Rethinking social hybrid business forms – A comparative analysis of recent reforms to Corporate Law meant to nurture social enterprising.

Cesar Antonio Flores Ramirez

Master Thesis
Title: Rethinking social hybrid business forms – A comparative analysis of recent reforms to Corporate Law meant to nurture social enterprising.
Cesar Antonio Flores Ramirez (U1233505 // 797131)
LLM. Master International Business Law
Under the supervision of Mrs. I. Skultétyová LLM
Tilburg University: June 12th, 2015

Word Count: 25404

Contents

Abstract 4
CHAPTER I 4
1.1 Introduction 4
1.2 Research Objectives 6
1.3 Research Questions 7
1.4 Structure and Methods 7
CHAPTER II 8
2.1 Brief Overview of the Development of the Social Enterprise 8
2.2 Definition of Social Enterprise 9
2.3 Market Demand for Social Enterprises 11
2.3.1 Customers 11
2.3.2 Social Entrepreneurship 12
2.3.3 Socially Responsible Investing 13
CHAPTER III 15
3.1 The Rationale behind the Need for Social Corporate Entities in the US 16
3.2 Non-profit Organizations as Social Enterprises 16
3.3 For-Profit entities as Social Enterprises 17
3.3.1 Shareholder Primacy and Managerial Discretion. 18
3.3.2 The Constituency Statutes 22
3.4 Enlightened Shareholder Value, the UK's approach to Company's Purpose 23
CHAPTER IV 24
4.1 The United Kingdom's Community Interest Company 24
4.1.1 Characteristics and Restrictions of Community Interest Companies 25
4.2 The United States' Low Profit Limited Liability Company (L3C) 29
4.3 The United States' Benefit Corporation 31
4.3.1 Characteristics and Requirements of Benefit Corporations 32
4.3.2 Public Benefit Corporation, the Delaware's approach 35
CHAPTER V 38
5.1 The Social Hybrid Business Forms Landscape 38
5.1.1 United States' Social Hybrid Business Forms Landscape 39
5.1.2 United Kingdom Social Hybrid Business Forms Landscape 40
5.2 Benefits of using Social Hybrid Business Forms 41
5.3 Criticism to Social Hybrid Business Forms 42
5.4 How to Improve Social Hybrid Business Forms? 45
CHAPTER VI 47
6.1 Conclusion, Not Necessary but Complementary 47
Bibliography 48

Abstract

The purpose of this paper is to research the value of the newly added hybrid business forms meant to cover the needs of social entrepreneurs and mission-driven businesses. In particular, the rationale behind them, namely the necessities of the social enterprise that traditional corporate law fails to address, hinder or oppose. Not until recently a wide assortment of new business entities was introduced, such as the Community Interest Company (CIC) in the UK, the low profit Limited Liability Company (L3C), and, recently in the spotlight, the Benefit Corporation in the US. These new business forms were created with the sole purpose of providing a special vehicle to enable for-profit mission-driven firms to conduct business with legal certainty while pursuing the triple bottom line: people, planet and profit, achieved by imposing a duty to consider stakeholders' interests and enhancing the transparency and accountability mechanisms of the firm. Nevertheless, their implementation raises numerous questions, since usage of the new entities is often condemned for being unnecessary, untested and ambiguous. This paper analyses the elements that differentiate the new entities from existing business forms within the traditional legal framework, expecting to justify their introduction and identify the advantages, weaknesses and efficiencies that they have to offer. Ultimately, if the existence of a special vehicle is deemed necessary to or supportive of the development of the Social Enterprise, this paper will propose changes to the current approach that might strengthen the current formula.

Keywords: Benefit Corporation, Social Enterprise, Hybrid Business Forms

CHAPTER I

1.1 Introduction

In the last decade there has been a growing tendency to consider, embrace and employ socially and environmentally responsible business models. The aftermath of the financial crisis exposed the shortcomings of the traditional business approach, causing both an increasing interest worldwide in social enterprising (Taylor, 2009) and an opportunity to reconsider corporate governance (Kelly, 2009). Furthermore, it is said that the line between doing good and conducting good business begins to disappear gradually as more socially motivated entrepreneurs, who want to make use of the full potential of business to address the most important social and environmental issues of modern society, join the lines of the Social Enterprise Movement[1]. This new breed of social entrepreneurs driven mainly by the goal to do good do not aspire to become mere executives of charitable non-profit organizations, instead they aim to distinguish themselves from the "status quo" by conducting business that pursues a "double bottom line" (financial and social) or "triple bottom line"[2] (Profit. People and Planet) producing benefits beyond wealth maximization.

In the United Kingdom, born out of a growing sense of frustration with corporate law and how complicated it was to embed social purposes in a legal form, Stephen Lloyd proposed the creation of an "off-the-shelf" entity for social enterprising (Lloyd, 2010). A special Social Enterprise Unit was created in 2001 by the British government with the sole purpose of identifying the barriers to the growth of the social enterprise sector and to propose strategies to

[1] In February 20, 2006, David Gergen published *The New Engines of Reform,* in his article he claims that "social entrepreneurs do more than treat society's ills –they envision widespread, systematic change that could prevent those ills from ever occurring".

[2] The phrase "the triple bottom line" was first coined in 1994 by John Elkington, the founder of a British consultancy called SustainAbility. (The Economist, 2009).

overcome its problems. Four years later in 2005, the *Community Interest Company* (CIC) was introduced in the United Kingdom, effectively enabling companies limited by guarantee and companies limited by shares to re-incorporate or incorporate as CIC. In essence, the CIC is a limited company subject to restrictions designed to ensure they will serve the community interests. At the beginning of 2015 there were more than 15000 registered CICs, and only last month 237 entities [re-]registered using this form (Office of the Regulator of Community Interest Companies, 2015). Yet, the number might be slightly trivial in contrast to the more than 3 million companies registered in the UK (GOV.UK, 2015). The characteristics, requirements and details of this form will be analysed in detail further in this paper.

At the other side of the Atlantic, around the first half of the past decade in the United States, many social entrepreneurs also began expressing their frustrations with the existing corporate law. Many of these social entrepreneurs argued that under the outdated corporate law, a combination of inappropriate old-style legal entities and outmoded law prevented them from pursuing their social plans. They demanded that the law catch up with them (Kelley, 2009). In their understanding, the stringent for-profit/non-profit dichotomy made the choice of entity the most difficult task, leaving them with a feeling that a significant change was desirable. On one hand, non-profit entities have limited possibilities for financing because they are prohibited from distributing profits, forcing them to operate by a great extend through donations. On the other hand, the for-profit entities gave the impression of being tied to the idea of "*shareholder wealth maximization*", often at expense of social and environmental ends. Although, some academics argue that corporate law is agnostic towards corporate purpose, giving for-profit entities room to pursue a vast array of lawful goals, including social, environmental and charitable ends. Others, advocates of the constituency statutes[3], argue that the desired flexibility is possible in any of the 41 states where such legislation is available.

As a matter of law, academics are partially right with the above mentioned solutions that seem, at first sight, fairly satisfactory. However, in practice, *shareholder's wealth-maximization* arguably remains at the nucleus of all corporate decisions, and constituency statutes' permissive approach does not result in a material change to usual business. In order to answer the dilemma of which entity is appropriate for social entrepreneurs, political forces, NGOs, policymakers and lawmakers began discussing possibilities for a new type of entity, fit to address the concerns of the social enterprise sector. As a result, in the United States a vast array of hybrid[4] social enterprise entities were introduced, not only allowing but creating a duty to generate public benefits in addition to financial returns. These new forms are the main focus of this paper, in particular the *Benefit Corporation*. The reason for this being that the entity is claimed to be the most effective vehicle to conduct business while ensuring that the core of the firm remains imbued with the value goals considered and attained. Its unique approach expands the flexibility, accountability and transparency mechanisms of the company, while at the same time changing the equation of the interests that directors must take into account in their decision-making process.

On October 1, 2010 subtitle 6c of Title 5 of Maryland's Corporations and Associations code took effect, making Maryland the first jurisdiction to add the new form within the United States. The new form which resembles the typical *stock corporation* (C corp), possess a set of major characteristics that distinguish it: (1) it is obligated by law to create a material positive impact on society and the environment, (2) it possesses an expanded set of duties for directors,

[3] Constituency statutes also known as anti-takeover legislation, essentially permits directors to consider other non-shareholder interest in weighing takeover offers and other decisions. (Easterbrook & Fischel, 1996)

[4] The hybridity of these entities resides in the combination of non-profit and for-profit elements. In the social enterprise context "Hybrid" refers to the combination of a novel mandatory consideration of all stakeholders, armed with the more traditional enforcement rights of directors and shareholders, aiming to pursue, promote and protect the social and/or environmental goals of the firm.

that requires them to consider non-financial stakeholders and stockholders alike, and (3) it has an obligation to report its overall social and environmental performance using a credible, comprehensive, independent and transparent third-party standard. The law was modelled on the *Model Benefit Corporation Legislation* proposed by B Lab[5].

Since then, 26 more states [6] have passed legislation adding *Benefit Corporations* to their current menu, including Delaware[7]. While the goals of these reforms are the same, two different trends to implement legislation arose since the Delaware's *Public Benefit Corporation* (PBC) was introduced. The differences of both approaches shall be explained in detail later in this paper. Nonetheless, to date there are only 2541 known benefit corporations all across the United States and only 302 in Delaware. Such a number is insignificant if it is taken into account that more than 6 million companies[8] are registered in the United States. Additionally, it must be noted that the form is not the most recent legal innovation in social hybrid business forms in the United States, nor the oldest. Other entities such as the *low profit limited liability company* (L3C), the *flexible purpose corporation* (FPC) and the *social purpose corporation* (SPC) have been introduced prior and post the benefit corporation reforms. For the purpose of this paper the FPC and SPC will be excluded, because unlike the L3C and the benefit corporation, they are not implemented in more than one jurisdiction. Nevertheless, the low usage of all these forms not only fails to reflect the growth of the social enterprise but also raises questions about the viability and efficiency of such entities.

1.2 Research Objectives

This paper builds upon existing literature about hybrid business forms for social enterprises, particularly reevaluating the validity of the so-called *Unnecessary Argument*[9] (Clemente, 2013). The weaker version of the *Unnecessary Argument* stresses that special vehicles for social enterprises are redundant because social enterprises can exist without them. This claim is deeply linked to a more fundamental debate whether a legal duty to maximize profits exist (Norked, 2012). The stronger version of the argument asserts that the existing paradigm addresses all the necessities of social entrepreneurs. Ultimately, the purpose it is not to simply question all the developments made to fulfill the needs of the social enterprise sector. Rather it is a quest to distinguish the elements that properly addresses these needs from those that fall short and need to be adjusted to cast away the ambiguity around these forms. In order to distinguish these elements, and obtain the answer the research questions of this paper, the next steps will be taken as follows:

i. It is essential to develop a brief overview of the rationale behind the emergence of hybrid business forms for social enterprises.
ii. It is crucial to determine the needs, limitations, constraints and problems of Social Entrepreneurs that lead to their creation.

---

[5] B-Lab is a non-profit that certifies socially responsible companies.

[6] Benefit corporation legislation is effective in Arkansas, California, Colorado, Delaware, Florida, Hawaii, Illinois, Louisiana, Maryland, Massachusetts, Nevada, New Jersey, New York, Oregon, Pennsylvania, Rhode Island, South Carolina, Utah, Vermont, Virginia, West Virginia and DC. (Find a Benefit Corp, 2015)

[7] Around 50% of all publicly-traded companies in the US and 64% of the Fortune 500 are incorporated in Delaware (Lipin, 2000).

[8] This number reflects only firms with pay roll and is based on data from the United States Census Bureau: Statistics of U.S. Businesses.

[9] Although the *Unnecessary Argument* explicitly refers to the clash of the Benefit Corporations vs Existing Law, yet, the critique is suitable for most hybrid business form of social enterprising.

iii. The existing business forms available for mission-driven business and their suitability must be explored with regards to the special needs of the social enterprise movement.
iv. A comparison shall be made between all existing hybrid business forms for social enterprises in the US. Additionally, a comparative analysis with the stringent UK approach will be drawn, in order to contrast the two significantly different approaches.
v. To conclude, if the existence of these forms is deemed essential, a list of improvements shall be presented that could improve the current approach.

1.3 Research Questions

This paper engages the problems concerning the implementation of new hybrid business forms from the perspective of the social enterprise movement. The reason to include the CIC is linked to the nature of the movement, being a global movement. This paper attempts to address the following question and sub-questions:

i.To what extent is it necessary to add social enterprise to the menu of available business forms in order to facilitate pursuance of the social goals?

a. What is the rationale behind the emergence of special vehicles for social enterprising?
b. What are the characteristics, goals and needs of the modern social enterprise movement?
c. In which ways does traditional corporate law hinder pursuing of social and environmental goals for for-profit entities?
d. What are the elements that distinguish traditional business forms from their new social counterpart?
e. Without the existence of these new forms, what other options do social entrepreneurs have to structure their businesses?
f. To what extent can changes in the current approach, specifically an addition of elements of other forms to the *Benefit Corporation,* reform and address the ambiguity related to its usage?
g. Alternatively, if such forms are not fundamental to the creation, development and promotion of social enterprising, what changes can be made to ameliorate the burdens and constrains that traditional corporate law places on them?

1.4 Structure and Methods

The structure of this paper engages the topic of hybrid business forms for social enterprising step by step. The first chapter provides an introduction to the topic and an overview of the methods, structure, research motives and questions of this paper. Chapter two offers a brief overview of the development of social enterprises in Europe and the United States and a definition of social enterprising, and reviews the increasing interest in the social enterprise movement worldwide. Chapter three provides an overview of the rationale behind the addition of special vehicles for social enterprising in the U.S., and the different approaches to corporate purpose in both jurisdictions. Chapter four offers an overview of the different social business forms available across the US and UK's Community Interest Company. Chapter five briefly analyses and compares the viable business forms for Social Enterprises, their advantages and disadvantages among them and in relation to the traditional corporate law approach. And finally, chapter six will draw a general conclusion and provide the answer to research questions

CHAPTER II

2.1 Brief Overview of the Development of the Social Enterprise

There is disagreement about the value and novelty of the modern approach of the Social Enterprise movement. This section will provide an overview of the origin and development of the social enterprise in Europe and the United States. Although the modern social enterprise movement is a global movement, as a concept it has developed in two different directions if we compare both jurisdictions, despite the fact that its emergence is caused by the needs of society that governments, private actors and non-profits were not able to address properly using traditional means. Thus, a comparative overview of the social enterprise sector is connected to the issue of the lack of a single universal concept of social enterprise. In essence, in the United States, social enterprises were seen simply as organizations that provide services and goods to the disadvantaged part of the population. In contrast, in Europe, social enterprises arose in response to the problem of structural unemployment.

The relevancy of Social enterprise became evident in the United States and Europe during the period of 1970-1980. In the United States, in response to national economic downturn, charities faced decrease of funds[10] and a significantly increased demand for their services due to unemployment. At the time, the pure non-profit organizations sought new sources of revenue, finding social enterprise commercial activities a solution to fill the financial gap. Similarly, in Western Europe, they emerged as consequence of fall in economic growth, retrenchment of the welfare state and increased unemployment at the end of the 1970s. At the time, many countries experienced a rise in unemployment up to 10%, creating market demands that governments and charities were unable to solve. As a result, in the early 1980s a wide array of social enterprises emerged to address those particular areas where the welfare state had retreat or had not been able to attend (Kerlin, 2006). Although these efforts were made by several charities and non-profit entities, they could be considered the first forms of social enterprising, motivated to a certain extent by purely altruistic goals rather than commercial. Nonetheless, its appearance established the foundations for the development of the modern social enterprise.

About eleven years after the appearance of the first form of modern social enterprise efforts, in continental Europe a new type of entity developed out of traditional concepts of social cooperation, the *Social Cooperatives*. The enactment of the *Social Solidarity Cooperatives*[11] in Italy in 1991 is considered by many to be the birth of the social enterprise movement in Europe (Defoumy & Nyssens, 2008). Almost every European jurisdiction possesses its own version of the Social Cooperative. Nonetheless, *Social Cooperatives* perform similarly to non-profit charitable entities generally without any form of profit distribution to their shareholders. For the purpose of this paper their importance as a starting point is recognized, however, most of these cooperatives lack the dual-mission element and focus on social, not environmental problems. They mainly serve as a work integration social enterprise (*WISE*), helping low-qualified unemployed people, who are at risk of permanent exclusion from the labour market (Defoumy & Nyssens, 2008). In 1998 the European Commission's Digestus Project began encouraging changes to member states to promote social enterprising along the same lines as the Italian cooperatives. Yet until the emergence of one of the newest organizational approaches in Europe, namely the Community Interest Company in the United

[10] The 1980s brought welfare large cutbacks in federal funding resulting in the loss of about $38 billion for charitable organizations in the US (Salamon, 1993).

[11] The Italian law introduced two types of social cooperatives: Type-A Social Cooperatives and Type-B Social Cooperatives, the former focuses in social, health and education and the later deals with unemployment and work integration for the disadvantaged. (Defoumy & Nyssens, 2008)

Kingdom in 2005, the focus was on non-profit entities without the dual-mission component characteristic of the modern social enterprise movement. Its origin and characteristics will be explained in the following chapters.

In contrast to the European approach that developed entities for social enterprising in a timely manner with great government involvement, rather than governmental, the United States experienced mainly private foundation support in the institutional context for social enterprising at the end of the 1980s. Most of these private actors performed tasks such as: information collection and creation of networks of social enterprises, support of social enterprise start-ups, social enterprise business competitions and individual social entrepreneur grants to improve their education and capabilities (Kerlin, 2006). The United States government provided indirect support; however, most initiatives were not directly aimed to promote the advance of the social enterprise. Among the few examples of direct support programs by the government is the Social Enterprise Initiative[12] of 1998-2001 by the City of Seattle, Washington (Praszkier & Nowak, 2011). Yet, at the entity level, no significant change was implemented until the appearance of the *L3C* in Vermont in 2008, which was followed by other hybrid entities, as will be explained in detail in the next chapter.

The difference in the approach of both jurisdictions to social enterprising is not significantly different from how to they approach other areas, such as their respective business law, corporate governance reforms and competition law. In the comparative analysis of corporate governance law reforms by Joseph A. McCahery and Erik P.M. Vermeulen (2006) they distinguished two systems with significant differences: (1) the market-oriented corporate model and (2) the relationship-based (or network-oriented corporate system). It is clear that their analysis refers to an absolutely different topic, namely the degree of influence that stakeholders and shareholders have in the process of corporate governance. Nonetheless, it reveals to a certain extent the striking differences in nature of both jurisdictions and their dissimilar conceptual conceptions of business related norms, but most importantly it supports that "the judiciary in Anglo-American systems seems to play a much more proactive role in shaping the actual contents of the corporate governance framework than in Continental European jurisdictions" (McCahery & Vermeulen, 2006) where the legislative dictates the direction. Hence the need for an overview of the landmark precedents that explain the rationale behind the need for special vehicles in the United States, as shall be explained in section 3.1.

2.2 Definition of Social Enterprise

The term social enterprise lacks a solid academic definition. This problem relates to the differences in conditions, development and approach of every jurisdiction's perception of what social enterprising is. The concept developed in parallel with the entities, for example in the United States the definition puts emphasis on revenue generation by non-profit organizations (Kerlin, 2006). Although, some academics include for-profit entities that engage in dual-mission business strategies and firms that conduct social efforts by means of corporate charity or corporate social responsibility (CSR). Yet there is a conceptual disagreement between practitioners and academia about which firms are within the concept of social enterprise and which are not. In contrast, in Europe, despite a similar division, their concept highlights the advanced manner in which firms address social needs that improve over time as the organization develops. Also, their conceptual approach greatly takes into consideration social

[12] The program offer jointly with various foundations a series of events aimed to provide entrepreneurial training for non-profits.

cooperatives as part of the third sector (Defourny & Nyssens, 2012). According to the EMES[13] (The Emergence of Social Enterprise in Europe) project, the "ideal type" of social enterprise possesses the following characteristics:

i. Continual commercial activities, namely producing and selling goods and/or services.
ii. Autonomy.
iii. Substantial financial risk.
iv. Their ultimate end is to benefit the community.
v. Initiative launched by citizens.
vi. Paid work is minimal within the organization.
vii. Democratic decision making, rather than based on capital or ownership.
viii. Participatory nature.
ix. Limit profit distribution (Defourny, 2001).

Because of the impossibility to obtain a single definition of social enterprise, anyone who attempts to engage in the subject is forced to use a variety of sources in order to develop an in-depth insight. The Organization for Economic Cooperation and Development (OECD) defines it as "any private activity conducted in the public interest, organized with entrepreneurial strategy, but whose main purpose is not the maximization of profit but the attainment of certain economic and social goals, and which has the capacity for bringing innovative solutions to the problems of social exclusion and unemployment" (OECD, 1998). Moreover, the European Commission defines a social enterprise as "an operator in the social economy whose main objective is to have a social impact rather than make a profit for their owners or shareholders" (Commission, 2015). Although these definitions capture the social end, they fail to cover the environmental component and the characteristic of consideration for the general well-being of the corporate purpose of the new legislation. Yet the definition can be blended in different ways: from a narrow point of view, Social Enterprise is "an entity offering products or services that directly impact the disadvantaged" (Haskell Murray, 2012). In contrast, from a broad point of view Social Enterprise is "an entity that uses business methods while also maintaining a significant social purpose" (Lane, 2012).

Linda O. Smiddy (2010) suggests that one of the most concise definitions is "the use of market-based strategies to promote the public good". Another succinct definition, commonly used, defines the Social Enterprise as "an organization or venture that achieves its primary social or environmental mission using business methods, typically operating a revenue-generating business" (Katz & Page, 2010). Nonetheless, social enterprises can take many forms, from the non-charity entities using business strategies to complement their funding, to the so-called commercial non-profits that usually just allocate subsidies to external beneficiaries as opposed to doing business for or with them. Non-profits mainly collect and distribute capital rather than produce goods and services. Another form consists of seasoned companies that engage in corporate charity and CSR. Corporate charities and CSR mainly reflect policies intended to boost a firm's goodwill or reputation, or as a response to pressures to address unfair distributional outcomes (Heal, 2004). Similarly to the manner that non-profits function, corporate charities simply distribute a significant but small amount of capital to disadvantaged beneficiaries directly or through a foundation. Furthermore, to a certain extent, CSR policies largely function similarly, except that they encompass a broader range of methods

[13] The EMES approach begun in 1996, it derives from extensive dialogue among several disciplines (economics, sociology, political science and management) and different national traditions present in the European Union (Defourny & Nyssens, 2012).

for passing on subsidies. A prime example is Google who commits 1% of their profits and equity to create solutions for global problems with the creation of the Google Foundation[14].

Dana B. Reiser (2009) notes that" Social enterprises integrate philanthropy into their business models at a more basic level than companies that make corporate contributions or practice CSR [Corporate Social Responsibility]".Although there is no doubt that these forms of social enterprise carry relevancy and impact society, they are a bit far from being properly called "modern social enterprises", a hybrid form for conducting business also referred to as dual-mission firms. Those firms "seek to generate both extra-ordinary returns for society and acceptable returns for its owners and investors" (Kelley, 2009). Ultimately, the firms and entrepreneurs under this category are aware that in order to succeed in gaining public support and gain access to different kinds of capital such as charitable, governmental and private, they must create a recognizable brand to signal consumers, public, investors and employees about the difference between them and companies with good marketing claiming to be part of this category - and those are the main subject of the recent legislation. It is most important to distinguish the subjects of the new legislation to determine their needs as a unique class. Their prominent potential improves as the market demand for social, responsible and environmental products, services and investments increases overtime

2.3 Market Demand for Social Enterprises

The market is considered the primary mechanism for allocating goods, services, maximizing wealth and well-being, and more importantly solving the existing social problems in capitalist societies. Social enterprises, as explained before, first arose to deal with the social problems that could not be ameliorated or resolved by the government, for-profit or non-profit entities as conceived in the traditional approach. The transition from mere "non-profit organizations that serve as apt instruments for privately-led efforts to improve society" (Clemente, 2013) into hybrid mission-driven businesses reflects a significant change in all socio-economic actors, their needs, their demands, their concerns and their preferences. The next section will briefly explain the development of the increasing market demand for something beyond wealth.

2.3.1 Customers

Economists and marketing strategists emphasize that "creating superior customer value is a key element for companies to succeed" (Porter, 1980), building customer value is fundamental to for-profit and non-profit organizations alike. The perception of "value" varies, especially in market strategy and consumer behaviour. What marketing strategists contemplate as "customer value" differs greatly from what sociologists and psychologists might consider "consumer value". In essence, the difference is that "customer value" refers to the valuation at the time of purchasing a good or service from the buyer's point of view and "consumer value" encompasses the different factors that affect the buyer's valuation of the product such as: (i) functional benefits, (ii) social benefits, (iii) affective benefits, (iv) epistemic benefits, (v) aesthetic benefits, (vi) hedonic benefits, (vii) situational benefits and (viii) holistic benefits (Wenben Lai, 1995). Recently, the equation of benefits that consumers consider while making purchasing decisions started taking into consideration their beliefs, and in some cases their sense of social and environmental responsibility.

---

[14] Larry and Sergey in their 2004 Founders letter said "We hope someday this institution may eclipse Google itself in terms of overall world impact by ambitiously applying innovation and significant resources to the world's problems" (Google, 2004)

There is increased consciousness by consumers to align their values with their purchases: given similar price and quality, 91% of global consumers are "very" or "somewhat likely" to switch brands to one that is associated with a good cause (CONE, 2013). Furthermore, data from the Natural Market Institute (NMI) in their U.S. Consumer Perspectives and Trends in Sustainability report 2013 distinguishes the consumer values taken into account while making purchases. In their findings they recognize what values attract people to sustainability: 21% of the consumers have deep personal and planetary health values, 20% place higher importance on personal health than environmental issues, 24% are driven by social pressure, 18% are driven by cost savings (any social or economic benefit is secondary) and 17% are unconcerned about the environment and society. The main trend is that consumers tend to award those companies that positively address social or environmental problems and punish negative corporate behaviour with their purchasing power.

While consumer demand for socially responsible products increases, the trust in corporations decreases because marketers use the terms "biological", "green", "responsible", "sustainable", and others so often that their meaning is lost. This problem is called Greenwashing. Greenwashing in essence refers to the use of the above mentioned terms as part of a marketing strategy to misguide the consumers into believing that products follow certain standards that qualify them. This phenomenon caused the emergence of various organizations that provide certifications, such as "Bio", "Fair Trade", "Green Seal", "Organic", and others, with the sole purpose of providing the consumers with particular details of the company's social or environmental performance (Clark, Jr & Babson, 2012). Nonetheless, there are few standards that provide an all-inclusive analysis of the company's performance and there is not a single universal transparent standard that could signal consumers which companies are genuine in this regard, and which merely possess good marketing.

2.3.2 Social Entrepreneurship

Typically a business entrepreneur is driven by the ambition to create entirely new industries, develop technologies that disrupt a particular industrial sector, improve current business models, and other new approaches to the manner of conducting business. In contrast, a social entrepreneur's main concern is not with business as an end but as a tool for developing ground-breaking solutions for social and/or environmental problems, aiming to implement these solutions on a global scale (Ashoka, 2015). In recent years the popularity of social entrepreneurship has been caused by several elements, despite the fact that there is something inherently appealing about social entrepreneurship. However, it must be clear that entrepreneurs are rarely driven by the prospect of financial gain, rather, both the entrepreneur and the social entrepreneur go after an opportunity that they previously identified, relentlessly pursuing it, all for the sake of realizing their ideas (Martin & Osberg, 2007). Yet, the critical distinction among them lies in the proposed value. On one hand, the entrepreneur's value proposition is structured to anticipate and serve the markets of the new product or service, and to a certain extend designed to obtain financial profit. On the other hand, the social entrepreneur structures his value proposition in the form of a "large-scale, transformational benefit that accrues either to a significant segment of society or to society at large" (Martin & Osberg, 2007).

Martin & Osberg (2007) distinguish the three fundamental components that identify social entrepreneurship: "(i) identifying a stable but inherently unjust equilibrium that causes the exclusion, marginalization, or suffering of a segment of humanity that lacks the financial means or political clout to achieve any transformative benefit on its own; (2) identifying an opportunity in this unjust equilibrium, developing a social value proposition, and bringing to bear inspiration, creativity, direct action, courage, and fortitude, thereby challenging the stable

state's hegemony; and (3) forging a new, stable equilibrium that releases trapped potential or alleviates the suffering of the targeted group, and through imitation and the creation of a stable ecosystem around the new equilibrium ensuring a better future for the targeted group and even society at large". Probably the most notable example is Nobel Peace Prize winner Muhammad Yunus, father of microcredit and founder of Grameen Bank. Yanus observed that Bangladeshis had limited options to access credit, unable to qualify for loans they had to resort to private lenders with high interest rates. Yunus began lending small amounts of money to 42 women from the village of Jobra. All women repaid the debt, proving that even with a trivial amount, the woman would invest in their own capacity to generate income. Yunus' effort resulted in the emergence of a global network of other organizations, making microcredit a worldwide industry (Yunus Centre, 2015).

Last year the Schwab Foundation for Social Entrepreneurship identified 37 promising entrepreneurs for their remarkable social and/or environmental work. Since its foundation in 1998, the Schwab Foundation has had the purpose of advancing social entrepreneurship and helping social entrepreneurs to achieve societal innovation and progress. The Schwab Foundation is a non-profit, independent and neutral organization under the legal supervision of the Swiss Federal Government. Its headquarters are in Cologny-Geneva, Switzerland (Schwab Foundation, 2015). In essence, the Schwab Foundation, rather than providing grants or investing financially in the organization, invests its limited resources to legitimize promising social entrepreneurs' work, enhancing their network allowing them access to financial and in-kind resources that enable them to grow and develop. Similarly, other non-profits such as the Ashoka Foundation play an important role in enhancing social entrepreneurship. The increase in this kind of entrepreneur in part is due to the large number of universities offering social entrepreneurship courses, Harvard and Stanford notably pioneered in this regard.

2.3.3 Socially Responsible Investing

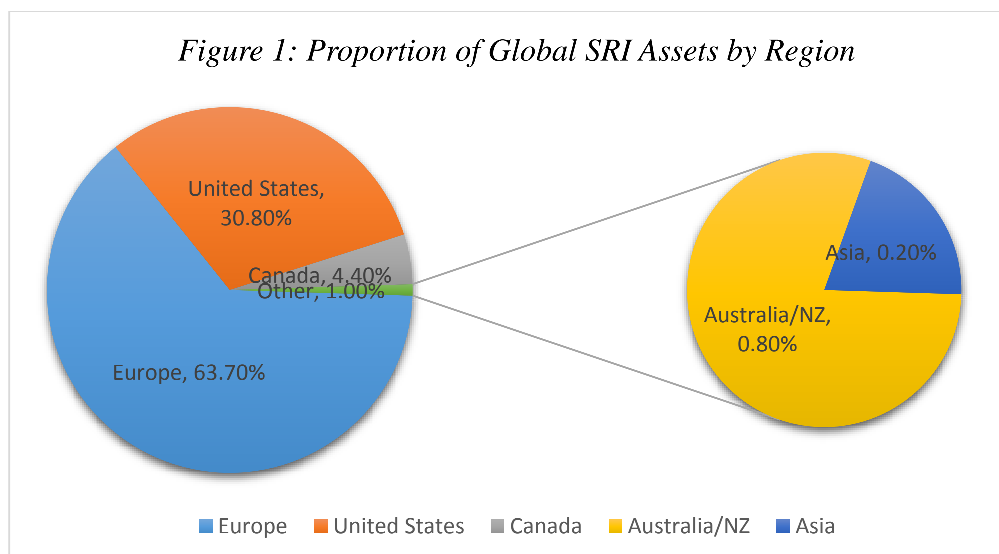
In recent years, institutional investors, such as pension funds and mutual funds, have become increasingly engaged in socially responsible investing (SRI). Evidence of that can be found in recent empirical data from the Global Sustainable Investment Review 2014 by GSIA[15], which indicates that there has been a significant growth in the global sustainable investment market both in absolute and relative terms, rising from $13.3 trillion at the outset of 2012 to $21.4 trillion at the start of 2014, and from 21.5% to 30.2% of the professionally managed assets in the regions covered by the report.[16] The 61% growth outpaced the growth in total professionally managed assets. As shown in figure 1, most of the SRI [17] assets in the report are located in Europe (63.7%) followed by the United States which, from 2012 to 2014, increased from 28.2% to 30.8%. The Global Sustainable Investment Review in its latest edition places special focus on impact investing[18] which relates to the core of social enterprising. Definitions of impact investing are still evolving, which might cause discrepancies in the regional classifications, where in some regions 'community banking deposits' and 'development finance' are included, and in others, as is the case in the European region, only 'investment assets' are counted.

[15] The Global Sustainable Investment Alliance is an international collaboration of membership based sustainable investment organizations.

[16] The results cover market studies of regional sustainable investment forums for Europe, the United States, Canada, Asia, Japan, Australasia and Africa.

[17] SRI covers sustainable, responsible, ethical, environmental, social investments and any other investment process that integrates financial analysis with the influence of ESG issues.

[18] In their 2014 edition there is a special focus on impact investing, which is defined by GSIA as "targeted investments, typically made in private markets, aimed at solving social or environmental problems".



Source: Global Sustainable Investment Review 2014

The European impact investing market increased by 146% since 2012 reaching about $28 billion at the beginning of 2014. Assets managed with an ESG[19] integration have grown 74% since 2012 and are estimated to cover 11% ($2.7 trillion) of all European professionally managed assets. Likewise, the US Social investment Forum (US-SIF) reported that 86 domestic asset managers and institutional investors identifying themselves as using impact investing strategies affected $36.8 billion in combined assets under management. Assets managed with ESG factors incorporated are valued at $6.20 trillion. Furthermore, the total US SRI assets were $6.57 trillion, a 76% increase over the 3.74 identified in sustainable strategies back at the outset of 2012. Under SRI, community/impact investing are to a certain extent included. Nonetheless, it only reflects a portion of social enterprise, due to the broad range of ESG investments such as: Negative/exclusionary screening[20], positive/best in class screening[21], norms-based screening[22], integration of *ESG* factors, sustainability themed investing[23], corporate engagement/shareholder action and, most importantly for this paper impact/community investment.

Table 1: Growth of SRI Assets by Region 2012-2014

	2012	2014	Growth
Europe	$8,758	$13,608	55%
United States	$3,740	$6,572	76%
Canada	$589	$945	60%
Australia/NZ	$134	$180	34%
Asia	$40	$53	32%
Total	$13,261	$21,358	61%

Source: Global Sustainable Investment Review 2014 *Asset values are expressed in billions

Anyhow, to correlate SRI with social enterprising is partially wrong, as it will reflect only a portion of community/impact investments. Nonetheless, it serves to show the increasing

[19] ESG criteria refers to the sustainable investing approach that considers environmental, social and governance, hence ESG, as factors in portfolio selection and management.
[20] The exclusion from a fund or portfolio of certain sectors, companies or practices contrary to ESG criteria.
[21] Investment in sectors, companies or projects selected that excelled in relation to their relative industry peers.
[22] Screening of investments against minimum standards of business practice based on international norms.
[23] Investment in assets specifically related to sustainability.

interest in SRI by investors building their portfolios. A study discovered that despite the skill of fund managers, on average, SRI mutual funds perform almost as well as other funds (Geczy, Stambaugh, & Levin, 2005). Furthermore, in the most recent edition of the Impact Investor Survey by J.P. Morgan and the Global Impact Investing Network, the survey captures data and market perspectives from 125 impact investors. Prominent results were found with regards to performance of impact investments. Among their most significant findings they reported that:

i. 80% of the respondents have their headquarters in Europe or the US while 70% of the assets under management are located in emerging and 30% in developed markets.
ii. In terms of capital committed, their intention is to invest 19% more in 2014 from $10.6 bn to $12.7 bn.
iii. About their priorities prior investing, 80% of the respondents indicated that financial returns are essential while 70% indicated that determining the impact objectives at the time of the investment is elementary.
iv. Collectively, the respondents manage a total of $46bn in impact investments, of which 58% is proprietary capital and 42% is managed on behalf of clients.
v. 54% reported that their objective is to obtain competitive market returns, 23% closer to market returns and 23% below market returns but closer to capital conservation.
vi. One of their most significant findings reveals that with regards to performance and risk of these investments, only 9% reported financial underperformance relative to expectations, 1% reported underperformance on impact, 16% outperformance against financial returns and 20% outperformance against their impact expectations.
vii. Microfinance represents a fifth of all respondents (21%), the same as Financial Services excluding microfinance, followed by Energy (11%) and Housing (8%).
viii. The capital managed is invested in: Seed/start-up companies (11%), post-venture stage companies (89%), growth stage companies (35%), mature private companies (44%), and publicly-traded companies (10%).

The survey concludes that most respondents are satisfied with their impact portfolios that seem to be in line with their expectations overall. Ultimately this reflects an increasing interest in impact investments as the respondents grew their capital committed. The next chapter will explain the background behind the notion that the traditional legal framework does not accommodate for-profit mission-driven companies in the U.S. and the divergent approaches to corporate/company purpose.

CHAPTER III

During the second chapter, diverging developments, approaches and definitions of social enterprises between the U.S. and the U.K were distinguished. The implementation of new entities meant to foster social enterprises reflects those deviating styles, as will be explained during chapter four. The reason to emphasize the rationale of the U.S. entities and include the U.K. rationale during the overview of the CIC is twofold. First, the different nature of the actors that pushed and/or work towards their implementation. In the U.S. the demand for special vehicles stemmed from private actors, mainly non-profits, while in the U.K. the CIC is born from a governmental initiative. The need to provide an in-depth explanation of the rationale behind the need for these forms in the U.S. is deeply connected with the implicit "*shareholder profit maximization*" nature of the jurisdiction. Whereas in the U.K. the underlying "*enlightened shareholder value*" nature of the jurisdiction, social business forms emerge from a different conditions.

3.1 The Rationale behind the Need for Social Corporate Entities in the US

There is no doubt that some forms of social enterprising, namely charities with insignificant commercial activities, foundations, corporate charity and firms with extend CSR commitments fit under the traditional for-profit/non-profit paradigm; however, mission-driven firms represent a unique challenge due to their characteristics, as it was identified in section 2.2. The two main reasons to doubt that traditional corporate law is able to accommodate mission-driven firms are: first, the limitations of the non-profit entities to access capital, distribute profits and sometimes they are limit to a certain amount of commercial activity without losing their tax exempt status. And, the second relates to the limits of for-profit entities which is deeply connected to the question whether corporation's sole purpose is to create value to its shareholders, the so-called *shareholder's wealth-maximization* maxim or *Shareholder Primacy*.

3.2 Non-profit Organizations as Social Enterprises

Typically, tax incentives and the nature of their purpose, drive social enterprises to incorporate as a non-profit entity. It was mentioned before that the concepts of charity and non-profit are tied to a segment of what could be regarded as a social enterprise in the U.S. The most defining characteristic of this kind of entity is the possibility to be exempted from federal income taxes and the possibility to receive tax-deductible donations. The first form of tax exemption first appears in the Tariff Act of 1894 stating that *"nothing herein contained shall apply to… …corporations, companies or associations organized and conducted solely for charitable, religious, or educational purposes."* Later on with the implementation of the Revenue Act of 1913 tax exemption was also granted to *"any corporation or association organized and operated exclusively for religious, charitable, scientific or educational purposes."* These benefits were further enhanced in 1917 with the introduction of tax deduction to donors for donations to non-profit organizations.

The problem emerges when those non-profit organizations want to include commercial activities as part of their operations, such as the sale of goods or provision of services, and retain their tax exempt status. The Internal Revenue Service (IRS) set the criteria to qualify for tax-exemption in section 501(c)(3) of the tax code. To qualify an organization should be: (i) "*a Corporation, community chest, fund or foundation", (ii) "organized and operated exclusively for one of the purposes identified by the IRS, hereinafter referred to generally as an "exempt purpose". (iii)"no part of the net earnings of which inures to the benefit of any private shareholder or individual", (iv) in addition, it may not be an action organization i.e., it may not attempt to influence legislation as a substantial part of its activities and it may not participate in any campaign activity for or against political candidates"*. At first sight the phrase "organized and operated exclusively" may disqualify any non-profit engagement in activities outside the exempt purposes. Yet the exemption criteria allow the non-profit to engage in other "substantial activities" even in the business sphere as long as the activity in question is "in furtherance of the organization's exempt purpose," according to section 501 (c)(3)-1(e).

The exemption criteria are not stringent by far about non-profits engaging in commercial activities, yet the boundaries of the definition of what 'substantial' means, the so-called "commerciality doctrine" has proven to be ambiguous. In essence the doctrine asks whether the non-profit business activity in question has a distinctive "commercial hue"[24]. Yet,

[24] In Airlie Foundation v. Internal Revenue Service 283 F. Supp. 2d 58 (D.D.C. 2003) The court stated that among the "major factors" courts have considered in "assessing commerciality" are competition with for-profit entities,

the commerciality doctrine fails to set a precise limit on the amount of profit a charity may earn from commercial conduct before losing its tax exempt status. In *Scripture Press Found. v. United States, 152 Ct. Cl. 463, 468 (1961)* the court deemed the existence of profits insufficient as evidence of a commercial purpose. In contrast, in a Private Letter Ruling[25] (PLR) (PLR) in 1980, the IRS told a non-profit that operated a prosthetic centre for injured veterans that, despite the fact that 47% of its revenue comes from the general public, they could retain their tax-exempt status (Doeringer, 2010). There is slight uncertainty while predicting whether conducting business will affect the tax exempt status, and above all the commercial activity must be insubstantial and further the exempt purpose. Needless to say, commercial activity cannot simply fund the exempt purpose as seen in *C.F. Mueller Co. v. Comm'r, 190 F.2d 120 (3d Cir. 1951)*, it must directly further the exempt purpose.

Satisfying this test shall not wholly exempt the non-profit from income tax responsibilities. IRC section 511(a) (1) imposes a tax on the unrelated business taxable income (UBIT) of organizations described in IRC sections 401, 501 and state colleges and universities. In principle UBIT shall be the applicable tax to "unrelated trade or business" income defined in I.R.C. section 513 as "any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its exempt purpose or function". In conclusion, non-profits are hindered by these tests, requirements and definitions that might be suitable for traditional charities, foundations, corporate charities, etc. Therefore non-profits suffer from significant barriers when it comes to conducting mission-driven business, meaning of course the inability to distribute residual earnings to individuals such as owners, stockholders, or anyone else, effectively removing the possibility to raise equity capital. Yet, payments for services rendered and for anything used in the work are permitted, and more importantly non-profits have limited sources of financing.

3.3 For-Profit entities as Social Enterprises

Social enterprises could, to a certain extent, incorporate as any of the traditional business forms available. Yet, for social enterprises' goals, the question relies on whether an implicit or explicit [legal] duty to maximize shareholder value exists while making use of any of these forms, and the degree of manoeuvrability that directors possess when taking non-shareholder constituencies into consideration in their decision-making process as part of the ultimate goal of the corporation. The corporate purpose incognita goes back to the 1930's, in a debate between two renowned corporate scholars, Adolf A. Berle and E. Merrick Dodd, featured in Harvard Law Review. In a nutshell, the series of position papers and responses referred to two adversary-like positions with regards to the corporate purpose. Berle proposed a trustee model in which the directors acted as trustees of the corporation on behalf of the shareholders, and this model granted him the title of "forefather of shareholder-primacy" (Bratton & Watcher, 2008). In response, Dodd advocated a position in which management must show discretion and choose the appropriate social goals for the corporation in addition to its profit-making function (Easterbrook & Fischel, 1996). His response caused him to be regarded as supporter of CSR or predecessor of progressive "communitarian" theories of corporate

extent and degree of low-cost services provided, pricing policies, and reasonableness of financial reserves. The court observed that the organization in this case "engages in conduct of both a commercial and exempt nature." It thus concluded that its entitlement to tax-exempt status "turns largely" on the primary purpose test. Using that test, the court found undue commerciality.

[25] A private letter ruling, or PLR, is a written statement issued to a taxpayer that interprets and applies tax laws to the taxpayer's represented set of facts. A PLR is issued in response to a written request submitted by a taxpayer. A PLR may not be relied on as precedent by other taxpayers or by IRS personnel (IRS, 2015).

governance (Mitchell, 1995). Years after, commentators and academics alike recognized the failure to solve the dilemma between these competing forms of interpretation of the corporation's purpose, and others even asserted that there is a misinterpretation of Dodd's and Berle's positions.[26]

Another different manner in which to arrive at the same conclusion of shareholder's primacy is to rely on certain models of corporate governance (Choudhury, 2009). One of these models is the property-centric view of corporations, of which its most famous supporter was Milton Friedman. Friedman claimed that in a "free-enterprise, private property system, corporate executives are the employees of the business owners (the shareholders) and, accordingly, owe these owners a duty to conduct the business so as to make as much money as possible" (Friedman, 1970). Yet this view is partially incorrect, as it is the case for publicly-traded companies, in which the shareholders merely own its shares, despite the possibility to acquire a controlling block and remove/replace management components that oppose their interests. A second governance model that supports shareholder primacy is the corporation as a "nexus of contracts". Contractarians perceive the corporation as the sum/nexus of contracts between its constituencies (Easterbrook & Fischel, 1996). The nexus of contracts model sustains that "shareholder primacy is justified because stakeholder interests enjoy contractual protection that is not similarly available to shareholders" (Bainbridge, 1993). It is assumed that stakeholders will contract *ex ante* for a compensation of the losses sustained as a result of the shareholder primacy norm.

Decades of debate left more side-questions by the different approaches than half-answers. Nonetheless, there are strong reasons to believe that, to a great extent, shareholder primacy is the ultimate guideline for a corporation's purpose in the U.S. Although the law, as written in most statutes addressing the corporate purpose, remains agnostic or neutral, allowing any lawful purpose. For example, the Delaware General Corporation Law (DGCL) Title 8. Section 101 (b) indicates that:

"the purpose of the corporation is to engage in any lawful act or activity for which corporations may be organized under the General Corporation Law of Delaware, and by such statement all lawful acts and activities shall be within the purposes of the corporation, except for express limitations, if any"

Other statutes make use of similar provisions regarding the nature of the corporate purpose. The reason to emphasize Delaware's provisions is linked to the ongoing preference of the majority of U.S. corporations to choose Delaware as their state of incorporation, which is also the reason to present a brief overview of the development judicial doctrine behind corporate purpose and its relation with managerial discretion.

3.3.1 Shareholder Primacy and Managerial Discretion.

It must be noted that case law has developed a great degree of inclination towards shareholder primacy as a standard. As stated before, in the U.S. the judiciary has a proactive role in shaping the direction of business norms, and evidence of shareholder primacy can be tracked back to *Dodge v. Ford Co., 170 N.W. 668 (Mich.1919).* John and Horace Dodge, then minority shareholders in the Ford Motor Company, challenged the decision of company founder and majority shareholder Henry Ford to stop the company's practice of paying special

[26] Bratton & Watcher (2008) observed that in fact neither Dodd nor Berle were supporting either position. Both were speaking to the politics of their time, defending a side yet without formally choosing one, Berle on the right and Dodd on the left.

dividends. Ford argued that his intentions were to direct the company's resources to expand the business, lowering the price of cars, and increasing the wages of the workers. At the trial his testimony indicated that he believed that the company was making excessive earnings and that it was preferable to be less profitable. The brothers argued and the court agreed, that Ford's actions perverted the corporation's purpose (Sneirson, 2011). In the context of the corporate purpose the Michigan Supreme Court dictated:

"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. The discretion of directors is to be exercised in the choice of means to attain that end, and does not extend to a change in the end itself, to the reduction of profits, or to the non-distribution of profits among stockholders in order to devote them to other purposes."

A recent case upholding the *Dodge v. Ford Co* decision is *eBay Domestic Holdings, Inc. v. Newmark, et al., C.A. No. 3705-CC (Del. Ch. 2010).*The case involves a minority investment (28.4%) by eBay in Craigslist and the majority shareholders and directors of craigslist Craig Newmark (42.6%) and James Buckmaster (29%). Craigslist, despite being a for-profit corporation, operated to a certain extent as a community service, craigslist's revenue stream originated from fees for online job postings in certain cities and apartment listings, rather than selling advertising to third parties. And regardless of its market share, which effectively made it the leader for online classifieds at the time, the site did not focus on monetization. After all, with only thirty-four employees craigslist is a small firm. In contrast, eBay is a large publicly traded company under a sophisticated business model operating with a fully monetized website, charging customers a fee for every sale made through its portal; eBay's main focus lay on expanding and enhancing its market share through acquisitions and actively advertising its services. The significant difference in eBay's approach conflicted with craigslist's underlying community service purpose.

At the time when eBay made its investment in craigslist in August 2004, it was negotiated in the Stock Purchase Agreement that eBay reserved the right to compete with craigslist. In the case that such competition appeared: (i) eBay would lose various negative covenants with respect to craigslist, (ii) eBay shall effectively lose any preemptive rights in connection with new share issuances of craigslist's stock, and, (iii) eBay would lose its right of first refusal with respect to any sale of shares by Newmark or Buckmaster. Craigslist's board of directors consisted of three persons, who were elected by cumulative voting ensuring that Newmark and Buckmaster got two seats and eBay had enough to claim the remaining seat. Not long after the negotiation, eBay launched Kijiji, an international classified ads service. As a response to Kijiji expanding to U.S. territory in June 2007, craigslist made three moves that resulted in the lawsuit: (i) implementation of a staggered board through amendments of the bylaws, (ii) approval of the "Rights plan"; and (iii) an offer to issue new craigslist stock in exchange for every share on which a craigslist's shareholder granted a right of first refusal in favor of craigslist, a sort of dilutive issuance mechanism. It is no surprise that the court found Newmark's and Buckmaster's reactions to be breaching their duties towards eBay.

There is a remarkable similarity with *Dodge v. Ford Co* in the analysis of Chancellor Chandler of the "Rights plan". Craigslist, as a closely held corporation with Newmark and Buckmaster acting as controlling shareholders, are in an evidently similar position as Ford's; as controlling shareholders they owe a fiduciary duty to the corporations' minority stockholders. Despite the fact that the Chancellor noted that: *"Jim and Craig did prove that they personally believe craigslist should not be about the business of stockholder wealth maximization, now or in the future. As an abstract matter, there is nothing inappropriate about an organization seeking to aid local, national, and global communities by providing a website*

for online classifieds that is largely devoid of monetized elements. Indeed, I personally appreciate and admire Jim's and Craig's desire to be of service to communities." the Chancellor followed the same line of reasoning in his analysis as *Dodge v. Ford Co.* by stating that:

"The corporate form in which craigslist operates, however, is not an appropriate vehicle for purely philanthropic ends, at least not when there are other stockholders interested in realizing a return on their investment. Jim and Craig opted to form craigslist, Inc. as a for-profit Delaware corporation and voluntarily accepted millions of dollars from eBay as part of a transaction whereby eBay became a stockholder. Having chosen a for-profit corporate form, the craigslist directors are bound by the fiduciary duties and standards that accompany that form. Those standards include acting to promote the value of the corporation for the benefit of its stockholders.

Some authors and academics undermine the impact of the *Dodge v. Ford Co.* decision, stating that its influence is minimal[27] with regards to the director's decisions about the corporate purpose; yet, a couple of cases share the same line of reasoning, as seen in eBay Domestic Holdings Inc. v. Newmark. This is not unexpected or novel, because directors, by possessing the power to manage and direct the corporation, owe the fiduciary duties of care and loyalty to the corporation and its shareholders. The duty of care refers to the requirement that directors inform themselves adequately as to all reasonably attainable information prior to acting on that decision[28]. And the duty of loyalty mandates that "the best interest of the corporation and its shareholders takes precedence over any interest possessed by a director… …and not shared by the stockholders generally" (Warren & Aronstam, 2007).

In the day-to-day management of the company, directors are permitted to consider other non-shareholder constituencies, as long as they can prove a rational connection between that consideration and shareholder value, and without breaching their fiduciary duties; the so-called business judgement rule allows them to do so, as stemmed in *Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984)*. The business judgement rule together with the enhanced scrutiny and the entire fairness test, form what some regard as the tiers of review for evaluating directors' decision making (Bainbridge S., 2011). The business judgement rule was articulated as a mechanism to protect and promote the role of the board as the supreme manager of the corporation, in *Aronson v. Lewis*, the business judgement rule is defined as such:

"It is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company."

The business judgement rule serves as a shield against second guessing director's decisions by the courts.[29] However, under special circumstances, namely a shift of control due to the possibility of a sale, it is unavoidable; managerial discretion shifts from the responsibility for the well-being of the entity into the pursuance of shareholder value maximization. The defenders of the corporate bastion turn into auctioneers with the sole end of obtaining the best

---

[27] Professor Lynn Stout (2008) notes that the context in which the *Dodge v. Ford Co.* has been cited once or twice in the past 30 years involves minority shareholder oppression rather defense of the shareholder primacy.

[28] In *Smith v. Van Gorkom, 488 A.2d 858, 872 (Del . 1985)* the Court of Chancery of the State of Delaware uphold *Aronson v. Lewis* by stating that that prior to making a business decision, directors must have informed themselves of all material information reasonably available to them.

[29] As noticed in *Orman v. Cullman, 794 A.2d 5, 20 (Del. Ch. 2002),* "the judgement of a properly functioning board will not be second-guessed and 'absent an abuse of discretion, that judgment will be respected by the courts.'"

possible deal in benefit of the company's shareholders.[30] And it is under these circumstances, usually referred as "*Revlon mode*", that the applicability of the business judgement rule is determined by the second tier, the "*Enhanced Scrutiny Test*"[31]. There are two steps in applying the test: (i) the reasonableness test that requires the board to demonstrate reasonable grounds to believe that a danger to corporate policy and effectiveness exists. After the first step is met, (ii) the court applies the proportionality test that requires the board to justify that its actions are reasonable in relation to the threat posed and that the response was not draconian and inappropriate to the threat (LII). Taking a step back to *eBay Domestic Holdings, Inc. v. Newmark*, remember the "staggered board" and "Rights plan" moves by craigslist. These defence mechanisms were evoked to protect craigslist and its corporate purpose; yet they were deemed as inappropriate measures with relation to eBay's competition threat, as noted by Chancellor Chandler:

These "*defensive devices that, if used correctly, can enhance stockholder value but, if used incorrectly, can entrench management and deter value-maximizing bidders at the stockholders' expense."*

The last tier to evaluate director's decisions is the entire fairness[32] test. For the purpose of this paper the test lacks of a connection with the corporate purpose. Instead the test serves as a way to displace the business judgement rule when a plaintiff successfully refutes its presumption. In short, the entire fairness test aims to protect the shareholders' interests when conflicted directors and/or controlling shareholders might be motivated by personal or individual gain, exercising their influence at the expense of shareholders' value as a class.

This section reviewed the precedents indicating shareholder primacy as the concept that drives corporate decision-making in the U.S. and to a great extent trumps over all non-shareholder constituencies. However, some academics still claim that shareholder primacy is not legally mandated, either in an explicit or implicit manner. This paper takes a neutral position in this regard, despite the fact that the evidence found in case law proves shareholder primacy steers judicial decisions; sustaining such a claim would only be possible in the narrow context of change of control of the firm. Still, *eBay Domestic Holdings, Inc. v. Newmark* provides a glimpse into the concerns of employing for-profit traditional entities for mission-driven firms. Paraphrasing Chancellor Chandler, even when philanthropic ends are allowed and praised, such ends do not quite fit in the corporation's purpose. The next section explores the so-called constituency or stakeholder statutes in the quest to try to fit social enterprises in the traditional paradigm.

[30] The so-called Revlon duties were introduced in *Revlon v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173 (Del.1986)* the Delaware Supreme Court held that when the sale of a company is unavoidable, the directors' duties shift from "defenders of the corporate bastion" to "auctioneers charged with getting the best price for the stockholders in the sale of the company".

[31] It is also referred as the UNOCAL test developed in *Unocal Corp. v. Mesa Petroleum, 493 A.2d 946 (Del. 1985)* , which is applied to a target's board decision making process under the threat of a takeover in order to determine if the business judgement rule will apply.

[32] As developed in *Weinberger v. UOP, Inc., 457 A.2d 701 (Del. 1983)* the test is not a bifurcated test, yet the court will take into account two aspects: fair dealing and fair price. Fair dealing answers the questions of when the transaction was timed, how was negotiated, initiated, structured and, how the approval was obtained by directors and shareholders. Fair price refers to the economic and financial considerations of the transaction in question.

3.3.2 The Constituency Statutes

These statutes expressly allow the management decisions to consider: (i) non-shareholder constituencies, namely employees, customers, suppliers, creditors and the community at large, (ii) long-term and short term interests of the firm, (iii) any other relevant community and societal considerations; and, (iv) the continued independence of the firm (Lovett & Basel). Their implementation was caused by the frenzy of hostile takeovers in the 1980's (Lawrence, 1992). In 1983, Pennsylvania became the first out of 41 states[33] that currently possess this legislation. At its conception the constituency statutes' main goal was to provide one more line of defence for target companies against hostile takeovers by decreasing director's accountability to shareholders. While some of these statutes are limited to the takeover context generally, others represent a direct rejection of the shareholder primacy nature of the corporate purpose (Million, 2010). CSR proponents noticed that these statutes were not limited to change of control situations, and claimed that the states that adopt such legislation are effectively a safe haven for socially responsible businesses. Indeed at first sight the constituency statutes are applicable to all director's decisions regardless of the context, yet these statutes are written in a language that might be considered permissible.

Jonathan Macey (2008) argues that constituency statutes do not change the legal landscape with respect to shareholder primacy: "these statutes cannot rationally be construed to permit managers to benefit non-shareholder constituencies at the expense of shareholders. Rather, these statutes are mere tie-breakers, allowing managers to take the interests of non-shareholder constituencies into account when doing so does not harm shareholders in any demonstrable way;" However, Sneirson (2009) argues the exact opposite: "states that constituency statutes expressly permit decisions that elevate other, non-shareholder considerations… …over the maximization of shareholder wealth." For mission-driven firms, the key concern lies in the permissible nature of the statutes, which allows, yet does not require consideration of stakeholders' interests that are the core of the corporate purpose of these kinds of firms. The consequences of having a permissible approach in claiming to be a social responsible business undermines the credibility of the firm. It is evident that the possibility to take non-shareholders' interests into consideration is akin to the mission-driven firms, case law interpreting these statutes have shown to be insufficient to determine to what extent directors can consider those interests, at expense of whom are considered and the role of the *Revlon* duties in their decisions.

The impact in directors decisions while considering non-shareholders' constituencies was raised in the Pennsylvania in *Keyser v. COM. NAT. FINANCIAL CORP., 675 F. Supp. 238 (M.D. Pa. 1987).* In a *Revlon* context, the court sustained that section "*1408 was amended to add subparagraph (B) which provides:*

In discharging the duties of their respective positions, the board of directors, committees of the board, individual directors and individual officers may, in considering the best interests of the corporation, consider the effects of any action upon employees, suppliers and customers of the corporation, communities in which offices or other establishments of the corporation are located and all other pertinent factors."

Thanks to the statute, the defendant board could consider so-called social issues in evaluating merger proposals. Yet, a side problem arose at the summary of the judgement where the court noted that: *"The extent to which price could be sacrificed for these so-called social issues in the factual context of this case is not a proper determination for the court."* This

[33] Notably Delaware has not enacted one of these statutes.

decision in particular raises the question, who decides what the director's duty of care mandates in constituency jurisdictions? It is not the objective of this paper to answer such questions. Ultimately, for mission-driven businesses, the concern is not to be able to provide enhanced managerial discretion, nor to consider social issues to the detriment of shareholders or to decrease director's accountability. Mission-driven firms indeed need to be able to consider stakeholders, shareholders and society as a whole. In order to do so effectively, directors must be accountable for their decisions.

3.4 Enlightened Shareholder Value, the UK's approach to Company's Purpose

Enlightened shareholder value (ESV) refers to the pursuit of shareholder wealth by a long-term strategy that seeks above all sustainable growth and profits while responsibly considering the company's relevant stakeholders and other factors. The ESV concept was first introduced in the UK Companies Act 2006, which determines that the management's ultimate responsibility is to the shareholders, but it is required to pursue that objective with regards to long-term consequences, employee interest, relations with suppliers, customers, and others, impact on the community and environment, and the company's ethical reputation (Millon, 2010). Under section 172 (1) of the UK's Companies Act 2006 provides the "Duty to promote the success of the company" as follows:

i. *A director of a company must act in the way he considers, in good faith, would be most likely to promote the success of the company for the benefit of its members as a whole, and in doing so have regard (amongst other matters) to—*
    a. *the likely consequences of any decision in the long term,*
    b. *the interests of the company's employees,*
    c. *the need to foster the company's business relationships with suppliers, customers and others,*
    d. *the impact of the company's operations on the community and the environment,*
    e. *the desirability of the company maintaining a reputation for high standards of business conduct, and*
    f. *the need to act fairly as between members of the company.*

ESV effectively represents the mean between strict shareholder primacy and the pluralist vision of stakeholder democracy. Needless to say, ESV does not place stakeholders' interests over shareholders' at all, the approach seeks to reject short-term strategies in favour of sustainable long-term strategies for the firm. In Section 172, stakeholders are categorised as internal stakeholders, such as employees, and as external stakeholders, such as creditors, customers and suppliers, as well as the environment and the local neighbourhood etc. This reform is also known as the 'enlightened shareholder' theory (Zhao, 2011). Furthermore, a long-term strategy would necessarily require the directors to consider the full extent of stakeholders' interests that may affect the possibilities for the company to succeed. The ESV concept is akin to social enterprising and notions of CSR, yet it falls short because the concept "to consider" is significantly beneath the concepts of "duty" and "obligation" to benefit society, and slightly beneath the concept of "balance" of all the constituencies of the firm. Nevertheless, the differences between both jurisdictions keep emerging during this paper, differences that stem from their diverging socio-economic conditions.

During this chapter, the rationale behind the need for social business forms in the U.S. and the divergent nature and concept of corporate purpose in both jurisdictions was reviewed.

During the next chapter these new forms will be explained in detail starting with the origin, rationale and characteristics of the Community Interest Company.

CHAPTER IV

4.1 The United Kingdom's Community Interest Company

The prelude of the appearance of the most robust social enterprise framework in Europe, namely the CIC (as stated earlier in this paper), began in 2001 under a slightly outdated society law[34] which had not been updated since 1965. Back then, the British government saw social enterprising as a convenient device to close the productivity gap with the US (Doeringer, 2010). The establishment of the Social Enterprise Unit was essential, its main objective was to identify the growth barriers of the social enterprise sector in the UK. One year after its creation as part of the first report, the unit defined "social enterprise" as a "business with primarily social objectives whose surpluses are principally reinvested for that purpose in the business or in the community, rather than being driven by the need to maximise profit for shareholders and owners" (Lloyd, 2010). This report further recognized four major areas that could be developed:

i. promote a transparency culture where all information about the social enterprise is available,
ii. guarantee that social entrepreneurs are well informed and have the possibility to receive advice
iii. make sure that financing is available for the social enterprise; and
iv. safeguard that social enterprises are able to conduct business (Doeringer, 2010).

The British government also created a £10 million fund and began developing metrics to measure the social impact of these entities. At the time, the choice of forms available for the social sector was similar to that available in the US, either [limited] companies or charities. Charities in the UK possessed a similar tax deduction to the US, the bottom tax rate was and still is 20% (GOV.UK, 2015) and they were able to engage in limited commercial activities as long as it directly advanced their purpose. The only choice of action available to them to increase the amount of this commercial activity was to set up a trading company, which is a variant of a limited company with restrictions on its distributions that cannot be done through a dividend. Needless to say, to set up two different entities and comply with two different set of requirements raises the costs of the company. The special unit did not miss this structural form used by one third of all charities prior to 2002 (Doeringer, 2010). Having fulfilled its purpose, the special unit communicated its final conclusion to the Parliament, strongly advising the creation of a special business entity that addressed the needs of the social enterprise sector and enhanced its capabilities. Finally, on the first of July of 2005 the Community Interest Company Regulations were enforced, making it possible to register as a Community Interest Company. The CIC is in essence a limited company that possesses a set of requirements and restrictions that guarantee that the company will pursue social interests.

[34] Stephen Lloyd claims that company law for the British government is the "Gold Standard" fundamental for the British economy and society. He explains that company law usually receives reforms every 8 years during his professional life notably, the law of societies did not.

4.1.1 Characteristics and Restrictions of Community Interest Companies

An organization that seeks to become a CIC must have the goal to benefit the community, and operate in a manner that furthers this cause. A community in the context of the CIC will be understood as a whole or a definable sector or group of people. Any group of individuals may constitute a community if they share a common feature that distinguishes them from the other members of the community and "a reasonable person might consider that they constitute a section of the community (Office of the Regulator of Community Interest Companies, 2012)." Moreover, subjecting to the regulatory regime of the CIC means that the entity will pursue a beneficial outcome for the community, rather than individual gain or the interest of a small group. CIC's are designed to be business entities governed by company law and are not allowed to be registered as charities, yet a charity is able to convert with the consent of the Charity Commissioners or the Scottish Charity Regulator. Additionally, organizations with a political nature[35] are unable to register as CIC's (Community Interest Company Regulations, 2005). Organizations must proceed cautiously before adopting the form, becoming a CIC has permanent long-term consequences. According to the CIC guidelines, regulations and related legislation, organizations must comply with all requirements and restrictions, and take into account the particular characteristics of the CIC meant to protect the community's benefits, as explained below.

Adoption of the CIC form. In addition to the documentation related to conversion or adoption of the form, existing companies need to pass a special resolution with a twenty-one day notice that must be given to their members. A majority of 75% of members voting in favor of the adoption or conversion is required (Office of the Regulator of Community Interest Companies, 2013).

Legal Structure. An organization that aspires to become a CIC is able to do so in three different forms: CIC limited by shares, CIC limited by guarantee, or alternatively, Public Limited Company (PLC). Regardless of the chosen structure, a CIC name must end in CIC or Community Interest Company and not Limited or Ltd.

Capital Structure. The CIC limited by shares has a dual purpose: to create a profit for its shareholders and to benefit the community. In contrast, profits of a CIC limited by guarantee shall be either reinvested in the CIC or used for social purposes.

Legal Framework. CICs are subject to company law as set in the Companies Act 2006 and related CIC legislation, namely the Companies (Audit, Investigations and Community Enterprise Act 2004; CAICE Act) and the Community Interest Company Regulations 2005.

Community Interest Test (Enhanced Company's Purpose). The main criteria to qualify as a CIC is the "Community Interest Test", this test was defined for the first time in the Companies Act 2004. The test is "whether a reasonable person might consider that the company's activities are being carried out for the benefit of the community." It is not a one-time accreditation, the company must continue to satisfy the test so long as it remains a CIC.

[35] Organizations such as political parties, political campaigning organizations or their subsidiaries.

The Regulator (Accountability). CICs are regulated by, monitored by and accountable to the Community Interest Companies' Regulator[36]. The Regulator considers the registration, conversion and documents for new CIC's, and decides whether the organization is eligible. The British government expected that the role of the regulator be of a "light-touch regulator" that guides, monitors and reviews new applications, and decides whether the registration or conversion is refused or accepted, rather than proactive scrutiny. Nonetheless, the Regulator possesses the power to investigate similar to the power of the Secretary of State. If it is deemed necessary, the regulator is able to appoint auditors, at her expense, to examine the accounts of a particular CIC (Office of the Regulator of Community Interest Companies, 2013).

The role of the Regulator is deeply linked to the enforcement procedure, despite the "light touch" regulatory regime. The Regulator will consider all the information and complaints from shareholders or any stakeholder about any existing CIC and their activities, and when necessary seek further information. When possible, the regulator shall seek to solve the matter informally with the CIC in question. When this is not possible due to the nature of the complaint or misconduct, the Regulator shall take appropriate enforcement action. The regulator possesses the following enforcement powers: (i) to bring civil proceedings in the name of a CIC, where its members or directors have failed to do so, (ii) to appoint or remove directors when a default condition[37] has arisen, (iii) to appoint a manager of a CIC to take control of specific aspects of the company's affairs that gave cause for concern, (iv) to vest (in trust) the property of the CIC upon the emergence of a default condition, (v) to order the transfer of shares or to extinguish an interest in a CIC by guarantee when a company appears to be an "excluded company,"[38]((vi) to present a petition to the court for the winding up of a CIC, and (vii) to apply to the court for a restoration to the Register of a particular CIC (Office of the Regulator of Community Interest Companies, 2013).

A Regulator decision might be appealed in accordance with the CAICE Act and CIC Regulations. Section 28 of the CAICE Act provides the criteria for the appointment of the Appeal Officer for CICs and describes her jurisdiction. Appeals may be brought on the grounds that the Regulator's decision was made with a material error of law or fact in accordance with the provisions of the CAICE Act. The Appeal procedure begins by sending a notice of appeal to the Regulator within two months of the date that the Regulator decision was enforced, except in relation to residual asset distribution in the winding up of a CIC, where the period is significantly lower. The Appeal Officer may allow the appellant and/or the Regulator to make oral or written representations, at any time the Appeal Officer may dismiss the appeal if she deems it unfounded, or she considers that the appellant is not entitled to bring the appeal in accordance with the CAICE Act. Upon reaching a decision, the Appeal Officer shall provide the appellant and the Regulator with the rationale behind her conclusions and the Appeal Officer, when she deems it appropriate, shall publish her decision (Office of the Regulator of Community Interest Companies, 2013).

Annual Report (Transparency). All the directors of a CIC have the obligation to prepare an "Annual Community Interest Company Report", which will be available to the public. The purpose of this report is to ensure that the CIC continues to satisfy the "Community Interest

[36] The British government expects that the Regulator encourage that development of the CIC "brand" and provide guidance and assistance on matters related to CICs.

[37] The Default condition arises where: (i) there has been a misconduct or mismanagement in the administration of the CIC, (ii) there is a need to protect the company's property, (iii) the company is not satisfying the community interest test; or (iv) if the company has community interest objects and it is not carrying any activities in pursuit of those objects.

[38] Any organization of political nature or within the criteria stated in Part 2 of the Community Interest Company Regulations 2005.

Test" and that it has been operating in a manner that benefits the community. The requirements of the Annual Report to the Registrar of companies include: (i) accounts, (ii) a CIC report with a £15 filing fee, and (iii) Annual return with a £15 filing fee. Similarly to ordinary companies, CICs are required to deliver copies of their accounts for each financial year to be placed in the public file. The requirements and penalties related to this component are similar to those for limited companies in accordance to the CAICE Act. However, unlike typical companies a CIC must prepare an Annual CIC Report to prove that the company keeps satisfying the Community Interest Test and has been operating in a manner that benefits the community.

The CIC regulations 2005 contain the minimum requirements for the Annual CIC report which include: (i) details of what the CIC has done to benefit the community, (ii) details of how the company has consulted its stakeholders about its activities, (iii) details of dividends declared (or proposed) on shares in compliance with the capping rules, and (iv) information on the transfer of assets to another locked body at less than market value for the benefit of the community. The Regulator provides a model for the CIC report, reviews the annual reports, provides feedback and is able to act accordingly in case of abnormalities. The last component is the Annual Return, which in essence is an updated overview of the essential information of the company (Office of the Regulator of Community Interest Companies, 2013).

Asset Lock. The asset locking restriction is meant to bind the capital to the CIC and its goals. In order to transfer any CIC's asset, such transfer must meet at least one of the following criteria: (i) It is made for full market value so that the CIC retains the value of the asset in question, (ii) it is made to another asset-locked body[39] as specified ex ante in the CIC's Articles of Association, (iii) it is made to another asset-locked body with prior consent of the Regulator; or (iv) the transfer shall benefit the community. CIC's assets cannot be returned to its members unless they themselves are considered asset-locked bodies. Yet, assets can be used as collateral, the transferability limitation is meant to protect the CIC's assets, rather than a bar to the CIC's normal trading, business activities or ability to meet its financial obligations. CICs structured as limited companies by shares must follow special rules for dividend distribution and every CIC is subject to a restrictive performance related interest cap.

Dividend and Performance Interest Caps. CICs with a share capital are able to adopt two different regimes to distribute dividends to its shareholders. The first, Schedule 2, restricts the payment of dividends to specified asset-locked bodies, or other asset-locked bodies with the Regulator's consent. Under Schedule 2 the amount payable as dividends is not subject to any dividend cap, yet must comply with the rules and constrains applicable to ordinary companies. The second, the Schedule 3, allows the CIC to pay dividends to shareholders who are not asset-locked bodies. However, the payment of a dividend is subject to a dividend cap[40]. The dividend cap has a single element called the maximum aggregate dividend cap of 35%, and it is meant to ensure that 65% of the CIC's profits are reinvested back into the company or serve in benefit of the community. Another restriction refers to the rare circumstances in which a debt or debentures are linked to the performance of the Company[41]. CICs possesses the same borrowing power of an ordinary company; however, with regards to performance related debts, because they are regarded to work similar to equity shares, if they would remain uncapped there would be a significant possibility that they become a way to circumvent the above

[39] Asset Locked body includes: Another CIC, a charity, a registered society or non-UK based equivalents.

[40] The cap previously had three elements: (i) dividend per share cap, which is link to the paid-up value of the share, (ii) the maximum aggregate dividend cap; and (iii) the capacity to carry-over unused dividend payments for up to 5 years. The dividend per share cap was removed on the first of October 2014 because it prove to be overcomplicated and restrictive discouraging investors from investing in CICs (GOV.UK, 2014).

[41] Sometimes such debts are called debt with equity characteristics.

mentioned *aggregate dividend cap*. Therefore, they are subject to 20%[42] of the average amount of a CIC's debt, or sum outstanding debenture issued by it, during the 12 month period immediately preceding the date on which the interest on that debt becomes due. (Office of the Regulator of Community Interest Companies, 2014).

Redemption and repurchase of shares. Sections 30(1) & (2) of the CAICE Act and Regulations 24 and 25 of the CIC Regulations 2005 impose additional rules to redeeming shares, share repurchases or reduction of share capital. The rationale behind this is that without restrictions, the asset-lock provisions would be avoidable and the CIC's assets would be unprotected. Regulation 24 protects the assets of the CIC from share redemption or repurchase unless the payments are set equal or below the paid up value of the shares. Any share related transaction in this regard must not exceed the paid up value of the shares, that is to say, the amount of the nominal value plus any premium paid. Additionally, the Articles of Association must comply with the Companies Act 2006 and CIC regulation in this regard. Regulation 25 prevents CICs from distributing their assets by decreasing their share capital, unless it is done by: (i) reducing part of the value of shares that is not paid up, or (ii) by paying to members no more than the paid up value of their shares (Office of the Regulator of Community Interest Companies, 2014).

Director's duties (Accountability). As mentioned before at the end of chapter 3, in connection to the ESV reform, the duties of the director consist of creating shareholder value which is still the primary task of management, but the management now has a duty to have regard to various stakeholder interests in connection with the company's interests in the long term (Zhao, 2011). The CIC's related regulation does not contain any special provisions outside the above mentioned consideration. There is an implicit obligation to pursue the benefit of the community as a CIC and state how that goal will be achieved.

De-registration, Conversion and Winding up. The only way to cease being a community interest company is by dissolution or conversion to a charity or another asset-locked body, such as an Industrial and Provident Society[43]. In any case, the Regulator will ensure that all the procedures have been followed and in the case of liquidation or winding up, she oversees that any surplus assets are transferred in a manner such that they remain available for community interests or charitable purposes rather than distributed to investors (Office of the Regulator of Community Interest Companies, 2013).

As seen above, CICs are subject to a complex set of rules, regulations and restrictions meant to prevent the misuse of the entity and create a credible brand. In comparison to other strictly for-profit or non-profit entities, CICs have access to grants and soft loans from the Community Development Finance Institutions (CDFIs) which are not available to ordinary companies. CDFI's investors have a 5% tax relief while investing in a CDFI. Nonetheless, the British government expects that CICs finance themselves through inward investment and trading. Furthermore, the registration procedure is fairly simply and scrutinized by the Regulator whom decides whether an organization qualifies to become a CIC. Yet the main issue the form has had in recent years was a lack of credibility as a brand. Commentators have

[42] Notably on the first of October 2014 the Performance Interest cap was increased from 10% to 20% under the same rationale followed to remove the dividend cap per share, namely to make the CIC more appealing for investors

[43] IPS or Industrial and Provident Society is an asset locked-body that conducts trade or business either as co-operative or in benefit of the community, the British equivalent to Social Cooperative. The IPS key features are democratic control (one member, one vote).

pointed out that the trade-off of becoming a charity over a CIC is the public awareness that charities always represent the community's interest, tax benefits and access to funding that non-charitable bodies cannot have. Naturally, these benefits would be at the expense of restriction on their objects, restrictions on commercial taxable trading and other constrains related to non-profits.

4.2 The United States' Low Profit Limited Liability Company (L3C)

In 2008, Vermont became the first state to enact the L3C legislation. Until now, eight other states have passed similar legislation allowing the creation of such entities. The L3C is a for-profit business form designed to retain the flexibility of a limited liability company (LLC) with the primary goal to achieve social or charitable benefits (Esposito, 2013). Moreover, it is structured to facilitate financing through program related investments (PRIs). Unlike the CIC which stems from an in-depth analysis of the socio-economic problems related to social enterprising, the L3C emerges from the observation that PRIs could be used to a great extent to capitalize social enterprises in the U.S. PRIs can be structured in multiple ways, as a loan, equity, loan guarantee, or any other transaction with an economic interest. In order to be able to fully understand the L3C, it is most important to understand the IRS provisions relevant to tax-exempt entities and PRIs.

A program related investment (PRI) is designed with the sole purpose of furthering a tax-exempt entity's exempt purpose, having the specific characteristics: (i) its primary purpose falls within the charitable purposes in accordance to I.R.C. section 170 (c)(2)(B), (ii) neither profit or appreciation of profit is the reason of the investment, and (iii) it does not fall within the excluded purposes such as lobbying or others of a political nature. Section 170 (c)(2)(B) defines charitable as being "organized and operated exclusively for religious, charitable, scientific, literary, or educational purposes, or to foster national or international amateur sports competitions (as long as it doesn't include the provision of equipment and athletic facilities)or for the prevention of cruelty to children or animals". The foundation has the responsibility to identify the nature of the purpose pursued by the organization in which the investment will be made and to ensure that its activities match with the foundation to qualify as a PRI. Moreover, foundations are different from charities, they are indeed recognized in IRC section 501 (c)(3) as one of the twenty-eight types of organizations[44] entitled to be receive tax exempt benefits.

Private foundations do not possess the same degree of regulation and tax benefits as charities, they are subject to somehow stricter requirements and restrictions. Yet, they are permitted to take full advantage of the PRI's part of non-profit law since the 1969 Tax reform. In a nutshell, PRIs open an optional path for foundations to make tax-free investments in socially beneficial business rather than donating the same amount to charities. As part of the foundation's annual obligations they have a "five percent qualifying distribution requirement". According to IRC section 4942 (e)(i)(A), private non-operating foundations must spend at least five percent of an average market value of their previous year's assets on charitable purposes. It used to be that foundations fulfilled the requirement through donations, for which they received zero return on investment. Yet, since their appearance, PRI's are not used as often as they were meant to be, the reason being that failure to invest in the correct organization jeopardizes the tax-exempt entity status. Steven Lawrence (2010) reported that "Of the nation's more than 75,000 grant making foundations, the Foundation Center has tracked 173 private and community foundations that made at least one PRI of $10,000 or more in 2006 or 2007.

[44] All 28 entities listed under section 501 (c)(3) are subject to the prohibition of private inurement to the benefit of any particular individual or shareholder.

Their program related investments were $734 million, or a small portion of the $91.9 billion in overall charitable distributions provided by foundations during this two-year timeframe".

The insignificant usage of PRIs was caused in part by how little guidance was available on what could be considered a PRI and what falls outside the concept. The consequence of an investment not falling within the narrow concept of "furthering their exempt purpose" entails that this would inevitably make the investment subject to UBIT and corporate income tax on the profits earned, and wouldn't count for the five percent requirement (Schmidt, 2010). The alternative as to make sure the qualification is met consists of the use of PLR, but such instruments are time-consuming and expensive for an already financially constrained entity like a foundation. In order to increase the number and size of PRI investments and simultaneously provide a flexible social business form, the L3C was created. Notably at the time of its enactment a clear definition of PRI was missing.

The L3C is a variant of the LLC as a business form, it does provide the same advantages and characteristics, namely contractual flexibility for governance provisions, fully fledged limited liability, and the possibility to attract capital investments. Yet, unlike the LLC, the L3C is required to operate in accordance with Internal Revenue Service (IRS) in order to qualify them as PRIs. The intention was to add a business form that aims to finance via "tranched" or layered investments with different degrees of risks and rates of return. Additionally, the L3C articles of incorporation must contain the following mandatory provisions: (1) stating a charitable purpose, (2) confirmation that the entity does not have a significant purpose of income of appreciation of property; and (3) stating that the entity does not have a political or legislative nature. Most statutes require that an L3C must include the "L3C" in its name. Conversely, these provisions are available for the traditional LLC form, but as noted in the CIC analysis, "Branding" and "Signalling" are key components for mission-driven businesses.

Unlike its British older counterpart, the L3C has been under heavy criticism by practitioners, academics, foundations and the general public. Reason being that L3C does not ease or encourage PRIs due the ambiguous nature of PRIs[45]. The reason for this is that foundations still have to proceed with the same due diligence for non-charitable purposes while fulfilling its *five percent requirement.* To counter that, legislative initiatives such as the Program-Related Investment Promotion Act 2008 and the Philanthropic Facilitation Act of 2010 were drafted, however neither initiative has been introduced. Additionally, the L3C lacks of any mechanism to ensure security and investor confidence like the CIC's transparency, restrictions on dividends, asset lock, and community benefit requirements. Furthermore, in April 2012 the American Bar Association Business Law Section released a formal letter opposing legislation for L3Cs on behalf of its LLCs, Partnerships and Unincorporated Entities Committee and Non-profit Organizations Committee.

The letter points out that L3Cs aren't better nor offer anything novel over other entities able to receive PRI's. Nonetheless, the L3C misguided foundations that must, according to non-profit law, fulfil its requirement to further a charitable purpose. Moreover, they noted that "Using a program related investment as part of the type of tranched financing promoted by L3C advocates portends serious risk of improper "private benefit" – i.e., using charitable assets to the benefit of private interests such as for-profit investors. "Private benefit" transactions are improper for a private foundation and imperil a foundation's tax-exempt status. A private foundation cannot remain qualified as a tax-exempt charitable entity if the foundation has transgressed the private benefit doctrine (Kleinberger, 2012)". The critique escalated when North Carolina's Governor Pat McCrory signed into law a new LLC Act effective since the

[45] In the note over PRIs at the IRS website L3C are not part of the examples given, a foundation considering investing in this kind of companies must have to either obtain an opinion of counsel or they can ask for a private letter ruling from the IRS, which is a lot more time-consuming, expensive and risky.

first of January of last year, removing the L3C from the menu of business forms available (Field, 2011).

For social enterprise objectives, the value proposed in the L3C form is somehow uncertain. L3C statutes do not provide transparency, accountability, and mission enforcement or conflict resolution mechanisms to pursue, maintain and promote social ends (Carter, 2010). Nowadays passage of L3C legislation seems to be stagnated despite the fact that around 1142 (interSector Partners, L3C, 2015) L3C have been incorporated across the U.S., yet the L3C is not the best the U.S. possesses in its arsenal of emerging entities for social enterprises. During the next section we explore the Benefit Corporations that are often regarded as the finest social business form for mission-driven firms in the U.S.

4.3 The United States' Benefit Corporation

The terms B-corp, Benefit Corporation, B Corporation and Public Benefit Corporation are sometimes used interchangeably to refer to different concepts. There is a fundamental difference between *"B Corporations"* which is a certification provided by B lab, *Benefit Corporations* (B-Corps) which refers to entities formed under one of the many states' corporate law that enabled the use of the form, and *Public Benefit Corporations* (PBC) which denotes the unique approach to Benefit Corporations' legislation by Delaware. During this section the characteristics of and differences among these concepts will be explored.

The origin and history behind the benefit corporation is tied to the force behind the initiative, namely B lab. B lab is a non-profit organization headquartered in Wayne, Pennsylvania, founded in 2006, that provides "B corporation certification" for for-profit organizations around the world. The certification is granted to a corporation that obtains a positive[46] "B Impact assessment[47]" review, submits the required documentation and adopts B lab's amendments in their bylaws together with the payment of a certification fee. After the process is complete, B lab certifies the company as a "B Corporation" subjected to B Lab's private regulatory regime that includes randomly selected on-site reviews and the preparation of annual public interest reports that serve to evaluate the progress in reaching the company's goals. Due to its private nature, certified *B Corporations* do not offer any legal benefits nor provide any right of action to hold the directors accountable when they deviate from their mission. Dana Brakman Reiser (2010) notes the certification for "B Corporation form realistically offers only moral, rather than legal, assurances to non-shareholders constituencies and social interests."

B Lab's ambition to "awake the corporate conscience" (Jay Coen Gilbert - On better Businesses, 2010) did not stop in simply being a provider of certification for sustainable social and/or environmental business. At the beginning of 2008, California Assemblyman Mark Leno responds to their request and agrees to introduce AB2944 assembly bill as a proposal to create a constituency statute. Unfortunately, governor Schwarzenegger vetoes AB2944 due to intense opposition, and the stage for a business form is delayed. B Lab's policy efforts are back and visible when Philadelphia City Councilmember James Kenney said there would be a press release stating the introduction of legislation to create the nation's first Benefit Corporation. Thanks to Senator Jamie Raskin and Jim Epstein, finally, on October 1, 2010 Maryland became the first jurisdiction to add the new form within the United States. Its characteristics and requirements are explained in the next section.

---

[46] In order to obtain a positive B Impact Assessment a company must obtain a minimum score of 80 out of 200.

[47] The B Impact assessment measures the impact a business on all of its stakeholders, best practices regarding the pursuit of social and/or environmental mission, corporate governance and the company's specific "Impact Business Models", which include the targeted specific benefit pursued by the company (B-Lab, 2015).

4.3.1 Characteristics and Requirements of Benefit Corporations

There are some slight differences between states in the twenty-six that have implemented the form. Nevertheless, the main characteristics consistent from state to state are: (i) enhanced corporate purpose to create a "material positive impact on society and the environment", (ii) expanded fiduciary duties by creating a duty for directors to consider non-shareholders constituencies, and (iii) obligation to report the firm's performance in regard to its social and/or environmental goals as assessed by a comprehensive, credible, transparent and independent third-party standard. However, the model Act proposed by B Lab proposes more elements and considers certain provisions as fundamental for the benefit corporation. A comparison of the variations in the statutes' provisions in every state is illustrated in table 2.

Table 2: Variations in the Statutes

Provision	Statutes that include that provision	Note
The Benefit Director	Hawaii, Illinois, Louisiana, New Jersey, Massachusetts, Pennsylvania, South Carolina, and Vermont and the District of Columbia	All nine jurisdictions required benefit directors to include statements in the Annual Benefit Report.
Benefit Officers	Hawaii, Illinois, Louisiana, New Jersey, Massachusetts, Pennsylvania, South Carolina, and Vermont and the District of Columbia	Conspicuously, the same nine jurisdictions to include the benefit director include also the benefit officer.
The Benefit Enforcement Proceeding	California, Louisiana, Illinois, Massachusetts, New Jersey, Pennsylvania, South Carolina, Virginia, and Vermont and the District of Columbia	Statutes that exclude the especial benefit enforcement procedure expect reliance in their respective corporate codes.
Public Comment.	Hawaii	Notably, this provision is unique to the Hawaiian statute which requires benefit corporation to "post a draft its benefit report on the public section of its website, or make it otherwise available to the public, for a sixty-day public comment period." Haw. Rev. Stat. § 420D-11(b).
Forfeiture of Social Enterprise Corporate	New Jersey	In the event a benefit corporation fails to summit the Annual Benefit Report two consecutive years, the Department of the Treasury has the power to file a statement that the entity has forfeited its status. N.J. Stat. Ann. § 14A:18-11(d)(1)

In essence, the Model Legislation's fundamental parts are: (i) mandatory "general public benefit" proposal with the option to choose an additional "specific public benefit", (ii)

adoption or winding up of the benefit corporation upon an affirmative vote of at least two-thirds of the corporation's shareholders, (iii) mandatory use of a third-party standard, (iv) mandatory consideration of stakeholders, (v) benefit enforcement procedure, and (vi) mandatory disclosure of an annual benefit report. An in-depth analysis of the main provisions is provided below.

Legal Structure. In a broad sense, Benefit Corporations are C-corps with enhanced governance mechanisms and requirements that protect, promote and allow the pursuit of public benefits and profit for its shareholders, as specified in the statute from the place of their incorporation.

Adoption of the Benefit Corporation. In order to become or convert into a benefit corporation, Shareholders owning at least two-thirds of the corporation's stock must approve such decision in accordance with section 105(a) of the Model legislation. Similarly, in order to abandon the status of Benefit Corporation, two-thirds must approve.

Legal Framework. The Model legislation states in section 101(c) that, unless it is provided otherwise, the state's business corporation law of the corporation's jurisdiction shall be generally applicable.

General Public Benefit (Enhanced Corporate Purpose). Benefit corporations are obligated to create "general public benefit", defined as "having a material positive impact on society and the environment"[48] and are allowed to choose a "specific public benefit,"[49] the Model Legislation provides a list of seven non-exhaustive possibilities for "specific public benefits,"[50] The rationale behind a broad definition of what is considered "*general public benefit*" is to prevent "greenwashing", the argument is that if the legislation only allows "*specific public benefits"* or another narrow construction, a firm would have the possibility to enjoy the benefits of the entity in terms of *"branding"* and *"signalling"* while performing poorly in other areas outside their narrow scope, which would defeat the purpose of the legislation, namely the creation of benefits for society as a whole.
There is no doubt that it is a trade-off by allowing narrow purposes and mandating the adoption of a broad purpose. On one hand, a broad definition allows the firm to be flexible without creating unnecessary prescriptive performance requirements (Clark, Jr & Babson, 2012). On the other hand, a broad approach undermines the meaning of the purpose by making it look too vague. In order to counter the drawback of a broad purpose, the figure of the third-party standard setter serves as a mechanism to assess the fulfilment of the benefit purposes, which together with the "annual benefit report" protects the social entity from misuse. Moreover, to have a defined prescribed performance would make the legislation less appealing for companies to adopt the form, due to the burdens accompanied by a cumbersome list of prescribed and prohibited activities that had to be specified in that case.

[48] Model Legislation § 201 (a)

[49] Model Legislation § 201 (b)

[50] The possibilities for specific public benefits include: (i) Providing low-income or underserved individuals or communities with beneficial products or services, (ii) promoting economic opportunity for individuals or communities beyond the creation of jobs in the ordinary course of business, (iii) preserving the environment, (iv) improving human health, (v) Promoting the arts, sciences, or advancement of knowledge, (vi) Increasing the flow of capital to entities with a public benefit purpose; and (vii) The accomplishment of any other particular benefit for society or the environment. Model Legislation § 102

Director's duties (Accountability). The directors of a benefit corporation, in considering the best interests of the corporation, shall consider the effects of their decisions upon seven different categories of stakeholders: (i) the shareholders, (ii) the employees of the benefit corporation, its subsidiaries and its suppliers, (iii) the interests of customers, (iv) community and society as a whole, (v) the local and global environment, (vi) the short-term and long-term interests of the benefit corporation, and (vii) the ability of the benefit corporation to pursue, accomplish and maintain its general benefit purpose and any specific public benefit purpose.[51]

Third-Party Standard (Transparency). A "third-party standard is defined as "a recognized standard for defining, reporting and assessing overall corporate social and environmental performance." It is meant to be comprehensive, assessing the overall effect of the operations of the company with regard to the interests listed in section 301 (a) and performed by an organization that must be independent from the benefit corporation and satisfies the following requirements: (i) *Credibility*, it is developed by an entity that has the access to necessary expertise to assess overall corporate social and environmental performance and uses a balanced multi-stakeholder approach to develop the standard, including a reasonable public comment period, (ii) *Transparency,* because the information about the standard, its development and the review of compliance is publicly available, including the criteria used to measure overall social and environmental performance, the relative weightings, the identity of the members of the organizations, the process to review the standard and an accounting of the revenue and sources of financial support of the entity.

The model legislation does not mandate a particular third-party standard setter, nor does any statute. There is a vast menu of third-party standard setters available such as: The Global Reporting Initiative (GRI), GreenSeal, Underwriters Laboratories (UL), ISO2600, Green America and others. Remarkably, B Lab and GRI offer their reporting and assessment tools for free. A usual critique is that these organizations are not required to obtain prior accreditation by a national or international standard body such as the American National Standards Institute (ANSI). The justification for this omission is made upon the grounds that it would create costs for a government regulatory body and become a significant burden for standard developers, who, given the early stage of development in this area, would not be able to comply, decreasing the available third-party standard options for benefit corporations and probably leading to a monopoly-like situation. This paper addresses this in the following chapter, arguing that such accreditation might in fact be beneficial to avoid greenwashing and enhance the credibility of the benefit corporations.

Dissenters' rights (Minority Shareholder's Protection). The model legislation and most statutes work in a complementary manner with the existing corporate statutory framework of the corporation's place of incorporation. Thus, in states where dissenters' rights are granted, the same rights would be enjoyed by the shareholders of the benefit corporation.

Annual Benefit Report (Transparency). The annual benefit report must be delivered to the shareholders and made available to the general public. The report must be filed with the department of state. This report includes a narrative description of the measures taken to pursue the general public benefit by the corporation and, if applicable, the measures taken in pursuit of specific public benefit as articulated in the corporation's bylaws. In the unfortunate case that unforeseen circumstances hinder the corporation's ability to achieve its social purpose, such circumstances must be reported. Additionally, the corporation must respond for its social and/or environmental performance in relation to its chosen third-party standard. The salaries

[51] Model Legislation § 301(a)(1)

of the directors must be made public; the model legislation requires that, as part of the management, the corporations must name a *benefit director*[52] whose main task in relation to the annual benefit report is to make an "annual compliance statement" confirming that the corporation has acted in accordance to its social and environmental purpose. The benefit director must assess if the other directors have performed their obligations considering the various stakeholders interests in relation to the corporation. Annual benefit reports are not required to be certified or audited by the third-party standard setter or any governmental or private body.

Scope of Director's Liability (Accountability). Notably, the Model Legislation excludes the director, officer and corporate liability from monetary damages. The idea behind this was to eliminate concerns about personal liability in the face of a lack of court precedent to dictate how to quantify it, and to ensure that courts place more emphasis on requiring the benefit corporations to comply with the commitments that it voluntary undertook. Despite the duty to consider the seven different stakeholders constituencies, directors are protected from suits by beneficiaries of the corporation's general public benefit. The Model Legislation section 301(d) states that third parties will not have a right of action because there rests no fiduciary duty on anyone who cannot bring a "benefit enforcement proceeding".

Benefit Enforcement Proceeding (Enforcement). The right of action provided by the Model act as stated before, it is a right enjoyed only by shareholders, directors, investors in the parent company and others specified in the bylaws in accordance with section 305(a). The benefit enforcement procedure may only be brought in case of a failure to pursue or to create the general and/or specific public benefit purpose established in the corporation's bylaws.

Benefit Corporation legislation as conceived in the Model legislation is very flexible without an absolute lack of credibility like the L3C, yet not as credible as UK's CIC. At this point there is a glimpse about why benefit corporations and L3C's are deemed ambiguous, namely the unavoidable trade-off of granting flexibility for the entity form at expense of credibility. The next section reviews the Delaware approach to benefit corporations, the Public Benefit Corporation.

4.3.2 Public Benefit Corporation, the Delaware's approach

On July 17, 2013, Jack Markell, Delaware's Governor, signed the Public Benefit Corporation (PBC) legislation which is part of the DGCL since August first, 2013 (DELAWARE GOV, 2013). Delaware presented its own version of benefit corporation law, while most other states follow the Model Legislation. It is no surprise that after Delaware's slightly different approach appeared, other states such as Colorado followed its lead. After all, when Delaware speaks, other states listen (Murray, 2014). Fifty-five PBCs were incorporated or converted in Delaware during the first three months of its enactment. Alicia E. Plerhoples (2014) reported in her analysis of the first three months of PBC law that "74% of public benefit corporations were new corporations in early stages of operation; 31% of public benefit corporations provide professional services; the technology and education sectors each represent 11% of public benefit corporations; 10% of public benefit corporations produce consumer retail

[52] Only few states have include the mandatory provision requiring the designation of a benefit director among them Hawaii, Illinois, Louisiana, New Jersey, Massachusetts, Pennsylvania, South Carolina, and Vermont. Notably those same states allow the selection of a benefit officer, who is in essence an independent director charged with the task of the benefit corporation in relation to the creation of its general and/or specific public benefits.

products; 9% are engaged in the healthcare sector; 35% of public benefit corporations could have alternatively incorporated as a charitable non-profit exempt from federal income tax".

For B Lab, Delaware's adoption of the corporate form represented a well-deserved win after eighteen months of lobbying and negotiating. However, it could be considered a partial win due to the slight but nonetheless significant changes of the Delaware approach in comparison to the Model Legislation proposed by B lab. The main characteristics of PBCs and differences with the Model Legislation are explained below.

Legal Structure. Similarly to benefit corporations, a PBC is, in essence, a standard C-corp with unique features, such as: enhanced corporate purpose, transparency mechanisms and accountability to pursuit social and environmental goals.

Adoption or Conversion into a PBC. Converting or adopting the PBC form requires an approval of ninety percent of the outstanding shares of each class of voting and non-voting stock of the converting corporation in accordance with DGCL. tit. 8, section 363(a). Notably, unlike the model, the voting requirement is significantly higher. In addition, after converting or incorporating as a PBC, it is required to include the words "public benefit corporation" or "P.B.C." in the chartered name, in order to notify that the entity is not a traditional corporation. This requirement is missing in many of the states' legislations and in the Model legislation at its conception. Needless to say this caused a significant burden to track entities that adopted the form across the country.

General and Specific Public benefits (Enhanced Corporate Purpose). Delaware's PBCs are required to choose a specific public benefit purpose or purpose in addition to the standard general public benefit purpose. DGCL. tit. 8, section 365(a). The rationale for this mandatory "specific public benefit" purpose is to provide more directorial guidance than the broad general public benefit. Under the DGCL. tit 8. Section 362(b) , a public benefit consists of a "positive effect(or reduction of negative effects) on 1 or more categories of persons, entities, communities or interests (other than stockholders in their capacities as stockholders) including, but not limited to, effects of an artistic, charitable, cultural, economic, educational, environmental, literary, medical, religious, scientific or technological nature." Remarkably the wording is similar to IRC's Section 170 (c)(2)(B) definition of charity.

Director's Duties (Accountability). PBCs' directors possess significantly greater accountability than the directors of a standard C-corp, whose primary duty is to act in the best interest of the corporation and its stockholders. Their duties are contained in a three-part balancing test in DGCL. tit.8 section 365, stating that "the board of directors shall manage or direct the business and affairs of the public benefit corporation in a manner that balances[53] the pecuniary interests of the stockholders, the best interests of those materially affected by the corporation's conduct, and the specific public benefit or public benefits identified in its certificate of incorporation." Another difference with regards to the corporation's management is that Delaware PBC legislation does not provide or even mention the concepts of benefit director or benefit officer.

Derivative Suits (Enforcement). Unlike the Model legislation that prescribes a unique benefit enforcement proceeding, section 367 of the DGCL. tit. 8 allows for PBC stockholders owning, individually or collectively, two percent of outstanding shares, or if traded on a

[53] It is often argued by academics and commentators alike that the word "balance" has a more onerous impact than "consider".

national securities exchange, the lesser of $2 million or two percent of the shares, to maintain a derivative suit against the board to enforce the directors' duties under Section 365.

Periodic Statements (Transparency). PBCs' boards of directors are required to at least biennially report their progress in the promotion of the public benefit. If the progress is insufficient, the corporation's stockholders will have several options, including removal and replacement of directors. In the situation in which stockholders brought a derivative suit, the court would probably defer to the business judgement of the board. The most probable outcome is that courts would use the same or similar breach-of-duty standards that they use in evaluating a breach of duty by the board of a traditional corporation. Moreover, unlike the Model legislation that specifies a list of requirements for the report and mandates to make such a report publicly available, Delaware's PBC legislation provides the main elements of these biennial statements: "The statement shall include (i) The objectives the board of directors has established to promote such public benefit or public benefits and interests, (ii) the standards the board of directors has adopted to measure the corporation's progress in promoting such public benefit or public benefits and interests, (iii) objective factual information based on those standards regarding the corporation's success in meeting the objectives for promoting such public benefit or public benefits and interests, and (iv) An assessment of the corporation's success in meeting the objectives and promoting such public benefit or public benefits and interests."

Scope of Director's Liability (Accountability). PBC legislation limits derivative suits to stockholders, in addition the statute in DGCL. tit. 8 section 365, expressly denies a director's duty to "any person on account of any interest of such person in the public benefit or public benefits identified in the certificate of incorporation or on account of any interest materially affected by the corporation's conduct and, with respect to a decision implicating the balance requirement … …will be deemed to satisfy such director's fiduciary duties to stockholders and the corporation if such director's decision is both informed and disinterested and not such that no person of ordinary, sound judgment would approve."

Conspicuously, the Delaware PBC does not require or mention the use of third-party standards in defining, assessing and reporting the operations of the company, proving that the corporations have been actively pursuing their public benefit goals. With regards to the excluding elements, it is the intention of the Delaware PBC statute to simply provide corporations the option to include these heightened requirements for the report in their certificates of incorporation or bylaws. Table 3 summarizes the main differences among both legislations as illustrated below.

Table 3: Table 3: Model Legislation / Public Benefit Corporation

Provision	PBC	Model Legislation
Adoption /Termination	90% of the shareholders / Two-thirds of shareholders §362.	Two-thirds of shareholders §105.
Benefit Report to Shareholders	Benefit report to shareholders biennially § 366(b).	Benefit report to shareholders annually § 402(a).
Benefit report public	Benefit report is optional § 366(c)(2).	Benefit report required to be made public § 402(b).

Specific Public benefit	Required to state specific public benefit § 362(a)(1).	Specific public benefit not required, optional § 201(b).
Benefit director	Benefit director not even mentioned in the statute.	Benefit director required for publicly traded companies § 302.
Enforcement Proceeding	Derivative suit.	Benefit enforcement proceeding § 305(a).
Director's Liability	Monetary liability for failure to balance stakeholders' interests permitted, but duty satisfied if director informed, disinterested, and rationally acts in best interest of corporation §365.	Monetary liability for failure to balance stakeholders' interests permitted, but duty satisfied if director informed, disinterested, and rationally acts in best interest of corporation § 301(e).

It is worth mentioning that there are other, rather new business forms, the FPC and SPC; however, these two newer forms are only available in one or two jurisdictions and are subject to tougher criticism. This chapter reviewed the main provisions of the most important hybrid business forms for social enterprising in the U.S. and U.K. The next chapter will illustrate the current picture that reflects the adoption of these forms in order to compare both jurisdictions simultaneously, identifying trends and preferences of social businesses. In addition, it will provide the main criticisms of these forms that might explain reasons to opt not to utilize them. And finally a conclusion will be presented.

CHAPTER V

5.1 The Social Hybrid Business Forms Landscape

Evidently, due to the relative freshness of the social enterprise movement and the short period of time since the enactment of most social enterprise forms in the U.S., available data and evidence of the performance, numbers, trends, industry niches and financing is limited to a few studies or has not even been the object of academic research yet. In addition, unintentionally the first statutes passed did not include any mandatory provision for newly created benefit corporations to include the denomination "Benefit Corporation" on their names, making the task of tracking these entities laborious. In contrast, data from U.K. social enterprises is easily obtainable due to the maturity of the CIC and the special institutional framework developed for CICs. Such data is available thanks to the Regulator of Community Interest Companies, who provides updated reports quarterly. Nonetheless, during this section the adoption is reviewed of the new forms across the U.S. and U.K. per state and in-aggregate prior to the overview of the major criticisms made against these new forms.

5.1.1 United States' Social Hybrid Business Forms Landscape

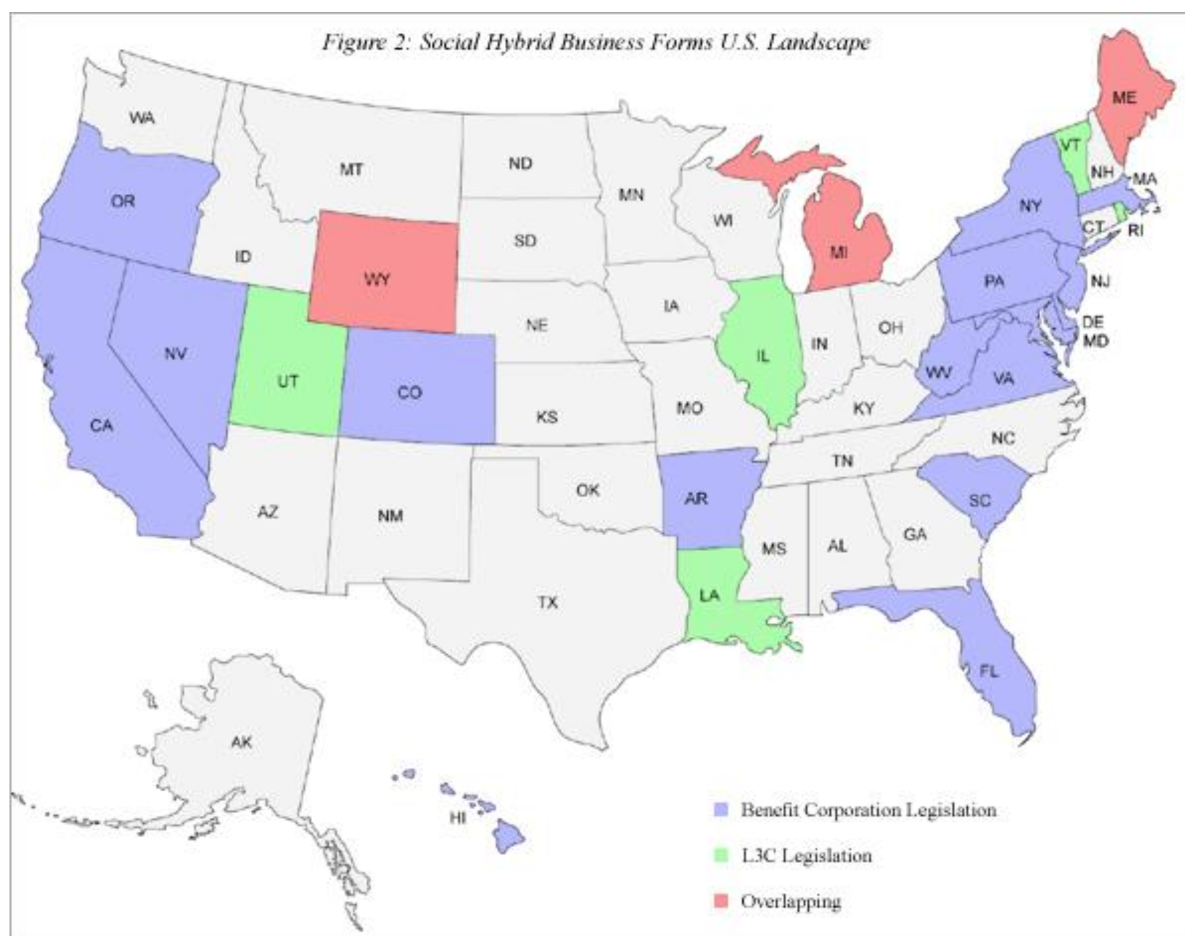
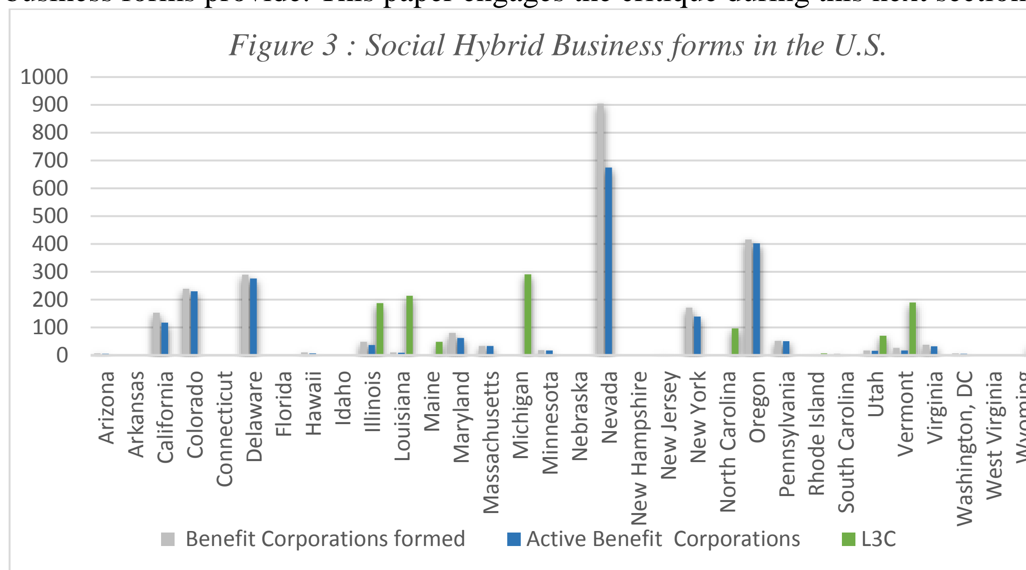


Figure 2: Social Hybrid Business Forms U.S. Landscape

Until now, 28 states have included the benefit corporation legislation following two trends: the Model Legislation and Delaware's PBC. In the case of L3C statutes, legislative efforts remain stagnant and even slightly regress in recent years with North Carolina being the first state to drop the form. Figure 2 illustrates the choice of entity form per state, regardless of the differences between both entities there is little overlap: only in four states, Vermont, Illinois, Louisiana and Rhode Island, both are present. According to B Lab, at this moment there are another fourteen states considering the addition of the benefit corporation to their corporate law framework. Ellen Berrey (2015) has engaged in the difficult task of gathering data from B Lab and the Secretary of State to report that from the 2541 benefit corporations across the state only 2144 are active as of April 2015. In Figure 3, the distribution of these entities across the U.S. can be appreciated. As stated before, in comparison to the sea of companies registered in the U.S., the number might be trivial. Moreover, despite the fact that the benefit corporation builds upon C-corps, there are no examples of publicly traded benefit corporations yet. Needless to say, the vote requirement makes it difficult or almost impossible for publicly traded companies to convert into the form.

Benefit Corporations' underlying goals sound very attractive to the public as a concept that challenges the strict dichotomy between for-profit and non-profit. Public opinion has been generally positive despite the accidental misuse of denominations by the media, misnaming B-corps as B-certified Corporations and Benefit Corporations alike. Well-known examples of Benefit Corporations are Patagonia, Plum Organics, The Big Bad Wolf, Ello, Greyston Bakery and others. Remarkeable examples of B-certified Corporations are Etsy, Warby Parker, Ben & Jerry's, Unilever, and many others. The difference, as explained in the last chapter, consists of

the choice of a different legal entity and the difficulty of leaving the status. Their goals are relatively the same. Therefore, this leaves the question of the degree of real value that the new hybrid business forms provide. This paper engages the critique during this next section.



Source: Berrey, E. (2015). *How Many Benefit Corporations Are There?* And interSector Partners, L3C.

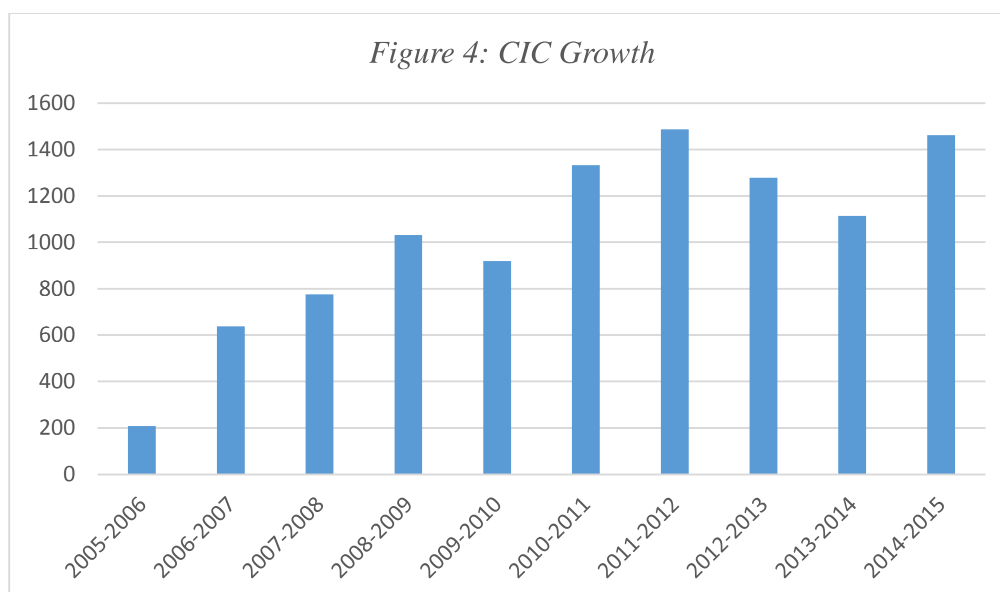
5.1.2 United Kingdom Social Hybrid Business Forms Landscape

In the U.K., the effectiveness of the CIC has gradually grown and the strictness of its provisions have decreased over the years. One fundamental problem CICs had since their conception was the lack of a recognizable brand, and unawareness of the existence of the entity. In addition, since its conception, the stringent mandatory provisions make them unattractive for investors. It is not surprising that as of December 2014, 78% of the CICs in the public register were limited by guarantee and only 22% were limited by shares. Since its enactment, the major amendments made to the entity are in relation to the dividend and performance interest caps, as explained before. Notably, the caps have been adjusted in 2010, 2013 and 2014 which are the years that presented higher growth of adoption in comparison to previous years, as illustrated in table 4 and figure 4.

Table 4: CIC adoption, termination and conversion

Year	Approved	Dissolved	Converted To a Charity	Growth
2005-2006	208	0	0	208
2006-2007	637	0	0	637
2007-2008	814	35	3	776
2008-2009	1120	86	2	1032
2009-2010	1296	372	5	919
2010-2011	1824	484	7	1332
2011-2012	2087	590	11	1486
2012-2013	2055	765	11	1279
2013-2014	1831	709	8	1114
2014-2015	2569	1104	3	1462
Total	**15104**	**4411**	**53**	**10639**

Source: The Office of the Regulator of Community Interest Companies, Operational Report, Fourth Quarter 2014-2015



Source: The Office of the Regulator of Community Interest Companies, Operational Report, Fourth Quarter 2014-2015

5.2 Benefits of using Social Hybrid Business Forms

There is a myriad of benefits linked to the adoption of a Social Hybrid Business Form. The benefits could be easily classified into five categories: (i) ability to legally protect the corporate mission, (ii) branding benefits, (ii) investor desirability, (iii) attracting and retaining talent and (v) legal certainty carrying the mission. The adoption of a legal entity provides more credibility for the firm's commitment towards social and/or environmental goals than certification schemes because unlike the latter, the firm is legally obligated to operate in a sustainable and conscientious manner. Moreover, when a corporation decides to be subject of a certification such as B Lab's certification, the firm suffers no severe consequences from leaving the status or failing to comply with the requirements of the third-party certification scheme over time. Moreover, Social Hybrid Business Forms based upon well-structured legislation provide a clear and transparent picture of the corporation that may result in a competitive advantage.

As stated in chapter 2, a significant portion of consumers believe that corporations must do more than just meet their profit-driven bottom lines, they should consider the ways in which they could become part of the solution to modern social and environmental issues. After the financial crisis there has been, to a great extent, a lack of trust by costumers in companies worldwide. Being certified or legally a social business can help solve this trust issue, effectively enhancing the firm's economic moat. Additionally, as stated before, an increasing number of impact investors are willing to increase their stake in community/impact investments (B Lab, 2015). Additionally, talent retention and recruitment might considerably improve because employees would be more attracted to obtaining a purposeful job in a firm where the directors have a legal duty to consider public benefit while managing the company.

According to a recent report from Net Impact (2012), accounting for a statistically-significant national sample of 1,726 individuals, including enrolled university students about to enter the workforce and currently-employed college graduates covering three generations in the U.S., one of the major considerations while seeking to join the labor market is the existence of a link between the position and their personal values. Moreover, a sense of purpose has proven to lead to job satisfaction, the report showed that individuals who are able to contribute to a direct social and/or environmental purpose through their position were significantly more satisfied with their position than those who did not by a 2:1 ratio. Recent generations have

shown to be more socially and environmental aware than previous generations since 1960. In addition, research has revealed significant evidence showing that firms with high levels of employee engagement (65%) recorded higher returns for their shareholders (20%) in comparison with firms where employee engagement was 45% or less.

The most significant benefit is the legal certainty that the mission shall be pursued and protected as the company grows, more investors or new management are brought in, or even when there is a succession in corporate management or investors. In this regard, a social corporation that has recently caught the attention of the media is Ello. Also known as the anti-Facebook, Ello is an ad-free social network which, after 23 of October 2014, converted into a Delaware PBC to protect its corporate purpose, integrating in its charter the following provisions: (i) Ello must never make money from selling ads, (ii) Ello must never make money from selling user data, and (iii) In the event that Ello is ever sold, the new owners would also have to comply with these terms (Ello, 2014). These provisions make it significantly difficult or almost impossible for investors to require Ello to ever show ads, sell user data, or sell the company to any buyer who would violate any of the listed conditions. Moreover, Ello just completed a Series A round of funding for the amount of $5.5 million, led by Foundry Group, Techstars' Bullet Time Ventures, and FreshTracks Capital. Seth Levine, managing director at Foundry Group, stated: “We're committed to their manifesto and are in this for the long haul.", similarly Mark Solon, managing partner at Techstars, said: "We believe in the mission and the PBC further enforces the manifesto, and Ello's vision to never market their users to third parties."

Nevertheless, it is often claimed that most benefits related to adopting a social legal entity are also available for certification schemes with the exception of legal protections. A prime example can be found in Etsy’s recent Initial Public Offering (IPO) past 16 of April, 2013. Etsy is an online martketplace for handmade and vintage goods, founded in 2005 by a carpenter looking to sell wooden computers (Picker, 2015). The company adopted B Lab’s certification in 2012, obtaining a score of 105 out of 200 on its standards as of late 2013 (Cole, 2015). It is the largest B-Certified Corporation to go through the process of an IPO with revenues of $195.6 million in 2014, its gross merchandise sales have increased roughly 16 percent every quarter since 2008 and many experts agree that the company has the potential to grow even further (Etsy, Inc., 2014). The Company sought to list on the NASDAQ planning to sell 16.6 million shares, priced at $14-$16 under the denomination NASDAQ:ETSY. The IPO priced at $16 a share, the high end of its expected range, meaning that Etsy raised almost $267 million. The following Thursday after the IPO, the shares traded as high as $35.74 before dropping back close to $32. Etsy plans to donate $300,000 of the proceeds from the IPO to its foundation Etsy.org, a non-profit for educating women and under-represented groups on how to build business. Etsy’s IPO serve as positive evidence that firms with social and environmental commitments operating with a long-term sustainable model are well received by the stock market.

These examples demonstrate the difficulties in validating the unnecessary agreement. On one hand, for business purposes, certification schemes serve as an efficient signal to display the quality of the business. On the other hand, if the company would be in a similar position as *Ford or Craigslist,* the outcome would be uncertain. In order to value the benefits, the next section offers an overview of the main criticisms of these hybrid forms.

5.3 Criticism to Social Hybrid Business Forms

Academics, commentators, investors and entrepreneurs have expressed their concerns about the new entities in the form of critiques on all fronts, from the degree of sustainability that hybrid entities have to the uncertain public market valuation for these kinds of firms, and

even challenge the legal certainty of these "untested" forms. While the former two should be subject to distinctive studies, the latter is the nucleus of this paper. One of the early criticisms consisted of the claim that the existence of these forms replaces one dichotomy, namely non-profit/for-profit with another, good/bad companies, having a spill-over detrimental effect on the whole ecosystem. Arguably, this has been proven wrong if one looks at the almost 10 years of CIC's existence, the major criticisms received regarding this entity were about the interest and dividend caps, and not any reputational negative effect on the rest of the British companies. Nonetheless, the most significant critiques have been made towards U.S. forms with regard to specific elements deemed insufficient.

As stated before, there is a trade-off: flexibility at expense of credibility. UK's CIC is regarded as a very restrictive form which, in comparison to PBC law or Benefit Corporation Legislation, scrutinizes every single aspect of the corporation, ensuring that the entity performs as claimed. Some critics state that the U.S. forms have the potential of greenwashing due to the great flexibility accompanied by uncertainty that the corporation will pursue its social purposes. Below is presented an in-depth analysis of the main criticisms, exposing the differences between the entities' provisions[54] that might explain any reasons to doubt the effectiveness of these forms.

Vague corporate purpose. A well-defined corporate purpose in the corporate charter serves to signal and guide the market about the social nature of the firm. The Model Legislation's broad corporate purpose is deemed vague and undefined; despite the fact that the "Community Interest Test" proposes a similar definition of company's purpose, the CIC possesses a vast array of mechanisms designed to protect the social interest and assets of the company. The Regulator makes sure the Community Interest Test is sustained by the company during its whole existence. Alternatively, a narrow construction would undermine the credibility of the entity with regards to the general well-being. Arguably, Delaware's PBC approach is optimal because it obligates the adoption of both general and specific public benefit, in order to ensure the corporation doesn't deviate from its social purposes and provides greater managerial guidance than the Model Legislation.

Inefficient Accountability mechanisms. First, with regards to third-party standards in the Model Legislation, the main critique is that neither the Government nor the third party standard setters have any enforcement power or even guidance (Callison, 2012). On one hand, unlike CICs that are overseen by the Regulator, U.S. entities are free to choose the most appropriate third-party standard based on their measuring techniques, their reputation and the industry-specific expertise they apply on their assessment. On the other hand, to be free to choose leads to the possibility of the appearance of third-party standard setters with low, easily attainable standards allowing greenwashing, hurting the credibility of the movement as a whole.

Second, in the case of PBC law, Delaware's exclusion of the third-party standard as a mandatory provision, relying on the stockholders as main defenders of the social purpose, hurts the "branding" objective of the form; under the rationale that if the shareholders and stakeholders interest are in conflict, the stockholders would have poor incentives to challenge any decision that benefits them in detriment of the other constituencies.

Third, even when the Model Legislation at first sight seems to be slightly superior to PBC law in providing branding through the mandatory "credible", "independent",

[54] Notably with regards to the L3C the statutes provide so little guidance and great flexibility that the whole critic applies to them, despite the fact that its major problem is the ambiguous nature of the PRIs.

"comprehensive" and "transparent" third-party standard, those requirements are not easily enforceable and do not seem to provide the creation of a consistent credible brand.

Lack of guidance for reporting. The Model Legislation provides a list of requirements for the report that are not mandated by PBC law. Yet none provide sufficient guidance on the manner of reporting the contents of the annual/biennial benefit report. The categories required in the Model Legislation in which the report must be presented are vague, allowing significant puffery (Callison, 2012). PBC law certainly expects the firm to develop best practices of reporting public benefits by not mandating any strict requirements. Moreover, a large part of the few annual benefit reports available are self-promotional and do not provide enough information for the reader seeking to obtain a full evaluation of the business' social and/or environmental practices.

Uncertainty about Director's duties. First, with regards to PBC and the Model Legislation there is no hierarchy or prioritization of the interest that directors are required to "consider" or "balance" (Emerson, 2013). Keeping into account the novelty of the entities, some managerial guidance could be beneficial, especially when the interest of the different constituencies of the firm conflict. Notably, the director's duties as provided in the Model Legislation do not differ from the British concept of ESV which governs the manner in which directors of ordinary companies operate their firms, clearly showing that "balance" might be more appropriate for sustainable long-term socially imbued business models.

Second, there is the underlying question of how the courts will hold directors accountable. PBC law expressively states in DGCL, tit.8 section 365(b) that directors will not be liable if a decision is "both informed and disinterested and not such than no person of ordinary, sound judgment would approve." Especially in the context of Mergers and Acquisitions (M&A), directors may use this freedom to easily sell-out through a sale, arguing that the decision balanced the firm's constituencies. In the traditional for profit context, M&A could have disciplinary consequences for directors, but in the social context, directors have no boundaries or responsibilities to choose a particular bid as long as the decision was made through balancing the various stakeholders. Under the PBC and Model Legislation, directors enjoy robust protections against unhappy shareholders that sue when directors take a lower financial bid. As pointed out by Callison (2012), "irresponsible directors might justify their actions (including self-interested actions) by pointing to some public benefit justification (or alternatively when public benefit is involved, to some private shareholder benefit justification). Managerial accountability has proven difficult in for-profit enterprises, and it is difficult to conceptualize accountability in a hybrid entity with broad general public purposes and narrow private purposes."

Ambiguous Enforcement procedure. Unlike the CIC that allows shareholders and stakeholders to present a claim to the Regulator, both the Model Legislation and PBC law only confer standing to the stockholders to bring a claim under the benefit enforcement procedure or a derivative suit accordingly. Callison notes (2012) that even if the stockholders are interested in the public benefit or the company gives other constituencies standing to bring a claim, the statutes foreclose the possibility of monetary liability for failure to create or pursue its social goals. There is no doubt that fear of frivolous litigation is the main reason for the lack of monetary damages; however, the lack of monetary liability slightly reduces the incentives for plaintiffs to act, and directors have less reason to fear the proceedings which inevitable reduces the public confidence in these procedures as effective enforcement or brand creating

mechanisms. Nevertheless, fear of punishment is not the only reason to obey the law,[55] yet the lack of any consequences for directors managing these firms might produce negative effects on the credibility of the firm's social ends.

The main critique on the enforcement procedures claims that such procedure allows shareholders and directors the right of action upon failure to adequately pursue a general public benefit, empowering them to litigate whenever any portion of the company is unhappy with its direction. This results in a significant reduction of the efficiency of the corporate boards, enabling open-ended shareholder litigation, always justified. This phenomenon is referred to as greenmail.

The most significant critique made by opponents of these entities is that existing law is adequate to conduct social enterprising. As stated earlier in this paper, it relates to the *unnecessary argument.* Shown during this paper have been the dangers of pursuing stakeholders' interest, the inefficacy of for-profit entities to protect the corporate purpose in the U.S., the inadequacy of non-profits crippled by the limits on their commercial activity in both jurisdictions and the benefits obtained by operating a sustainable socially responsible business. At this point it would not be justified to deem these new forms *unnecessary*, yet in their current form they are evidently suboptimal. The next section will provide a brief summary of elements that might lead to the correct formula.

5.4 How to Improve Social Hybrid Business Forms?

It is evident that, despite the significant differences among entities, jurisdiction and approach, every legislation's underlying goal is to provide an entity capable of having (i) [protections for the] enhanced corporate purpose, (ii) accountability mechanisms, (iii) transparent reporting, (iv) expansion of the director's fiduciary duties, (v) a recognizable brand, (vi) expansion of the director's duties; and (vii) an enforcement procedure. The success of these forms depends to a great extent on the effectiveness of their provisions. It is prime to address the areas covered by the statutes that provide either insufficient guidance or are subpar for social enterprising. As Joseph A. McCahery and Erik P.M. Vermeulen pointed out (2006) "from an efficiency standpoint, the business parties would always prefer to use a legal organizational form that defines and sets forth the ownership structure and provides important contractual provisions in advance."

At this point, the differences between the U.S. entities and the U.K. CIC are evident. In a broad sense, U.S. entities need to improve some provisions to enhance their credibility and the CIC might benefit from allowing more flexibility. As a general remark on U.S. forms, one of the greatest issues is the lack of legitimacy in the manner that social business performance is evaluated. L3Cs lack any mechanism to prove their social and/or environmental performance; to a certain extent this is evident because similarly to the LLC, the form is meant to be the entity of choice of micro, small and few medium businesses, and the costs associated with reporting, assessment and corporate tax are undesirable for these type of firms. Nonetheless, third-party standards for Benefit Corporations should be regulated or accredited. Regardless of B Lab's argument concerning the perils of obligating third-party standard setters to be scrutinized, the only way to ensure the legitimacy, transparency and above all cohesion among the different third-party standards is through accreditation by a national or international

[55] Former Chancellor of the Delaware Court of Chancery William Allen has written, in the duty of care context, that "there is some virtue to the judicial articulation of non-enforceable standards of conduct" since "most human beings place value on thinking of themselves as moral actors who live up to societal expectations." (Allen, Jacobs, & Strine Jr., 2002)

standard body such as ANSI. This paper suggests a brief list of recommendations to improve the effectiveness of each form as explained below.

U.K. CIC. The British approach has proved to be very efficient in protecting the social and environmental goals of the firm, the creation of a credible and reliable brand armed with a vast array of mechanisms to avoid greenwashing or greenmail. It is the opinion of this author that the dividend and performance interest caps should be greatly reduced, allowing greater dividend distribution. There is no doubt that all the asset-lock provisions ensure the protection of CIC assets, yet evidence proves that the CIC fails to attract investors and to fully enable socially oriented business to make use of the full potential of mission-driven business models. Only 22% of the CICs formed limited by shares, it is clear that CICs are not attractive investments. As long as the figure of the Regulator retains the same level of involvement, there would be little risk for community interest assets.

L3C. It is the opinion of this author that this entity does not really propose anything different than the traditional LLC. Nonetheless, the only manner in which the effectiveness of this entity could be enhanced is through the introduction of the two statutes mentioned in section 4.2. Still, in terms of protection of the mission and branding there is little to no value in the use of this form.

PBC and Benefit Corporation. There is no doubt that the entity that is the closest to the right balance of flexibility and credibility is Delaware's Public Benefit Corporation. However, in terms of branding it could benefit from requiring a third-party standard, provided that these third-party standards become more credible and convergent in their practices and criteria of assessment. Additionally, both entities could benefit from providing more specific requirements for reporting, such as percentage of revenue donated to charities or foundations, hours per employee donated to charities, recycling per employee, percentage of employees paid a living wage, amount of goods given in buy-one-donate one business, etc. Even when the costs of reporting might be significant for some social enterprises, if these reports are mandatory, the data should be verifiable and organized in specific categories so the readers obtain a clear picture of the entity's operation and are able to compare different entities, understanding the progression of social impact in a specific industry over time.

Additionally, this author agrees with the majority of academics that the PBCs and Benefit Corporations would greatly benefit if they included a partial "asset lock mechanism" similar to the CIC to ensure that firms do not gain value by conducting business socially and then selling making profit in detriment of society's well-being. Moreover, with regards to enforcement proceedings, a slight involvement of the third-party standard setter in the form of an opinion would prevent greenmail and unnecessary conflicts arising from disagreements about the direction of the business specifically related to the pursuit of the social and/or environmental mission.

To conclude, this paper recognizes the high degree of difficulty in finding the right formula to achieve the balance between credibility and flexibility while addressing *ex ante* conflicts that might appear while conducting long-term sustainable business using any of these forms. The following chapter presents the answer to research questions in the form of a general conclusion.

CHAPTER VI

6.1 Conclusion, Not Necessary but Complementary

During this paper, the controversial and novel topic was engaged of the degree of necessity of hybrid business forms for social enterprises as part of the current corporate law framework. A clear non-refutable answer is, to a certain extent, not available. Under their current form, their effectiveness is uncertain. On one hand, for U.S. mission-driven businesses operating under traditional business forms with a certification scheme, the new entities provide the same or similar competitive advantages as the certification schemes in terms of branding and signalling that the firm is operated under a long-term business model with high regard to social and environmental issues. On the other hand, as shown in *Dodge v. Ford Co.* and *eBay Domestic Holdings, Inc. v. Newmark, et al.,* there is somehow little legal protection for the philanthropic, social or environmental corporate goals when other constituencies' interests of the firm give rise to conflicts, without the legal protection granted by the new hybrid forms.

The main rationale behind the creation of these forms in the U.S. is to provide legal certainty, legitimacy and protection to the social, philanthropic and/or environmental corporate purpose. In addition, their creation stems from the insufficient options found in non-profit and for-profit organizational entities of the traditional paradigm, as illustrated during early chapters of this paper. Moreover, the new entities are meant for those social entrepreneurs seeking to make their financially sustainable endeavours outside the constrained tax-exempt donation non-profit organizational model or the shareholder-centric for-profit organizational model. Whether a legal duty to create shareholder value exists or not is irrelevant for their existence. It is evident that as a practical matter, most ordinary companies are managed under the rationale of *shareholder's wealth-maximization*. Two decisive events are yet to appear: First, the court's interpretation of the mission-driven corporate purpose with regards to other constituencies of a firm that chose the certification scheme over the legal form. And second, the court enforcement of the provisions from the new statutes allowing the creation of these forms. If such situations ever arrive, their outcome would greatly determine the new legal entities' fate, and prove their real value.

For U.K. mission driven businesses born under a significantly different rationale, the main challenge consist of proving that CICs are capable of becoming appealing enough for investors seeking community/impact opportunities. The main rationale behind the form's creation is to address the needs of the British social enterprise and avoid unnecessary complicated structures combining charities and trading companies. Nonetheless, the higher degree of effectiveness of the CIC in relation to its American counterparts stems from the well-developed institutional framework to accommodate CICs. The figure of the Regulator effectively oversees, protects and legitimises the social purpose and assets, ensuring a constant stream of benefits to the community. Yet, even a robust and mature social enterprise framework like that of the British could benefit from comparing and adjusting its policies and regulations to provide the desired flexibility that promotes the development and growth of social enterprises.

Social Hybrid Business Forms are not strictly essential for every form of social enterprising. Nonetheless, they are extremely attractive for those firms that seek to generate both extra-ordinary returns for society and acceptable returns for its owners and investors. Their main problem remains the trade-off of credibility and flexibility, upon the discovery of the perfect balance and the correct formula, these forms have the potential not only to address the needs of the social sector but to even cause a paradigm shift in corporate law.

Bibliography

Allen, W. T., Jacobs, J. B., & Strine Jr., L. E. (2002). *Realigning the Standard of Review of Director Due Care with Delaware Public Policy: A Critique of Van Gorkom and its Progeny as a Standard of Review Problem.* Northwestern University Law Review, Vol. 96, P. 449, 2002 .

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

Ashoka. (n.d.). *Ashoka Innovators for the Public*. Retrieved April 24, 2015, from What is a Social Entreprenneur: https://www.ashoka.org/social_entrepreneur

Bainbridge, S. (2011, Januari 01). *The Business Judgement Rule is NOT a Standard of Review.* Retrieved from ProfessorBainbridge.com: http://www.professorbainbridge.com/professorbainbridgecom/2011/01/this-is-the-sort-of-arrant-nonsense-about-the-business-judgment-rule-up-with-which-i-will-not-put.html

Bainbridge, S. M. (1993). In Defense of the Shareholder Wealth Maximization Norm: A Reply to Professor Green. *Washington & Lee Law Review*.

Berrey, E. (2015). *How Many Benefit Corporations Are There.* University at Buffalo, SUNY.

B-Lab. (2015). *Attract Investors, Certified B Corporation.* Retrieved June 10, 2015, from B corporation: http://www.bcorporation.net/become-a-b-corp/why-become-a-b-corp/attract-investors

B-Lab. (2015, June 07). *B Impact Assessment Demo*. Retrieved from B Impact Assessment: http://b-lab.force.com/bcorp/impactassessmentdemo?id=a03C000000ISEBSIA5

Brakman Reiser, D. (2009). For-Profit Philanthropy. *Fordham Law Review, Volume 77, Issue 5*.

Brakman Reiser, D. (2010). Governing and Financing Blended Enterprise. *Symposium on the Law of Philanthropy in the Twenty-First Century, Part I,Volume 85, Issue 2*.

Bratton, W. W., & Watcher, M. L. (2008). Shareholder Primacy's Corporatist Origins: Adolf Berle and 'The Modern Corporation'. *Journal of Corporation Law, Vol. 34*, 99.

C.F. Mueller Co. v. Comm'r, 190 F.2d 120 (3d Cir. 1951).

Callison, W. J. (2012). *Putting New Sheets on a Procrustean Bed: How Benefit Corporations Adress Fiduciary Duties, the Dangers Created and Suggestions for Change.* American Univ. Journal of Law & Business.

Carter , B. (2010). The Low-Profit LLC (L3C); Program Related Investments by Proxy of Perversion? *Arkansas Law Review*, 243.

Choudhury, B. (2009). Serving Two Masters: Incorporating Social Responsibility into the Corporate Paradigm. *Pennsylvania Journal of Business Law, Vol. 11*, 631.

Clark, Jr, W. H., & Babson, E. K. (2012). How Benefit Corporations are Redefining the Purpose of Business Corporations. *William Mitchel Law Review*, p817.

Clark, W. H., Vranka, L., LLP, D. B., & LLC, C. G. (2013). *The need and rationale for the Benefit Corporation: Why it is the legal form that best adresses the needs of social entrepreneurs, investors, and, ultimately, the public?*

Clemente, M. (2013). *Benefit Corporations: Novelty, Niche, or Revolution.* Retrieved from http://dx.doi.org/10.2139/ssrn.2359226

Cole, M. (2015, April 15). *Etsy IPO: Everything You Need to Know*. Retrieved June 11, 2015, from The Fiscal Times, Business+Economy: http://www.thefiscaltimes.com/2015/04/15/Etsy-IPO-Everything-You-Need-Know

Commission, E. (2015). *Social enterprises - European Commission*. Retrieved from Ec.europa.eu: http://ec.europa.eu/growth/smes/promoting-entrepreneurship/we-work-for/social-economy/enterprises/index_en.htm

Community Interest Company Regulations . (2005).

CONE. (2013). *2013 CONE Communications/Echo Global CSR Study.*

Defoumy, J., & Nyssens, M. (2008). *Social Enterprise in Europe: Recent Trends and Developments.* Social Enterprise Journal 202.

Defourny, J. (2001). *Introduction: From Third Sector to Social Enterprise.* Routledge.

Defourny, J., & Nyssens, M. (2012). *The EMES Approach of Social Enterprise in a Comparative Perspective.* EMES European Research Network, Working Paper no.12/03.

DELAWARE GOV. (2013). Governor Markell Signs Public Benefit Corporation Legistalion. *NEWS.DELAWARE.GOV*.

Dodge v. Ford Co., N.W. 668 (Mich. 1919).

Doeringer, M. F. (2010). *Fostering Social Enterprises: A Historical and International Analysis.* DUKE J. COMP. & INT'L L.

Easterbrook, F. H., & Fischel, D. R. (1996). *The Economic Structure of Corporate Law.* Harvard University Press.

eBay Domestic Holdings, Inc v. Newmark, et al., C.A. No. 3705-CC (Del. Ch. 2010).

eco offciency. (2015, april 1). *Benefits of Becoming a Sustainable Business.* Retrieved april 1, 2015, from eco offciency: www.eco-officiency.com/benefits_becoming_sustainable_business.html

Ello. (2014). *Ello Charter Letter signed by its investors.* Retrieved May 23, 2015, from https://ello.co/downloads/ello-pbc.pdf

Emerson, C. (2013). *Delaware's Public Benefit Corporations: Comparative Analysis and Fiduciary Duties.* Widener University School of Law.

Esposito, R. T. (2013). The Social Enterprise Revolution in Corporate Law: A Primer on Emerging Corporate Entities in Europe and the United States and the Case for the Benefit Corporation. *William & Mary Business Law Review 639* .

Etsy, Inc. (2014). *Form S1 Registration Statement under the Securities Act of 1933.* Retrieved April 27, 2015, from http://www.sec.gov/Archives/edgar/data/1370637/000119312515077045/d806992ds1.htm

Field, A. (2011, Jan 11). *North Carolina Officially Abolishes The L3C*. Retrieved June 05, 2015, from Forbes / Entrepreneurs: http://www.forbes.com/sites/annefield/2014/01/11/north-carolina-officially-abolishes-the-l3c/

Find a Benefit Corp. (2015, April 21). Retrieved from Benefit Corp Information Center: http://benefitcorp.net/find-a-benefit-corp

Friedman, M. (1970). The Social Responsibility of Business is to Increase its Profits. *The New York Times Magazine*. Retrieved May 25, 2015, from http://www-rohan.sdsu.edu/faculty/dunnweb/rprnts.friedman.dunn.pdf

Geczy, C., Stambaugh, R. F., & Levin , D. (2005). *Investing in Socially Responsible Mutual Funds.* Retrieved from http://papers.ssrn.com/sol3/papers.cfm?abstract_id=416380

Gergen, D. (2006, February 20). The New engines of Reform. *U.S. NEWS & WORLD REPORT*, p. 48.

Global Sustainable Investment Association (GSIA). (2014). *2014 Global Sustainable Investment Association (GSIA).* GSIA.

Google. (2004). *2004 Founders' IPO Letter.*

GOV.UK. (2014, October 01). *New Dividend and performance related interest caps now in place.* Retrieved June 06, 2015, from Office of the Regulator of Community Interest Companies: https://www.gov.uk/government/news/new-dividend-and-performance-related-interest-caps-now-in-place

GOV.UK. (2015). *Charities and Tax*. Retrieved Mach 18, 2015, from GOV.UK: https://www.gov.uk/charities-and-tax/tax-reliefs

GOV.UK. (2015). *Statistics at Companies House*. Retrieved from Companies House: https://www.gov.uk/government/organisations/companies-house/about/statistics

Haskell Murray, J. (2012). Choose Yout Own Master: Social Enterprise, Certifications and Benefit Corporation Statutes. *American University Business Law Review*. Retrieved from http://ssrn.com/abstract=2085000

Heal, G. (2004). *Corporate Social Responsibility: An Economic and Financial Framework.* Columbia Business School - Finance and Economics; National Bureau of Economic Research (NBER).

interSector Partners, L3C. (2015, March). *What is you Bottom Line?* Retrieved June 01, 2015, from interSector Partners, L3C: http://www.intersectorl3c.com/l3c_tally.html

IRS. (2015, Februari 28). *TEB Private Letter Rulings: Some Basic Concepts*. Retrieved from IRS: http://www.irs.gov/Tax-Exempt-Bonds/TEB-Private-Letter-Ruling:-Some-Basic-Concepts

Katz, R. A., & Page , A. (2010). The Role of Social Enterprise. *Vermont Law Review*, 59.

Kelley, T. (2009). *Law and Choice of Entity on the Social Enterprise Frontier.* University of North Carolina (UNC) at Chapel Hill - School of Law.

Kelly, M. (2009). Not just for Profit. *54 Strategy+Business*.

Kerlin, J. A. (2006). *Social Enterprise in the United States and Europe: Understanding and Learning from the Differences.* International Society for Third-Sector Research and The Johns Hopkins University.

Keyser v. Commonwealth National Financial Corp., 675 F. Supp. 238 (M.D. Pa. 1987).

Kleinberger, D. S. (2012). *ABA Business Law Section, on Behalf of its Committees on LLCs and Nonprofit Organizations, Opposes Legislation for Low Profit Limited Liability Companies (L3Cs).* William Mitchell Legal Studies Research Paper No. 2012-05.

Lane, M. J. (2012). *Social Enterprise: Empowering Mission Driven Entrepreneurs.* American Bar Association.

Lawrence , S. (2010). Doing Good with Foundation Assets: An Updated Look at Program Related Investments. *The PRI Directory xviii-xiv*. Retrieved June 05, 2015, from http://foundationcenter.org/gainknowledge/research/pdf/pri_directory_excerpt.pdf

Lawrence, M. E. (1992). A Theoretical and Practical Framework for Enforcing Corporate Constituency Statues. *Texas Law Review Vol 70, Number 3*. Retrieved April 15, 2015, from http://scholarlycommons.law.case.edu/cgi/viewcontent.cgi?article=1382&context=faculty_publications

LII. (2015, May 23). *Enhanced Scrutiny Test.* Retrieved from Cornell University Law School: https://www.law.cornell.edu/wex/enhanced_scrutiny_test

Lipin, S. (2000). *Firms Incorporated in Delaware are Valued More by Investors.* Wall Street Journal.

Lloyd, S. (2010). *Transcript: Creating the CIC.* Vermont Law Review, Volume 35, Number 1, Fall 2010.

Lovett, T. G., & Basel, V. R. (n.d.). *The Role of the Constituency Statute in the Shareholders' World.* Dealmaker Counsel. Retrieved June 02, 2015, from http://www.lindquist.com/files/Publication/2bb272e5-b42e-4eb6-8cf7-2126afda88a4/Presentation/PublicationAttachment/5663ba4c-4258-428e-82fc-23f7ae3f612d/The%20Role%20of%20the%20Constituency%20Statute%20in%20the%20Shareholders%27%20World.pdf

Lynn, S. (n.d.). *Why We Should Stop Teaching Dodge v. Ford.* UCLA School of Law, Law-Econ Research Paper No. 07-11. Retrieved from http://papers.ssrn.com/sol3/papers.cfm?abstract_id=1013744

Macey, J. (2008). A Close Read of an Excellent Commentary on Dodge v. Ford. *VA. L. & BUS. REV. 177*, 190.

Martin, R. L., & Osberg, S. (2007). *Social Entrepreneurship.* Standford Social Innovation Review.

McCahery, J. A., & Vermeulen, E. P. (2006). *Corporate Governance and Innovation – Venture Capital, Joint Ventures, and Family Businesses.* ECGI - Law Working Paper No. 65/2006.

Million, D. (2010). *Enlightened Shareholder Value, Social Responsibility, and the Redefinition of Corporate Purpose without Law.* Washington: Washington & Lee Public Legal Studies Research Paper Series.

Millon, D. (2010). *Enlightened Shareholder Value, Social Responsibility, and the Redefinition of Corporate Pupose without Law.* Wahington & Lee Public Legal Studies Research Paper Series.

Mitchell, L. E. (1995). *Progressive corporate law.* Boulder: Westview Press.

Murray, H. J. (2014). Social Enterprise Innovation: Delaware's Public Benefit Corporation Law. *4 Harvard Business Law Review 345*.

Net Impact. (2012). *Talent Report: What Workers Want in 2012.* Retrieved June 10, 2015, from https://netimpact.org/sites/default/files/documents/what-workers-want-2012-summary.pdf

NMI. (2013). *U.S. Consumer Perspectives and Trends in Sustainability.* Natural Market Institute.

Norked, N. (2012, May 13). *Benefit Corporations vs. "Regular" Corporations: A Harmful Dichotomy.* Retrieved from Harvard Law School Forum on Corporate Governance and Financial Regulation: http://corpgov.law.harvard.edu/2012/05/13/benefit-corporations-vs-regular-corporations-a-harmful-dichotomy/

OECD [Organization for Economic cooperation and Development]. (1998). *Social Enterprises in OECD countries.* Paris: OECD.

Office of the Regulator of Community Interest Companies. (2012). *Information and guidance notes, Chapter 2: Preliminary Considerations.*

Office of the Regulator of Community Interest Companies. (2013). *Information and Guidance Notes, Chapter 4: Creating a Community Interest Company.*

Office of the Regulator of Community Interest Companies. (2013). *Information and guidance notes: Chapter 10, Transfer of Assets and ceasing to be a CIC.*

Office of the Regulator of Community Interest Companies. (2013). *Information and guidance notes: Chapter 11: The Regulator.*

Office of the Regulator of Community Interest Companies. (2013). *Information and Guidance Notes: Chapter 8 Statutory Obligations.*

Office of the Regulator of Community Interest Companies. (2014). *Information and Guidance notes: Chapter 6 The Asset Lock.*

Office of the Regulator of Community Interest Companies. (2015). *Community Interest Compannies Registered in April 2015.* Office of the Regulator of Community Interest Companies.

Orman v. Cullman, 794 A.2d 5, 20 (Del. Ch. 2002).

Picker, L. (2015, April 15). *Etsy Surges in Debut After Craft Marketplace's $267 Million IPO*. Retrieved June 10, 2015, from BloombergBusiness: http://www.bloomberg.com/news/articles/2015-04-15/etsy-said-to-raise-267-million-pricing-ipo-at-top-of-range

Plerhoples, A. E. (2014). *Delaware Public Benefit Corporations 90 Days Out: Who's Opting In?* Georgetown Law Faculty Publications and Other Works, Paper 1342.

Porter, M. (1980). *Competitive Strategy.* New York: NY:Free Press.

Praszkier, R., & Nowak, A. (2011). *Social Entrepreneurship: Theory and Practice.* Cambridge University Press.

Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.22 173 (Del. 1986).

Salamon, L. (1993). *The Marketization of Welfare: Changing nonprofit and for profit roles in the American Welfare state.* Social Service Review.

Schmidt, E. (2010). *Vermont's Social Hybrid Pioneers: Early Observations and Questions to Ponder.* Vermont Law School Legal Studies Research Paper Series Research Paper No. 10-53.

Schwab Foundation. (n.d.). *About us*. Retrieved April 18, 2015, from Schwab Foundation for Social Entrepreneurship: http://www.schwabfound.org/content/about-us

Scripture Press Found. v United States, 152 Ct. Cl. 463,468 (1961).

Smiddy, L. O. (2010). Corporate Creativity: The Vermont L3C & Other Developments in Social Entrepreneurship. *Vermont Law Review, volume 35*, 3-12.

Smith v. Van Gorkom, 488 A.2d 858,872 (Del. 1985).

Sneirson, J. F. (2009). Green is Good: Sustainability, Profitability, and a New Paradigm for Corporate Governance. *Iowa L.aw Review 987*, 1001-1007.

Sneirson, J. F. (2011). *Shareholder Primacy: An Intellectual History from Dodge v. Ford through the Rise of Financialism* .

Taylor, C. R. (2009). Carpe Crisis: Capitalizing on the Breakdown of Capitalism to Consider the Creation of Social Business. *New York School Law Review*, 743.

TEDx Talks. (2010, December 01). Jay Coen Gilbert - On better Businesses. Philadelphia. Retrieved December 28, 2014, from https://www.youtube.com/watch?v=mGnz-w9p5FU

The Economist. (2009). *Triple Bottom Line: It consist of Three Ps: Profit, Planet and People.* Retrieved Februari 15, 2015, from http://www.economist.com/node/14301663

Unocal Corp. v. Mesa Petroleum, 493 A.2d 946 (Del. 1985).

Warren, I. H., & Aronstam, B. R. (2007). *Delaware's Business Judgment Rule and Varying Standards of Judicial Review for Assessing Director Conduct in M&A Transactions.*

Weinberger v. UOP, Inc., 457 A2s 701 (Del. 1983).

Wenben Lai, A. (1995). *Consumer Values, Product Benefits and Consumer Value: A Consumption Behavior Approach.* Retrieved April 18, 2015, from Association for Consumer Research: http://www.acrwebsite.org/search/view-conference-proceedings.aspx?Id=7772

Yahoo! Finance. (2013, October 23). *Ello Becomes A Public Benefit Corporation And Legally Vows To Forever Remain Ad-Free; Founders And Investors Sign Charterr.* Retrieved May 23, 2015, from Yahoo! Finance: http://finance.yahoo.com/news/ello-becomes-public-benefit-corporation-130000817.html

Yunus Centre. (n.d.). *Citation The Nobel Peace Price for 2006*. Retrieved April 15, 2015, from Yunus Centre: http://www.muhammadyunus.org/index.php/professor-yunus/nobel-peace-prize/citation

Zhao, J. (2011). Promoting more socially responsible corporations through UK company law after the 2008 financial crisis: turning of the crisis compass. *International Company and Commercial Law Review, 22 (9)*, 275-284.