.<sup>93</sup> Instead, it just must “specify objectives by which to measure the FPC’s impact as it relates to the special purpose.”<sup>94</sup> The flexible purpose corporation still does not help breach the gap of trust between consumers and corporations.

#### *D. Non-Profit Corporation*

The ability to pursue a social business as a non-profit corporation is stunted by the IRS’ strict constraints.<sup>95</sup> First, to qualify the entity as a non-profit organization, and thus gain tax exemption for its operations and for donors’ gifts directed toward the entity, an organization must be “organized and operated exclusively for religious, charitable, scientific, testing for public safety, literary, or educational purposes . . . .”<sup>96</sup> For an entity involved in a revenue-generating business, its actions are further regulated by the commerciality doctrine, which takes away tax exemption when “commercial activities . . . are not in furtherance of their exempt purposes.”<sup>97</sup> However, if the commercial activities, even if highly lucrative, are in furtherance of the exempt purpose, they may still qualify as tax-exempt.<sup>98</sup> This exemption is criticized as being unfair, especially when a non-profit organization is directly competing with non-tax exempt organizations within its commercial activities.<sup>99</sup> Thus, the IRS will slap the hands of *non-compliant* non-profit organizations with the unrelated business income tax (“UBIT”) when such organizations garner net income from: (1) a trade or business, (2) regularly carried on, that is (3) substantially unrelated to the

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<sup>92</sup> *Id.* at 324.

<sup>93</sup> *Id.* at 325.

<sup>94</sup> *Id.*

<sup>95</sup> Raz, *supra* note 22, at 293.

<sup>96</sup> I.R.C. § 501(c)(3) (West 2010). An organization includes corporations, community chests, funds or foundations. *Id.* Furthering this section, organizations that “foster national or international amateur sports competition (but only if no part of its activities involve the provision of athletic facilities or equipment), or for the prevention of cruelty to children or animals . . . .” are also recognized as tax-exempt. *Id.*

<sup>97</sup> Cherry, *supra* note 78, at 360. There are also restrictions of not letting net earnings inure to the benefit of any private shareholder or individual. *Id.*

<sup>98</sup> *Id.* at 361–63. The charitable organization’s purpose does not include pouring the money into the cause, but must be in direct line of helping the cause. *Id.* For example, Save the Children’s holiday catalogs generate fundraising, but do not directly further the purpose of saving the lives of vulnerable and exploitable children, and thus may not be tax-exempt. *Id.*

<sup>99</sup> *Id.* at 362.

organization's exempt purpose.<sup>100</sup> In trying to garner financing outside of commercial activity and donations, charitable organizations are quite restrained since they cannot pay dividends or make distributions of any earnings.<sup>101</sup>

#### *E. For-Profit Corporation*

California native, Google, was heralded in early 2006 in forgoing a non-profit structure for its new arm "Google.org," created to "find initiatives that will be sustainable and can receive economies of scale" instead of merely funneling money over to support causes.<sup>102</sup> The for-profit nature of Google.org allows flexibility that would be constrained by a non-profit structure; as a for-profit, it can more easily pursue "funding start-up companies, forming partnerships with venture capitalists, and lobbying lawmakers."<sup>103</sup>

However, though no legal action has taken place against Google.org, uncertainty arises when such an organization allots one billion dollars to pursue "arguably non-business purpose[s]," instead of distributing dividends.<sup>104</sup> Though dividends are never promised to shareholders, the expectation among owners is that the directors and officers will make decisions that will steer the corporation towards optimal performance and higher financial viability.<sup>105</sup> The concern is that Google may have opened itself up to "potential liability from stockholders for a due care cause of action [because] [t]his use of money will constantly be subject to the scrutiny of investors, who may challenge the organization's decisions."<sup>106</sup> Is Google protected by the fact that it was founded under the motto, "Don't Be Evil,"<sup>107</sup> and warned potential investors before going public of its plans to set aside "1% of the company's stock plus an equal percentage of profits for philanthropy"<sup>108</sup> before going public?

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<sup>100</sup> *Id.* at 366. A trade or business is defined when "activity that is carried on for the production of income from the sale of goods or the performance of services . . ." *Id.*

<sup>101</sup> Raz, *supra* note 22, at 293–94. This is other than paying its employees a salary. *Id.*

<sup>102</sup> Milbrandt, *supra* note 69, at 427.

<sup>103</sup> *Id.* at 427–28.

<sup>104</sup> *Id.* at 428.

<sup>105</sup> ALAN PALMITER & FRANK PARTNOY, CORPORATIONS: A CONTEMPORARY APPROACH 33, 36 (2010).

<sup>106</sup> Milbrandt, *supra* note 69, at 428.

<sup>107</sup> *Id.* at 425.

<sup>108</sup> *Id.* at 426.

## IV. IS THE BENEFIT CORPORATION NEEDED?

*A. The Business Judgment Rule Backdrop*

Many believe that it *is* enough under the Business Judgment Rule.<sup>109</sup> This rule “traditionally protects directors from liability for business decisions, even those that result in losses to the corporation.”<sup>110</sup> However, there must be some reality-testing to take into account that the “vast resources, [the] global vision . . . and [the] practically limitless budget for sophisticated legal counsel” of Google.org is anything but the norm for most businesses pursuing the triple bottom line.<sup>111</sup> An argument, also stemming from the Google.org story, has been made that if profits are redefined to incorporate not only monetary profit but to measure environmental footprints and social investments, the business judgment rule stands perfectly capable to legally protect a corporation’s decisions made in good faith.<sup>112</sup>

Academics believe that social and environmental endeavors are “investments that add both social and financial value to corporations’ bottom line and are therefore within the scope of the business judgment rule, and furthermore, that the board of directors has a duty to be informed of the potential for social entrepreneurship in their company.”<sup>113</sup> Professor Janet Kerr poignantly stated three reasons for why corporations should not be hesitant to pursue social entrepreneurship: (1) “judicial action and recent shareholder constituency statutes have opened the door to allow directors of public companies to take non-shareholder interests and concerns into consideration when making investment decisions,” (2) social entrepreneurship is wise investing, and (3) as social and financial impact is measured, research “shows that corporations are profiting from social entrepreneurship.”<sup>114</sup> These social investments are framed as supporting an entity’s long-term profitability, and such propositions have been supported with empirical evidence in specific

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<sup>109</sup> Janet E. Kerr, *Sustainability Meets Profitability: The Convenient Truth of How the Business Judgment Rule Protects a Board’s Decision To Engage in Social Entrepreneurship*, 29 CARDOZO L. REV. 623 (2007).

<sup>110</sup> PALMITER & PARTNOY, *supra* note 106, at 543.

<sup>111</sup> Thomas Kelley, *Law and Choice of Entity on the Social Enterprise Frontier*, 84 TUL. L. REV. 337, 345 (2009).

<sup>112</sup> Kerr, *supra* note 110, at 628 (quoting senior advisor of the Silicon Valley Community Foundation, Peter Hero, “I think how you count profit is the issue here . . . Google.org is measuring return on cleaner air and quality of life. Their bottom line isn’t just financial. It’s environmental and social.”).

<sup>113</sup> *Id.* at 633.

<sup>114</sup> *Id.* at 634–35.

business sectors.<sup>115</sup>

However, decision makers of social businesses have been operating under a long history of legal uncertainty. Some of the most oft-quoted corporate cases seem to support the idea of shareholder wealth maximization: the idea that directors and executives of a corporation are granted powers that “[are] at all times exercisable only for the ratable benefit of the shareholders.”<sup>116</sup> In the infamous case of *Dodge v. Ford Motor Co.*,<sup>117</sup> the Supreme Court of Michigan heard the complaint of Ford Motor Co. shareholders who opposed Mr. Ford’s desires to “continue the corporation henceforth as a semi-eleemosynary institution and not as a business institution.”<sup>118</sup> Ford’s view was that, “[a]lthough a manufacturing corporation cannot engage in humanitarian works as its principal business, the fact that it is organized for profit does not prevent the existence of implied powers to carry on with humanitarian motives such charitable works as are incidental to the main business of the corporation.”<sup>119</sup> The court commented that “a business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end.”<sup>120</sup> It expounded, stating that, “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.”<sup>121</sup> It should be noted that the court did not state that a corporation could not benefit others, just that this cannot be the “primary purpose.”<sup>122</sup> However, though often cited, the case does not hold water as a legal rule of shareholder wealth maximization.<sup>123</sup> Academics point out that: “(1) the oft-cited statements purporting to require shareholder primacy are mere dicta; (2) the case is old and no longer accurately represents corporate law; and (3) the decision came from a court that has little influence on corporate law.”<sup>124</sup>

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<sup>115</sup> Ioannou, *supra* note 11.

<sup>116</sup> Jessica Chu, *Filling a Nonexistent Gap: Benefit Corporations and the Myth of Shareholder Wealth Maximization*, 22 S. CAL. INTERDISC. L.J. 155, 165 (2012). This is a quote from the “Great Debate” between famous corporate law experts, Adolph Berle and Merrick Dodd. *Id.* It should be noted that Dodd actually won the debate when it took place in 1950s with his “stakeholder viewpoint” that a “public company’s purpose ‘included providing secure jobs for employees, quality products for consumers, and contributions to the broader society.’” *Id.* at 166.

<sup>117</sup> *Dodge v. Ford Motor Co.*, 170 N.W. 668 (Mich. 1919).

<sup>118</sup> *Id.* at 683.

<sup>119</sup> *Id.* at 684.

<sup>120</sup> *Id.*

<sup>121</sup> *Id.*

<sup>122</sup> *Id.*

<sup>123</sup> Chu, *supra* note 117, at 175–76.

<sup>124</sup> *Id.* at 175 (quoting Lynn A. Stout, *Why We Should Stop Teaching Dodge v. Ford*, 3 VA. L. & BUS. REV. 163, 166–67 (2008)). “Dicta” refers to a remark made by the court that “does not establish legal precedent and can be disregarded by future courts.” *Id.* at 176.

However, the case is still taught in Corporation courses across the nation, and few cases have reached the courts to set precedent for the triple bottom line business movement once and for all.

One of the most recent cases directed towards the business judgment rule came to the Delaware Court of Chancery in 2010 in *eBay v. Newmark*<sup>125</sup>, when the founder of Craigslist and his CEO were brought to court by minority shareholder, eBay, for implementing a “poison pill rights plan” that essentially “prevented eBay from mounting a takeover campaign . . . [and] from selling more than 15% of its stock to a buyer other than Jim or Craig.”<sup>126</sup> Craig Newmark incorporated his pet project, Craigslist, as a for-profit Delaware corporation, but boasted in its “relatively non-commercial nature, public service mission, and non-corporate culture.”<sup>127</sup> The Delaware Court of Chancery struck down Craigslist’s poison pill rights plan on several grounds, one of which was “that because [C]raigslist rejects shareholder value maximization, its action was motivated by an impermissible corporate purpose as a matter of law.”<sup>128</sup> The court expounded on this, stating: “I cannot accept as valid for the purposes of implementing the [poison pill] 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.”<sup>129</sup>

Since Delaware is widely respected as the leading corporate law state,<sup>130</sup> such strong language has led academics to take Delaware’s stance to mean that “stockholder wealth maximization is the only game in town”<sup>131</sup> and to caution that this strong stance would impinge upon contracting parties who “mutually consent to shareholder value-eschewing purposes.”<sup>132</sup> However, Delaware Governor Jack Markell’s recent enthusiastic support for benefit corporation businesses that are profitable and see profits “as a means to fuel growth in social impact as well as to generate attractive returns for stockholders,”<sup>133</sup> tells another tale. According to Governor Markell, Delaware has implemented benefit corporations as a new entity for current companies who “feel understandably constrained by existing corporate law that recognizes only one legitimate

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<sup>125</sup> *eBay Domestic Holdings, Inc. v. Newmark*, 16 A.3d 1 (Del. Ch. 2010).

<sup>126</sup> David A. Wishnick, *Corporate Purposes in a Free Enterprise System: A Comment on eBay v. Newmark*, 121 YALE L.J. 2405, 2407 (2012).

<sup>127</sup> *Id.* at 2405.

<sup>128</sup> *Id.* at 2408.

<sup>129</sup> *Id.* at 2410.

<sup>130</sup> PALMITER & PARTNOY, *supra* note 106, at 41.

<sup>131</sup> Wishnick, *supra* note 127, at 2412.

<sup>132</sup> *Id.*

<sup>133</sup> Jack Markell, *A New Kind of Corporation to Harness the Power of Private Enterprise for Public Benefit*, THE HUFFINGTON POST (July 22, 2013, 2:06 PM), [http://www.huffingtonpost.com/gov-jack-markell/public-benefit-corporation\\_b\\_3635752.html](http://www.huffingtonpost.com/gov-jack-markell/public-benefit-corporation_b_3635752.html).



purpose—to maximize value for stockholders.”<sup>134</sup> Delaware’s leaders envision that:

[N]ew Delaware public benefit corporations will harness the power of private enterprise to create public benefit . . . . In the long term, as many enter the public capital markets, they will help combat the plague of short termism that we have seen over the last five years can undermine a shared and durable prosperity.<sup>135</sup>

*B. The Business Judgment Rule and The Corporate Growth Phase*

As is evident from *eBay v. Newmark*, there are chinks in the armor of the business judgment rule when it comes to corporations’ growth stages, especially when it comes to hostile takeovers or corporate mergers.<sup>136</sup> When comparing traditional corporations with California’s new social business hybrids, a major concern is over this “accountability gap” between directors and shareholders.<sup>137</sup> In California, where no constituency statute is present, there is uncertainty as to what may happen during this phase where valuation of the company for stockholder wealth maximization is in the limelight.<sup>138</sup> The Delaware Supreme Court has held that “concern for non-stockholder interests is inappropriate when an auction among active bidders is in progress, and the object no longer is to protect or maintain the corporate enterprise but to sell it to the highest bidder.”<sup>139</sup> Once in this “Revlon mode,” the board’s “decision-making process face[s] heightened scrutiny when challenged in court.”<sup>140</sup>

An argument has been made that courts may be more hesitant to apply the Revlon ruling when it is at the expense of social purposes woven into a corporation’s articles of incorporation, such as is required with benefit corporations.<sup>141</sup> Although both benefit corporations and flexible purpose corporations write purposes into their charters, neither “take[s] a redistributive

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<sup>134</sup> *Id.*

<sup>135</sup> *Id.*

<sup>136</sup> Alicia E. Plerhoples, *Can an Old Dog Learn New Tricks? Applying Traditional Corporate Law Principles to New Social Enterprise Legislation*, 13 TENN. J. BUS. L. 221, 243 (2012).

<sup>137</sup> *Id.* at 228.

<sup>138</sup> *Id.* at 242.

<sup>139</sup> *Id.* at 244. This Delaware takeover doctrine is enacted when a business’ board decides “to exchange a controlling stake in the company, either for cash or non-voting securities, or for voting shares in an acquirer with a controlling shareholder but not when it exchanges 100% of its voting shares for voting shares in a widely held acquirer, most commonly through a stock-for-stock merger.” *Id.*

<sup>140</sup> *Id.*

<sup>141</sup> *Id.* at 250. This holds true for flexible purpose corporations as well. *Id.*

approach” in delegating powers of rights of actions to beneficiaries other than the shareholders and the corporation itself.<sup>142</sup> This stance to maintain the shareholder primacy norm is a persuasive statement that “shareholders’ interests are more than just financial.”<sup>143</sup> It has been proposed that in times of corporate acquisitions of social enterprises, a similar fiduciary analysis to the Revlon mode’s analysis of a board’s decision-making process will be enacted, but will expand the evaluation of a firm’s value to its ability to “create social and environmental value.”<sup>144</sup>

In the United States, the “legal rules governing the corporation’s actors are an amalgam of state statutes, judicial decisions, and privately created default rules.”<sup>145</sup> While states’ corporate codes “do not limit the corporate purpose of a corporation to shareholder wealth maximization,”<sup>146</sup> many states have still adopted constituency statutes that “explicitly authorize directors to consider interests of . . . employers, creditors, customers, suppliers, and the community.”<sup>147</sup> However, for California and other states that do not have constituency statutes, businesses face difficulty in trying to toe the lines of legality in decision-making.<sup>148</sup>

A recognizable “dissensus within the law and business communities” exists in defining “what corporate purposes are justifiable.”<sup>149</sup> Since the decision in *Smith v. Van Gorkom*, the stress placed on a board’s informed decision-making has been paramount in the corporate legal world.<sup>150</sup> Board members become informed through “the process of gaining sufficient familiarity with the background facts and circumstances in order to make an informed judgment.”<sup>151</sup> Thus, many courts’ evaluations of a board’s decisions become highly process-oriented.<sup>152</sup>

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<sup>142</sup> *Id.*

<sup>143</sup> *Id.*

<sup>144</sup> *Id.* at 263.

<sup>145</sup> PALMITER & PARTNOY, *supra* note 106, at 40.

<sup>146</sup> Chu, *supra* note 117, at 168.

<sup>147</sup> *Id.* at 172.

<sup>148</sup> *Id.* at 173.

<sup>149</sup> Wishnick, *supra* note 127, at 2412. Wishnick also notes that a precedent that focuses on making profit maximization mandatory would “limit entrepreneurs’ abilities to satisfy the ethical preferences of [the] minority of investors.” *Id.* at 2413. Some academics argue that while corporate law does encourage shareholder primacy, shareholder wealth maximization itself is “not a legal mandate . . . [but rather] a standard of conduct that has been accepted as the most efficient way to control the actions of directors.” Chu, *supra* note 117, at 180.

<sup>150</sup> PALMITER & PARTNOY, *supra* note 106, at 563, 569.

<sup>151</sup> *Id.* at 569 (quoting the MODEL BUS. CORP. ACT § 8.30(b) cmt. (2007)).

<sup>152</sup> *Id.*

## V. WHY A BENEFIT CORPORATION IS GOOD BUSINESS

### *A. Process-Oriented*

The benefit corporation legislation buttresses the business judgment rule by not only writing a social purpose into a company's DNA, but by also offering a detailed process for boards' decision-making.<sup>153</sup> Thus, the benefit corporation legislation "removes the legal uncertainty that directors face by simply making mission-driven companies legal."<sup>154</sup> In addition, by requiring an annual benefit report that details the benefit corporation's activity in pursuing its general social purpose, increased documentation of decision-making processes will most likely occur. Thus, in the case of a benefit corporation merger or acquisition, a board will have a better argument for its decisions under both the combined benefit corporation legislation and the business judgment rule. As the market percentage of conscious consumers continues to increase, and as businesses catch on that the mission can be profitable for drawing the top employees, corporate buy-outs and mergers of benefit corporations may see a rapid increase.<sup>155</sup> California corporate lawyers need to be ready to guide their benefit corporations through this process, especially when it comes to the interaction between shareholder rights.

Critics target these shareholders rights as a source of potential abuse and increased liability for businesses that undertake incorporation as a benefit

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<sup>153</sup> MODEL BENEFIT CORP. LEGISLATION § 301(a) (B Lab, Inc. 2013), available at <http://benefitcorp.net/attorneys/model-legislation>. Seven interests the committees of the board and individual directors "shall consider" when making decisions include: (1) the shareholders, (2) the employees and work force, (3) the interests of customers as beneficiaries of the general public benefit or specific public benefit purposes of the corporation, (4) the community and societal factors, including those of each community in which offices or facilities are located, (5) the local and global environment, (6) the short-term and long-term interests of the corporation itself, and (7) the ability of the corporation to accomplish its general public benefit purpose and any specific public benefit purpose. *Id.*

<sup>154</sup> Chu, *supra* note 117, at 183. When the Golden Gate Bridge was under construction, the investment in a vast safety net "gave workers an abiding sense of security as they moved more freely—and quickly—across the slippery, half-constructed steel." *Work Site Safety and Accidents*, PBS, <http://www.pbs.org/wgbh/americanexperience/features/general-article/goldengate-safety/> (last visited April 4, 2013). Like the safety net, the benefit corporation legislation will give business managers a sense of freedom in enacting projects that they may have been wary of without the legal assurance that they are fully protected.

<sup>155</sup> Kerr, *supra* note 110, at 629 (quoting GlaxoSmithKline CEO Jean-Pierre Garnier who observed that when the pharmaceutical giant decided to pursue social good by selling 90% of their vaccines at or below cost in developing countries, it had a new competitive advantage: "Top scientists are drawn to GSK because they want their research to make a difference. Doing good, and being admired for it, also boosts general morale at the company . . . [which] creates a more aligned workforce, which helps us outperform our competitors.").

corporation.<sup>156</sup> In writing into the articles of incorporation the right of shareholders to bring enforcement proceedings,<sup>157</sup> a business hands more power to shareholders to bring action “on the basis that a director or officer failed to pursue or create . . . the public benefit purpose . . . [or] failed to consider the interests of the various stakeholders.”<sup>158</sup> However, this extra enforcement goes towards the increased accountability that creates the consumer trust that is an advantage of the benefit corporation and that is “specifically desired by most of the mission-driven entrepreneurs and investors interested in new corporate form legislation.”<sup>159</sup> The allowance of such proceedings allows shareholders to prevent the company from green-washing techniques that can destroy consumer trust and harm the company’s reputation.<sup>160</sup> As the California Corporate Code makes clear, this right of action is limited to owners, and does not carry over to third parties or beneficiaries of the benefit corporation’s general public purpose.<sup>161</sup>

### *B. Accountability*

The requirement of a third-party standard in the benefit corporation’s annual report ensures that the company does not “simply choose what information [it] wish[es] to relay” and deceive consumers, but that it keeps accountable to a metric that is a “recognized standard for defining, reporting and assessing corporate, social, and environmental performance which is comprehensive, independent, credible, and transparent.”<sup>162</sup> For California benefit corporations, the requirement of this standard does not translate into requiring an audit, but means that they are “allowed to self-report” and conform not to an organization, but just to the third-party standard.<sup>163</sup> While the corporation maintains the discretion to select the standard it abides by for the annual report, it still must provide its rationale for doing so.<sup>164</sup> Essentially, “[t]he

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<sup>156</sup> Chu, *supra* note 117, at 186.

<sup>157</sup> See *supra* text accompanying notes 58–61.

<sup>158</sup> Chu, *supra* note 117, at 186.

<sup>159</sup> *What Are My Liabilities?* B CORP., <http://benefitcorp.net/for-directors/what-are-my-liabilities> (last visited Sept. 30, 2013).

<sup>160</sup> See *supra* text accompanying notes 8–9.

<sup>161</sup> CAL. CORP. CODE § 14623 (Deering 2012).

<sup>162</sup> OSUSKY, *supra* note 52, at 4. The chosen third-party standard must be: (1) *comprehensive* in order to consider not just environmental impact, while ignoring human right, (2) properly *fit* the intended purpose of benefit corporations to pursue a general public benefit, and (3) *independent*, so that the chances that the company could manipulate the outcome are drastically reduced. *Id.*

<sup>163</sup> *Id.* at 6. For a list of examples of different third-party standards available to California benefit corporations to use in compliance of the statute, see *Id.* at 17–23.

<sup>164</sup> *Id.* at 4, 6.

third party standard requirement is meant to maintain the integrity of benefit corporations, and the statute maintains the integrity of the standards themselves.”<sup>165</sup>

The credibility requirement for a standard ensures that the creating third party is recognized for its expertise in “social and environmental impact” and stipulates that a developed standard must undergo a “public review period (of at least 30 days) in which stakeholders are able to provide commentary.”<sup>166</sup> The standard’s transparency requirement keeps the benefit corporation and the third-party accountable to the public, who is able to easily access information regarding the weighting of the scores, the third-party members who helped develop the standard, the third-party’s funding strategy, and “the method in which the standard is developed and revised.”<sup>167</sup> Such transparency and accountability helps bridge the gap of mistrust between many consumers and businesses in the American economy.

Some critics believe that the creation of benefit corporations will have no hand in changing normative thinking among the business sector, but will actually “further[] the unwarranted belief that ‘regular’ corporations are unable to do social good.”<sup>168</sup> They state that large, public corporations will not adopt benefit corporation legislation due to the main hurdles of having to adopt a general social purpose and having to accrue costs to publish an additional annual report.<sup>169</sup> However, as the California Corporate Code elaborates, the general social purpose that is required to be written into the articles of incorporation is very broad itself.<sup>170</sup> Thus, the businesses would not be limited in the activity they pursue, as long as they are simultaneously impacting society and the environment for the better.<sup>171</sup> Further, while there may indeed be upfront costs for businesses in compiling and publishing the annual benefit report, the growth

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<sup>165</sup> *Id.* at 11.

<sup>166</sup> *Id.* at 5.

<sup>167</sup> *Id.*

<sup>168</sup> Chu, *supra* note 117, at 187.

<sup>169</sup> *Id.* at 186–87. Adding a general purpose requires an amendment to the articles of incorporation, and thus, critics argue that the corporations will not want to limit the activities they legally are able to pursue. *Id.*

<sup>170</sup> CAL. CORP. CODE § 14601 (Deering 2012). “‘General public benefit’ means a material positive impact on society and the environment, taken as a whole, as assessed against a third-party standard, from the business and operations of a benefit corporation.” *Id.*

<sup>171</sup> With the adoption of benefit corporation status amongst businesses such as King Arthur Flour, Method, and Seventh Generation—all business that have nation-wide distribution chains—it can be seen that large businesses are able to pursue this joint endeavor successfully. *An Evolution in Impact Measurement*, B CORP. (2012), <http://www.bcorporation.net/blog/an-evolution-in-impact-measurement>; *Seventh Generation: Committed to Impact*, THE BLOG (Feb. 28, 2013), <http://www.bcorporation.net/blog/seventh-generation-committed-to-impact>; *Find a B Corp*, B CORP. (2012), <http://www.bcorporation.net/community/find-a-b-corp>.

rate of the benefit corporation community is evidence that this idea is gaining traction. Businesses may be willing to pay a larger up-front investment when they can also reap the movement's branding potential.

### C. Cross-Sector Social Partnerships

Another positive aspect of benefit corporation status is seen in the pursuit of "cross-sector social partnerships."<sup>172</sup> In the light of green-washing techniques and distrust of CSR,<sup>173</sup> such partnership can give benefit corporations the extra endorsement of authenticity in their statements of general social purpose. In addition, the collaboration can offer benefit corporations a form of free advertising and promotion, with the added bonus of giving the benefit corporations access to "a whole new avenue for potential customers: the Nonprofit's staff, clients, members, donors, etc."<sup>174</sup> A benefit corporation could partner with a charitable organization in its social purposes and thus write off expenses as tax deductible.<sup>175</sup> For a corporation that is taxed twice, an incentive to give to non-profits is that gifts of up to 10% of the corporations' profits are tax-exempt.<sup>176</sup>

In a normal cross-sector social partnership, there is the threat that "the pressure from the Collaboration commercialization pull that distorts the Nonprofit's mission could result in the questionable ethical and legal status of a Nonprofit claiming a mission but not pursuing it."<sup>177</sup> This opens up the possibility of a charitable organization's tax-exemption status being revoked.<sup>178</sup> However, with the requirement that a benefit corporation legislative include a general social purpose in its articles of incorporation, a non-profit may be more confident in choosing a partner that shares common social goals. In addition, a non-profit would be confident that its interests will at least be discussed and

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<sup>172</sup> Marya N. Cotten & Gail A. Lasprogata, *Corporate Citizenship & Creative Collaboration: Best Practices for Cross-Sector Partnerships*, 18 J.L. BUS. & ETHICS 10 (2012). A cross-sector social partnership ("CSSP") includes "partnerships between firms in the profit-seeking sector and those in the civil society sector such as nonprofit and nongovernmental organizations." *Id.* at 10.

<sup>173</sup> *Id.* at 15 (noting that some critique CSR as "nothing more than window dressing.").

<sup>174</sup> Christyne J. Vachon, *Scratch My Back, and I'll Scratch Yours: Scratching the Surface of the Duty of Care in Cross Sector Collaborations—Are For-Profits Obligated to Ensure the Sustainability of Their Partner NonProfits*, 8 HASTINGS BUS. L.J. 1, 5 (2012).

<sup>175</sup> Matthew F. Doeringer, *Fostering Social Enterprise: A Historical and International Analysis*, 20 DUKE J. COMP. & INT'L L. 291, 304 (2010).

<sup>176</sup> *Id.* While state laws allow corporations to give above this level of tax deduction, "the laws are generally interpreted to authorize only reasonable levels of giving." *Id.* However, double taxation may be quite profitable to a non-profit, as it can receive a larger amount of money from the corporation's charitable giving. *Id.*

<sup>177</sup> Vachon, *supra* note 175, at 25–26.

<sup>178</sup> *Id.* at 25.

considered in the benefit-corporation's decision-making processes.<sup>179</sup> The heightened duties placed upon benefit corporations could encourage non-profits to pursue cross-sector partnerships with them with less risk.

*D. Capitalizing on Socially Responsible Investment Trends*

The beneficial nature of the metrics imposed upon a benefit corporation may be coming at the perfect time for the rising generation of donors. In a new study of high wealth capacity "Gen Xers and Millennials" who are inheriting "the \$40 trillion wealth transfer, along with those making their own wealth," the top facets of a philanthropic strategy were to:

[C]onduct due diligence and research before deciding who to support; first decide philanthropic goals or ideal solutions, then search for potential recipients who fit those; fund efforts that address root causes and attempt systemic solutions; and have information about an organization's proven effectiveness or measurable impact before deciding whether to support it.<sup>180</sup>

One interviewee said, "People are thinking differently about philanthropy . . . . They're saying, 'Well, there are . . . these social businesses and there are these double-bottom-line, triple-bottom-line investments.' There are a million different ways to be philanthropic in 2012 that there weren't in 1985."<sup>181</sup>

This is backed up by recent data collected by the US SIF Foundation's Forum for Sustainable and Responsible Investment, which states that sustainable and responsible investing ("SRI") money has continued to be on the rise in the

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<sup>179</sup> The benefit corporation's decision-making process involves evaluating the impact of a decision upon stakeholders that are a part of it. MODEL BENEFIT CORP. LEGISLATION § 301(a) (B Lab, Inc. 2013), available at <http://benefitcorp.net/attorneys/model-legislation>.

<sup>180</sup> Michael Moody & Sharna Goldseker, *Next Gen Donors and Their Plan for Greater Impact*, STAN. SOC. INNOVATION REV. (Feb. 12, 2013), [http://www.ssireview.org/blog/entry/next\\_gen\\_donors\\_and\\_their\\_plan\\_for\\_greater\\_impact](http://www.ssireview.org/blog/entry/next_gen_donors_and_their_plan_for_greater_impact). The study included a national survey and in-depth interviews with thirty 21–40 year olds with the following attributes:

Three out of four participants in the study come from families with a foundation, 36 percent are from families with at least one (and often multiple) donor-advised fund. More than 20 percent also have their own donor-advised fund or foundation. Fifty percent say they are already very or fairly experienced in philanthropy, and nearly all say they expect to get much more involved in philanthropy in the years to come.

*Id.*

<sup>181</sup> *Id.* One survey respondent wrote, "I believe my parents give much more for the 'feel good' feeling that comes along with giving, whereas I am dead-set on maximizing the impact of my philanthropic dollars." *Id.*

United States.<sup>182</sup> “Today, more than one out of every nine dollars under professional management in the United States is invested according to strategies of [SRI].”<sup>183</sup> With the third-party standard requirement for benefit corporations, and the transparency requirement inherent therein, benefit corporation legislation may indeed be the right business strategy at the right time. Its focus on the triple bottom line is evidently striking a chord with the next generation of philanthropists, consumers, and investors. In addition, for those companies acquiring the B Corp label, B Lab’s standard in providing a scoring metric for qualification will meet these rising conscious investors’ desires for measurable impact.<sup>184</sup>

## VI. IMPACT

### *A. How California Can Attract Benefit Corporations*

#### *i. Tax Incentives*

It has been noted that, “[t]o the extent that directors are risk-averse, the lack of corporate law precedent is a true barrier to the proliferation of these new corporate forms.”<sup>185</sup> California could take a note from Philadelphia, Pennsylvania’s economic development strategy in enacting tax credits for local corporations looking to do business in the state as benefit corporations.<sup>186</sup> Even if these tax credits were offered for a limited time and eventually graduated out, it would bring notoriety to the entity, with the hopes of building a foundation for the triple bottom line business movement to be used as a catalyst for changing the traditional idea of corporations as purely profit-seeking ventures.

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<sup>182</sup> *Id.*

<sup>183</sup> US SIF FOUNDATION, REPORT ON SUSTAINABLE AND RESPONSIBLE INVESTING TRENDS IN THE UNITED STATES 11 (2012), available at [http://www.ussif.org/files/Publications/12\\_Trends\\_Exec\\_Summary.pdf](http://www.ussif.org/files/Publications/12_Trends_Exec_Summary.pdf). “Through surveys and research undertaken in 2012, US SIF Foundation identified . . . the overall total of SRI assets is \$3.74 trillion, a 22-percent increase since year-end 2009.” *Id.*

<sup>184</sup> 2012 B CORPORATION ANNUAL REPORT (B Lab, Inc. 2012), available at [http://www.bcorporation.net/sites/all/themes/adaptivetheme/bcorp/pdfs/BcorpAP2012\\_Web-Version.pdf](http://www.bcorporation.net/sites/all/themes/adaptivetheme/bcorp/pdfs/BcorpAP2012_Web-Version.pdf). In addition to starting the B Corp and benefit corporation movements, B Lab has partnered with leaders in investor associations to create Global Impact Investing Rating System (GIIRS), a “comprehensive and transparent system for assessing the social and environmental impact of developed and emerging market companies and funds with a ratings and analytics approach analogous to Morningstar investment rankings and Capital IQ financial analytics.” *What GIIRS Does*, GIIRS (2012), <http://giirs.org/about-giirs/about>.

<sup>185</sup> Plerhoples, *supra* note 137, at 264.

<sup>186</sup> Munch, *supra* note 18, at 188. Philadelphia offers tax credits for “local corporations certified by B Lab.” *Id.* Hawaii’s attempts at offering relief from its state corporate income tax was vetoed by the governor, and there are talks that the towns of Yonkers, New York and Media, Pennsylvania are proposing tax incentives for local businesses incorporating as benefit corporations. *Id.*



There has been an argument made that Federal and state tax exemptions could extend to social enterprises in their socially beneficial pursuits, just as non-profits benefit from tax exemptions in their actions furthering charitable purposes.<sup>187</sup> The argument is that “it is economically unjustifiable and inefficient to grant tax exemptions based solely on the form that an enterprise chooses, and that tax exemption ought to be available for socially beneficial activities regardless of whether the entity generating those benefits is organized as a for-profit or nonprofit.”<sup>188</sup> However, the counter-argument stems from the inherent temptation within for-profit companies to reduce quality when dividends and compensation depend upon profit,<sup>189</sup> and the possibility that the tax exemption could be abused by for-profits who would masquerade their market ploys as social purposes and green-wash consumers in order to make a profit that is bolstered by fake tax-exempt practices.

While the benefit corporation legislation does have the advantage of accountability and transparency, which would help combat this temptation of companies to take advantage of the system, a tax-exemption status for social purposes would put a large burden on the government in oversight requirements. There is also the “Theory of Imperfect Consumers,” that hypothesizes that the only reason donors might choose to contribute to a for-profit charity is because of confusion, ignorance, or fraud.<sup>190</sup> If the government were to offer tax-exemption based on actions rather than entity, the ability of a benefit corporation to lobby or be involved in politics may be altered. As of now, a benefit corporation has the right, like any corporation, to become politically involved.<sup>191</sup> However, just as non-profits are kept from substantial political campaigning,<sup>192</sup> if a benefit corporation were to gain tax-exemption for some of its social involvement, it may be restricted in such practices. Therefore, California would be best to offer tax breaks, instead of tax exemption, and such tangible encouragement for social innovators could help boost the local economy.

#### *ii. California-Endorsed Benefit Corporation Label*

As conscious consumerism grows and other consumers begin to

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<sup>187</sup> Kelley, *supra* note 112, at 363.

<sup>188</sup> *Id.*

<sup>189</sup> Benjamin Moses Leff, *The Case Against For-Profit Charity*, 42 SETON HALL L. REV. 819, 877 (2012) (“[i]n trying to meet performance measures in other areas, managers may be tempted to cut back on costs related to quality, thus leading to poor product quality (and thus inefficiency)”).

<sup>190</sup> *Id.* at 862.

<sup>191</sup> PALMITER & PARTNOY, *supra* note 106, at 135–38.

<sup>192</sup> See I.R.C. § 501(c)(3) (West 2010) (stipulating that “no substantial part of the activities . . . [of a nonprofit should be] carrying on propaganda, or otherwise attempting, to influence legislation . . .”).

understand the mission behind social businesses, benefit corporations will be looking for ways to gain continued publicity and market expansion. Benefit corporations offer California and other states the assurance that its constituents will be able to access information to help them make informed buying decisions of goods and services.<sup>193</sup> In a state where legislation has been passed to force such transparency upon a subset of corporations,<sup>194</sup> the benefit corporation's annual benefit report and accountability standards are likely to strongly resonate with the public. If California began now to help its citizens understand the movement, and the beneficial nature for consumers looking to rebuild their trust in the corporate world, it could experience a large influx of benefit corporation businesses. This would not only help in raising state revenue from increased filing fees, but it may help support the state in its community development and environmental protection goals, as benefit corporations take local stakeholders into consideration throughout the decision-making process.<sup>195</sup>

To attract benefit corporations, California could offer its own state-endorsed label for benefit corporations to place on their advertisements and product packaging. While the B Corp label is available from B Lab, some benefit corporations may be unwilling to pay the price tag associated with its third party review process. One attraction of the B Corp label is that it creates a community of common thinkers and business service discounts.<sup>196</sup> However, for those benefit corporations who are not interested in B Lab affiliation, California could offer a similar label and similar advantages. Most importantly, however, the California-endorsed label would help increase consumer awareness of what such a business stands for, and could help the movement gain more popularity.

### *B. California Lawyers Advising Benefit Corporations*

If California decides to embrace its identity as the incubator state of social innovators, the full support of California's Bar should be behind it to offer legal counsel and caution to the eternally optimistic entrepreneur. However, in serving this unique entity set, should Californian attorneys be aware of any higher ethical standards?

Attorneys have the ethical duty as counselors-at-law to recognize the desires and expectations of the legal client and to spot issues for the future.<sup>197</sup>

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<sup>193</sup> See *supra* text accompanying notes 163–68.

<sup>194</sup> See S.B. 657, *supra* note 14.

<sup>195</sup> See *supra* text accompanying note 49; see also Kelley, *supra* note 112.

<sup>196</sup> See *supra* text accompanying note 43.

<sup>197</sup> LAW. MANUAL PROF. CONDUCT (ABA) Rule 1.1: Competence. “A lawyer shall provide competent representation to a client. Competent representation requires the legal knowledge, skill,

The California State Bar's professional and ethical rules state that an attorney, when she knows that an agent of the organization acts or intends or refuses to act in a manner in violation of a law, or in a manner which is likely to result in substantial injury to the organization, may take actions, subject to the duty of confidentiality, in the "best lawful interest of the organization."<sup>198</sup>

A question presents itself as to what is considered a "substantial injury to the organization" when dealing with benefit corporations. Would a failure to pursue the general social purpose be considered "substantial injury"? If so, California corporate lawyers could be considered an extra layer of accountability, added onto the annual public benefit report's third-party standard, when it comes to the board's decision making processes and actions. Since the corporation is the client, the attorney must continually monitor the board in its decision-making and ensure that the articles of incorporation are being upheld, including the support of the general social benefit purpose.

## VII. CONCLUSION

While many debate the need for the benefit corporation legal status, the fact is that it has already become a part of the corporate code in forty percent of the nation's states. As conscious consumerism grows and with it, the desire to make informed buying and investment decisions through increased transparency between consumer and company, the benefit corporation will gain popularity. However, with its increased attraction, the benefit corporation community will have to be vigilant in protecting its standards of accountability to ensure that profiteers do not taint the movement's branding power. It is speculated that larger, private corporations who desire to tap into these growing niche markets of consumers may buy out benefit corporations. The benefit corporation legislation ensures that there are thorough decision-making processes for boards to take advantage of to protect themselves if their business judgment is brought into question during transitional phases. In addition, the benefit corporation provides a platform off of which to launch successful cross-sector partnerships with charitable organizations. The movement is entering society at the perfect time to leverage demand.

Corporate citizenship is on the rise in the business world with the expectation that the corporation will "live up to its ethical duties of contributing to society in a positive, measurable way."<sup>199</sup> This is a difficult standard for

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thoroughness, and preparation reasonably necessary for the representation." *Id.*

<sup>198</sup> THOMAS D. MORGAN & RONALD D. ROTUNDA, 2013 SELECTED STANDARDS OF PROFESSIONAL RESPONSIBILITY 325 (2013) (citing CA PROF. CONDUCT RULES 3-600: Organization As A Client).

<sup>199</sup> Cotten & Lasprogata, *supra* note 173, at 15.

normal corporations to uphold with “the realities of financial markets and the current state of the legal and regulatory environment, which motivates no more than the moral minimum in corporate actors.”<sup>200</sup> Thus, the legal freedoms that benefit corporation legislation offers to businesses wanting to pursue the triple bottom line, while also ensuring accountability in decision-making processes, is a huge asset. Choosing to incorporate as a benefit corporation can be an excellent decision, not only for the business, but also for consumers and society as a whole.

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<sup>200</sup> *Id.* at 16.