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Mission Possible?: Funding and Accountability in Benefit Corporations

A Thesis submitted in partial satisfaction of the
requirements for the degree Master of Arts in
Global Studies

by

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June 2018

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ABSTRACT

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by

Michael Joseph Cianos

There exists only a handful of empirical studies on B Corps, and even fewer on benefit corporations, yet understanding how social entrepreneurs wield these forms is an important area to continue investigating considering their rapid adoption. Though often used interchangeably, the two terms refer to different things: the benefit corporation is a legal entity (akin to a C Corp, LLC, etc.) designed to institutionalize a multi-stakeholder approach to business and more rigid transparency requirements, and B Corps are companies that have been certified by B Lab—the nonprofit behind the whole movement—as meeting certain social and environmental standards. Benefit corporations only explicitly exist in the U.S. and Italy, however there have been significant efforts to pass legislation in Australia, Argentina, Canada, Chile, and Colombia. B Corps, on the other hand, have spread all around the world, and B Lab now has an Asian headquarters in Taiwan, an East African headquarters in Kenya, and a European headquarters in Amsterdam.

Both of these forms have arisen in response to the dominance of shareholder-value-driven capitalism, which was born in the U.S. but has since spread to many areas of the world by way of Washington Consensus-style economic reforms. Despite its prevalence, there is growing dissatisfaction with the model's inability to address non-commercial objectives. Previous efforts to reconstitute corporate models in order to serve multiple functions (e.g. CSR, ethical

certifications, triple bottom line approaches) have tended to run afoul of market pressures whereby competition in product, capital, and labor markets—coupled with the primacy of shareholder value—relegate the non-commercial functions to a secondary status. The benefit corporation and the B Corp were conceived as a direct response to these problems. This study asks *whether* and *how* they help provide committed social entrepreneurs the space they require to pursue their social goals (the wider problem of preventing strictly commercial companies masquerading as socially conscious businesses is beyond the scope of this project).

This research set out to explore the experiences of early adopters of the benefit corporation in order to understand how the legal form might impact a company “on the ground.” However, since many of this study’s participants were also B Corps, the findings that resulted have a great deal to do with B Corps, as well. The study consists of 12 semi-structured interviews with founders, CEOs, general counsels, and executives of benefit corporations over the course of 3 months. Interviews focused primarily on how being a benefit corporation impacts funding and how, if at all, it impacts a company’s day-to-day operations. Two primary hypotheses resulted, which both can be better understood by applying the economic notions of *signaling* and *screening*: (1) being a benefit corporation acts as a screening mechanism to help founders find better alignment with “traditional” investors and (2) being a benefit corporation does not significantly change behavior or encourage internal and horizontal accountability, but being a B Corp does. The latter hypothesis is strengthened by explaining how being a B Corp acts as a signal during the hiring process, and how combining it with a screen may make the development of a strong internal accountability mechanism more likely.

These findings have significant relevance for social entrepreneurs who are considering becoming either a benefit corporation or a B Corp (or both), as well as for legislators and investors.

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I. INTRODUCTION

This research set out to begin to answer the question: What are the non-legal impacts of a business's decision to either establish itself as, or convert itself to, a benefit corporation? Due to the relative novelty of the entity and the fact that it is, at its core, a legal creation, the vast majority of extant literature on the subject comes in the form of legal analysis. While such analyses are critical to our understanding of this new business form, corporations do not only exist on paper. They are real, culturally-unique entities, run by people, operating under different value systems, and interacting with the world around them. Legal analyses may be able to provide insight into the necessity (or lack thereof) of benefit corporation legislation, as well as its possible loopholes, likely lawsuits, and areas for improvement, but they do not tell us things like how investors perceive the form, why founders choose it, and how it might influence a company's operation.

Given that so little empirical research has focused on benefit corporations, the intention of this research was to start digging into some of these areas—areas that cannot be explained by analyzing statutes. It is *not* the intention of this study to provide a verdict on whether or not the “B” movement is capable of remaking the global corporate landscape in a more equitable and sustainable image. I do not intend to defend or reject the usefulness and philosophy behind benefit corporations or B Corps. This study was designed to explore the experiences of some prominent early adopters of the form and to develop some working hypotheses about what sorts of non-legal impacts adopting the form might have.

This study involved 12 semi-structured interviews with founders, general counsels, and executives of benefit corporations, which resulted in two key hypotheses: (1) being a

benefit corporation acts as a screening mechanism to help founders find better alignment with “traditional” investors and (2) being a benefit corporation does not change behavior or encourage internal accountability but being a B Corp does. A detailed distinction between a benefit corporation and a B Corp appears later in this chapter; however, briefly stated, the former is a legal entity (like a C Corp or an S Corp), and the latter is a company that has been certified by a nonprofit organization called B Lab.

This paper proceeds in the following way. Chapter I is broken down into four sections. The first two deal with defining benefit corporations and placing them in context. In the first, I discuss the history of corporate charters in the United States in order to demonstrate that benefit corporation legislation actually seeks to reinvigorate the original purpose of the corporation, namely to serve a critical social function. In the second, I describe the differences between the benefit corporation form and the B Corp, which is an important distinction to understand before moving forward. I then examine the existing literature on benefit corporations and discuss many of the disputes and oft-mentioned assumptions on which this study sought to shed empirical light. The final section of this chapter is a discussion of methods.

Chapters II and III are focused on the empirical findings of this study and building the case for the two hypotheses mentioned above. Chapter II introduces signaling and screening theory as a framework for understanding the fundraising experiences of many participants in this study and argues that being a benefit corporation can help social entrepreneurs find better alignment with more traditional investors—i.e. those who would not self-identify as “impact investors.” This chapter deals exclusively with benefit corporations. Chapter III switches focus to the issue of accountability and discusses this study’s findings in conjunction with a

prominent critique put forth by Briana Cummings regarding the inadequacy of benefit corporation and B Corp accountability mechanisms. In this chapter, I argue that being a benefit corporation does not significantly change behavior or encourage internal and horizontal accountability, but being a B Corp does, and it does so in many of the ways Cummings' suggests it should. Additionally, I show how these accountability mechanisms could be strengthened and made more likely by using the B Corp as a signal, and combining with a screen, to attract and retain more high-quality, mission-aligned employees.

To conclude, Chapter IV briefly summarizes the key contributions of this study, discusses its limitations, and makes suggestions on how future research might be able to build upon the core hypotheses around which this paper is focused.

A. Brief History of the U.S. Corporation and Corporate Responsibility

Two hundred and fifty years ago, the idea of a corporation existing to serve a public function would not sound so out of place. In 1790, for instance, if a business wanted to act as a corporation, it was required to petition its state legislature and make a case that it was going to serve a critical societal purpose—like building roads or providing water (Hiller 2013). The corporation's existence, therefore, was inextricably linked to its stated function and it was restricted from engaging in business activities that fell outside of its initial purview. Since charters were for a limited duration and were subject to periodic review and renewal, corporations could have their charters revoked if they failed to adequately perform their function (Speth 2012).

Charter revocation was not merely a rhetorical threat; in fact, it was commonly put into practice. As late as the 1850s, banks in Mississippi, Ohio, and Pennsylvania lost their

charters for “committing serious violations that were likely to leave them in an insolvent or financially unsound condition” (Derber 1998, 124; Banerjee 2008). Turnpike corporations in Massachusetts and New York had their charters revoked for “not keeping their roads in repair” (Derber 1998, 124; Banerjee 2008). Corporations that did not sufficiently provide their stated public good lost their incorporation status altogether. In fact, in 1815, the court in *Terret v. Taylor* declared: “A private corporation created by the legislature may lose its franchises by a misuser or nonuser of them...This is the common law of the land, and is a tacit condition annexed to the creation of every such corporation.”¹

However, the process of incorporation started to change in 1811, when rapid innovation began driving industrialization so quickly that state offices in New York became overrun with incorporation petitions. Unable to keep up with the sheer volume of requests, the state passed a general incorporation statute. This made incorporating a bit easier, but companies were still required to specifically state their purpose. Other states followed suit and this continued until Delaware and New Jersey took general incorporation statutes a step further (in 1896 and 1899, respectively) by essentially allowing any legal purpose to be sufficient for a company’s incorporation; by the end of the Civil War, “charters were available under any pretext, and almost impossible to revoke” (Carroll 2008, 22; Hiller 2013; Sprague 2010). The ease with which companies could now incorporate was arguably good for business, but “the more uniform incorporation and approval process weakened the corporate-society link” (Hiller 2013, 288).

¹ *Terret v. Taylor*, 13 U.S. (9 Cranch) 43 (1815).

Throughout this period of successive changes, the corporation shifted from being legally conceived of as a regulated public entity to one that was increasingly more private, eventually coming to enjoy many of the property rights afforded individual citizens. This shift was heavily influenced by the landmark decision of the US Supreme Court in *Trustees of Dartmouth College v. Woodward* in 1819, just four years after *Terret*, in which lawyers for Dartmouth Corporation argued that the rights of private corporations must be “protected from the rise and fall of popular parties and the fluctuations of political opinions” (Perrow 2002, 41; Banerjee 2008). The court agreed, thus significantly weakening “the common law principle of retention of sovereign power over state chartered corporations” and restricting legislatures from violating a corporation’s apparent right to property (Linzey 1995, 231).²

The significance of *Dartmouth v. Woodward* for the evolution of the corporation cannot be overstated. In addition to the changes discussed above, the decision established what became known as the “Dartmouth College doctrine,” which prohibited legislatures from revising or repealing charters once granted (Linzey 1995).³ This had long-lasting and far-reaching consequences, as Thomas Linzey summarizes:

No longer would the corporation created by the sovereign be subjected to arbitrary interference. The corporation, instead of being viewed as a functionary of the state, providing goods and services that the state could not, began to assume an existence of its own. This posed a great threat to the state’s control of corporate abuses, since the judiciary seemed willing to acquiesce to this autonomous existence and to reinforce this new “paradigm” under the rubric of contractual principles (Linzey 1995, 232).

² *Trustees of Dartmouth Coll. v. Woodward*, 17 U.S. 518 (1819).

³ *Trustees of Dartmouth Coll. v. Woodward*, 17 U.S. 518 (1819).

Though the *Dartmouth College* decision closed the door for legislatures to directly revoke or amend corporate charters, states did not readily submit to the new apparent hierarchy. In response, legislatures resorted to using *quo warranto* actions to correct corporate abuses, which they exercised quite regularly to varying degrees of success.

This was, unsurprisingly, a period of increasingly divergent economic and social motives: “While this system of property rights gave more power to corporations in a post-charter era, it also served as the primary incentive to maximize economic return for shareholders. Any reference to ‘social good’ was at best symbolic and derivative in that the economic function provided the social good” (Banerjee 2012, 57).

The ensuing decades saw the growth of large corporations and the corporate ruling class in the United States, who wielded considerable influence over virtually all facets of society, from the economy to the government. No longer tied down by strict charters or the threat of revocation, corporate leaders took advantage of their privileged position through the cultivation of monopolies and trusts, as well as by carving out a special privilege for themselves in the eyes of the law. Public purpose came to be defined so broadly that corporate privileges could almost always be justified in the name of “prosperity and growth; and in general for the freedom to externalize costs” (Perrow 2002, 45; Banerjee 2012).

Through a unique combination of legal personhood and their positioning within a society that was becoming increasingly obsessed with and prideful of its prosperity, corporations found themselves a license to make money in a whole host of new ways, all the while externalizing the costs. Consider an 1839 court decision in Kentucky on a petition by Louisville residents protesting a company’s decision to build a railroad through their neighborhood: “A railroad will be allowed to run its locomotives into the heart of Louisville

despite the noise and pollution from its smokestacks (the externality), because so necessary are the agents of transportation in a populous and prospering country that private injury and personal damage must be expected” (1839 Kentucky court decision, cited Perrow 2002).

Robert Hay and Ed Gray label this period as the “profit maximizing management” phase in the development of social responsibility, which lasted until roughly the time of the Great Depression. They argue that in the 1920s and 30s the relationship between business and society transitioned to one of “trusteeship management,” characterized by corporate managers striving to achieve a greater balance of profit and other stakeholder considerations, such as those of customers, employees, and the community (Hay and Gray 1974; Carroll 2008). According to Nicholas Eberstadt, it was around this time that social responsibility re-emerged as an expectation of the corporation, which was increasingly being viewed as an institution with societal obligations. He suggests that “business might never have turned back toward responsibility and accountability if the culmination of corporate irresponsibility had not been the collapse of the economic system” (Eberstadt 1973, 21-22).

Toward the middle of the twentieth century, discussions around the social responsibilities appeared to really be coming to the fore. Richard Appelbaum charts a period in the 1950’s in which several prominent business minds expounded on the obligations corporations have toward society. The most notable was the 1951 book *The New Society: The Anatomy of the Industrial Order* by Peter Drucker, who is considered by many to be the father of modern management. In it he argued that “corporations were not fundamentally driven by the profit motive but were instead political bureaucracies with responsibilities to their communities” (Appelbaum 2016, 34). Two years later, the economist Howard R. Bowen published *Social Responsibilities of the Businessman*, which opened with the two

questions that sit at the center of this discussion: “Are businessmen, by virtue of their strategic position and decision-making power, obligated to consider social consequences when making private decisions? If so, do they have social responsibilities that transcend obligations to owners or stockholders?” (Bowen 2013, 2). Appelbaum notes that his response to both was “short and simple”: yes (Appelbaum 2016, 34). Following on their heels, economist Carl Kaysen published an article coining the term “soulful corporation,” which perhaps more explicitly than his predecessors, reflected exactly what it is that benefit corporations seek to achieve today. Kaysen argued that the modern corporation no longer focused exclusively on profit maximization, but rather saw “itself as responsible to stockholders, employees, customers, the general public, and, perhaps most important, the firm itself as an institution” (Kaysen 1957, 313).

What Drucker, Bowen, and Kaysen were getting after was what has come to be called “managerial capitalism” (or managerialism) – a phase lasting until roughly the 1970s in which managers of public companies, “rather than seeing themselves as mere agents of shareholders, corporate directors and professional executives...viewed themselves as stewards of or trustees charged with guiding vital social and economic institutions in the interests of a wide range of beneficiaries” (Stout 2013, 1171; Dodd, Jr. 1932). But things changed drastically in the mid-1970s when, against the backdrop of the 1973-74 bear market, finance economists began calling into question the efficacy of managerial capitalism (Stout 2013). In 1976, Michael Jensen and William Meckling’s *Theory of the Firm*—“destined to become the most frequently cited paper in management literature”—expressed a deep concern with the separation of ownership and control that characterized managerialism, arguing that “the passivity of dispersed shareholders in public corporations as a serious

weakness that invited professional managers to neglect shareholders' interests in pursuit of their own, leading managers to shirk or even steal from the firm" (Stout 2013, 1173; Jensen and Meckling 1976). As Lynn Stout suggests—"Ideas can matter"; this one certainly did:

[T]he idea that shareholder powerlessness in public corporations was a serious problem turned out to be an idea that mattered quite a lot. In the decades following the publication of Jensen and Meckling's article, managerial capitalism fell into academic disrepute. It was replaced by a new business theory: the theory of "shareholder primacy." According to shareholder primacy theorists, the only legitimate purpose of the corporation was to maximize shareholder value. And the best way to secure this objective was to make managers more accountable to shareholders, for example by giving shareholders greater control over boards or by tying executive pay to share price (Stout 2013, 1173).

Stout details the story of shareholder primacy's ascent as an ideology, culminating in a series of "modest but collectively significant" changes in corporate law and practice in the 1990s and early 2000s, which had "the practical effect of driving directors and executives in public corporations to focus on share price as their guiding star" (Stout 2013, 1177).

Perhaps it is not coincidental that it was around this time that corporate bad behavior became the subject of widespread public contempt, when labor abuses in the global supply chains of major corporations like Nike and Gap took centerstage. While labor practices are now merely one branch of the tree, they were the seed from which today's brand of highly-visible corporate social responsibility (CSR) sprouted: "The emergence of firms that publicly express a commitment to behave in socially responsible ways is the direct result of

revelations about corporate abuses, worker strikes, and activist campaigns that began in the 1990s and continue to the present” (Appelbaum 2016, 36).

Now, here we are in 2018, having just recovered from another economic collapse rooted largely in corporate irresponsibility—the very culprit Eberstadt blamed for the Depression ninety years ago. Corporate social responsibility proclamations, convincing as they may be at times, have largely been shown not to carry much weight. Perhaps the problem is rooted in the reason why today’s brand of CSR arose in the first place—that is, “in large part to preserve brand value in the face of embarrassing revelations while avoiding government regulation” (Appelbaum 2016, 49). Its reason for being, in other words, was to limit outside intervention and preserve, to the maximum extent possible, the status quo—not to institutionalize some deeper transformation in the way corporate directors thought about the role of business in society. In light of its original purpose, its shortcomings should not be surprising.

While CSR is seemingly more visible now than at any other point in the post-*Dartmouth* corporate era, few would argue that the corporate-society link is as strong as it once was. Of course, returning to “the way things used to be” is not an inherently beneficial or desirable project. Nevertheless, it does seem like the weakening of this link has opened the door to short-term profit maximization and all its accompanying activities—corporate lobbying to the tune of billions of dollars annually; the norm of shareholder primacy; the Supreme Court’s decision in *Citizens United*—which are generally seen as responsible for, or at the very least enablers of, much of the corporate bad behavior witnessed today.

When we consider this whole story, corporate social responsibility and the benefit corporation’s attempt to embed it into the American firm emerge as merely the latest attempt

to *realign* incentives and *re-embed* the values upon which managerial capitalism operated. The benefit corporation is a response to the rise of a relatively recent and specifically U.S.-driven brand of shareholder capitalism, though what it seeks to achieve is not particularly new or novel. Its goal is to return the U.S. corporation to one that more closely resembles Kaysen's soulful corporation, which he saw as the status quo some fifty years ago.

B. The Benefit Corporation and the B Corp

In 2006, a nonprofit named B Lab set out to redefine what it meant to use “business as a force for good.” They began by developing the B Impact Assessment, a tool that could be used to rate companies across five categories: environment, workers, community, customers, and governance. The goal was to encourage companies to voluntarily take the assessment, pay a small fee relative to their size, and, if they scored high enough, obtain the “B Corp” certification. B Lab grew steadily over the next couple of years and in 2009—in large part due to an unplanned meeting between B Lab and Maryland State Senator, Jamie Raskin, at a party in Washington, D.C.—decided to expand its influence into corporate law. Within thirty days of that meeting, the first benefit corporation legislation was introduced, and just eight months later, eleven companies registered to be the first ever benefit corporations.⁴

At present, thirty-four states have passed benefit corporation legislation (albeit each one is slightly different) and six states are in the process of doing so. Benefit corporations are, in essence, modified versions of traditional corporations with three key differences: (1) they have an expanded purpose beyond maximizing shareholder value to *explicitly* include

⁴ B Lab. “Our History.” Bcorporation.net. www.bcorporation.net/what-are-b-corps/the-non-profit-behind-b-corps/our-history (accessed January 9, 2018).

general and specific public benefit; (2) they are required to consider/balance the impact of their decisions not only on shareholders but also on their stakeholders; and (3) they are required to make available to the public, except in Delaware, an annual benefit report that assesses their overall social and environmental performance against a third-party standard.⁵

The essential difference is that a “B Corp” is merely a business that has been certified by B Lab, while a benefit corporation is a legal entity form. B Lab, though, has always required companies to amend their articles prior to certification. A company had to incorporate B Lab’s Legal Framework language, which includes a “Purpose Clause” and a “Directors Clause”, in order to be eligible.⁶ These amendments required board approval and served to communicate throughout the organization the values and priorities that B Corps stand for. As new legal forms became available, however, B Lab started requiring that B Corps actually change their legal status, depending on what state they were registered in. Companies registered in states that have not passed benefit corporation legislation or something similar are not required to change their legal status but may have to make other changes. For example, companies in states that have “constituency statutes” must amend their articles using certain language, and companies in states with no “constituency statutes” must build certain language into their Term Sheets.⁷ Moving forward, as more states pass benefit corporation legislation, we can expect a much higher proportion of B Corps to be

⁵ B Lab. “FAQ.” Benefitcorp.net. www.benefitcorp.net/faq (accessed January 9, 2018).

⁶ B Lab. “Corporation Legal Roadmap.” Bcorporation.net. www.bcorporation.net/become-a-b-corp/how-to-become-a-b-corp/legal-roadmap/corporation-legal-roadmap (accessed January 9, 2018).

⁷ Rules vary significantly depending on the state that a company is registered in and when a company became a B Corp. For a full state-by-state breakdown of the legal requirements for B Corp certification, visit <https://www.bcorporation.net/become-a-b-corp/how-to-become-a-b-corp/legal-roadmap/corporation-legal-roadmap>.

benefit corporations. However, the reverse is *not* true; benefit corporations will (likely) never be required to become B Corps.

1. Benefit Corporations

The basis for benefit corporation legislation is what B Lab calls the “Model Legislation,” which is typically used as a sort of template and is adapted to fit the needs of each state.⁸ Generally, benefit corporation legislation departs from traditional corporation legislation in three fundamental areas: corporate purpose, accountability and transparency. Some states address these three categories slightly differently but detailed below are the aspects that are more or less constant.

With regard to corporate purpose, all benefit corporations are required to include in their articles of incorporation that they have the “purpose of creating general public benefit.”⁹ Optionally, businesses may include one or more “specific public benefits” that are to be pursued in addition to the general benefit. The Model Legislation defines general public benefit as “a material positive impact on society and the environment, taken as a whole, from the business and operations of a benefit corporation assessed taking into account the impacts of the benefit corporation as reported against a third-party standard.”¹⁰ Specific public benefit is a bit more intricately defined and, in the Model Legislation, includes:

⁸ The Model Legislation can be read in full by following the links located at <http://benefitcorp.net/attorneys/model-legislation>.

⁹ “Model Benefit Corporation Legislation,” § 201 (2017).

¹⁰ “Model Benefit Corporation Legislation,” § 201:97-100 (2017).

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

That a general benefit is required and is distinct from specific benefits is important.

Legislators wanted to “ensure a holistic assessment of the firm’s impact on stakeholders,” which meant that a company only committing to a specific benefit was not enough (Collins and Kahn 2016, 341). This would present obvious problems, as a company could feasibly be successful in achieving a specific benefit, while their conduct in other areas could make their net impact a harmful one. In other words, “you shouldn’t be able to dump toxic waste out the window but get a gold star because you built a school” (Collins and Kahn 2016, 341).¹¹

The essential value of the benefit corporation is allowing this purpose to persist and remain central to the business throughout its lifecycle. To this end, Vermont, for example, requires that a company’s “board of directors provide a statement of reasons why it is proposing a merger or sale in which the surviving corporation is not a benefit corporation”

¹¹ Citing personal communication with Elizabeth Babson on March 24, 2014.

(Esposito 2013, 698).¹² To further protect a benefit corporation's stated purpose, most states require a two-thirds vote in order to make any changes to such purpose, even if the company is to remain a social enterprise (Esposito 2013).

Benefit corporations are also intended to expand the duties of directors to include consideration of other stakeholder groups. In addition, of course, to their fiduciary duty to shareholders, they are to also consider the effects of any action or inaction upon:

- (1) The employees and work force of the benefit corporation, its subsidiaries, and its suppliers;
- (2) The interests of customers as beneficiaries of the general public benefit or a specific public benefit purpose of the benefit corporation;
- (3) Community and societal factors, including those of each community in which office or facilities of the benefit corporation, its subsidiaries, or its suppliers are located;
- (4) The local and global environment;
- (5) The short-term and long-term interests of the benefit corporation, including benefits that may accrue to the benefit corporation from its long-term plans and the possibility that these interests may be best served by the continued independence of the benefit corporation; and
- (6) The ability of the benefit corporation to accomplish its general public benefit purpose and any specific public benefit purpose.

Most benefit corporation statutes allow for directors to prioritize these considerations in any way that they would like, giving them a large degree of flexibility (Esposito 2013). This is

¹² *e.g.* VT. STAT. ANN. tit. 11A, § 21.06(a)(1) (2012).

where the second “pillar” of benefit corporation statutes, accountability, becomes particularly salient. While benefit corporations are permitted to grant specific stakeholder groups with a right of action, this is incredibly rare, and shareholders typically remain the only group that can truly hold directors accountable. If they choose to do so, the statutes allow for them—in most states—to bring what is termed a “benefit enforcement proceeding,” which is defined by the Model Legislation as “a claim, action, or proceeding for: (1) failure of a benefit corporation to pursue or create general public benefit or a specific public benefit purpose set forth in its articles; or (2) violation of an obligation, duty, or standard of conduct.”¹³ To date, a benefit enforcement proceeding has never been brought.

One of the most important features of benefit corporations is their commitment to transparency, which in most cases is achieved through the annual benefit report. All states require that an annual benefit report is distributed annually to shareholders, and some states require that the most recent report is made available on the company’s website. A company’s annual benefit report is designed to “assess its performance in creating general public benefit against a third-party standard” and is seen as a way to protect against the abuse of the benefit corporation status.¹⁴ In general, such reports are required to include, among other things, the ways in which a benefit corporation pursued its general public and specific benefits; the extent to which the benefits were realized; the process and rationale for selecting the third-party standard; and an assessment of the overall social and environmental performance of the firm.¹⁵ The third-party standard is designed to ensure that benefit corporations cannot simply determine their own reporting measures and that the standard-setters are indeed fully

¹³ “Model Benefit Corporation Legislation,” § 201: 86-92 (2017).

¹⁴ “Model Benefit Corporation Legislation,” § 102: 276-277 (2017).

¹⁵ “Model Benefit Corporation Legislation,” § 401: 1-6 (2017).

independent from the firm, but as we shall see later, many critics have raised concerns about this.

Aside from these three core areas of legislation, there are a couple state-to-state variations that are worthy of mention before moving on and which help to illustrate the different ways in which states adopt the Model Legislation. Several states, for example, require the appointment of a “benefit director” to sit on the board. Benefit directors are typically treated the same way as any other director and may be elected and removed in the same manner (Esposito 2013). Typically, the benefit director’s primary duty is to prepare the annual benefit report, which must include a statement from him or her addressing the corporation’s performance in achieving its stated purpose and maintaining its standards of conduct. Another example is the “public comment requirement,” only utilized in Hawaii, which requires the company to “post a draft of its benefit report on the public section of its website, or make it otherwise available to the public, for a sixty-day comment period” (Esposito 2013, 706).¹⁶ This gives external stakeholders the ability to have a say in each annual benefit report. These are, of course, not the only legal features relevant to benefit corporations, but they are arguably the most central. Other important features will be discussed in the literature review below.

It is worth noting that there has been a growing interest in the benefit corporation around the world, as well. In 2015, Italy passed benefit corporation legislation, and there has been significant interest in doing so in Australia, Argentina, Canada, Chile, and Colombia.¹⁷ The United Kingdom has a comparable entity called the Community Interest Company,

¹⁶ HAW. REV. STAT. § 420D-11(b)

¹⁷ B Lab. “International Legislation. Benefitcorp.net. www.benefitcorp.net/international-legislation (accessed January 13, 2018).

which is a for-profit entity designed for the same purpose but that differs from the benefit corporation in a few significant ways. For one, it is subject to an “asset lock” that caps dividends to shareholders and prevents the distribution of assets to directors, members, or equity holders in the event of dissolution (Esposito 2013). Community Interest Companies are also overseen by a CIC Regulator, who can intervene in a company in several non-trivial ways—including enforcing the community interest test, ordering audits, commencing civil proceedings, removing directors, and appointing a manager after directors have been removed (Esposito 2013). The creation of the CIC is no doubt a hallmark moment—it is the only new company structure introduced in the UK in the past 100 years.

2. B Corps in Detail

As mentioned earlier, B Corps are companies that wish to have an independent “seal of approval” for their social and environmental responsibility and, to that end, have been certified by a nonprofit called B Lab. According to their website, becoming a B Corp is a three-step process.¹⁸ Briefly, companies start by assessing their performance. This is a six-step process that starts with taking the “B Impact Assessment,” which includes over 200 questions across the categories of governance, workers, customers, community, and the environment. When taking the assessment, “customers” is not its own category, however questions are designed to generate a score for that area, as well. Table 1 gives some examples of questions given during the assessment. The assessment is, undoubtedly, the central feature of B Lab.

¹⁸ B Lab. “How to Become a B Corp.” Bcorporation.net. www.bcorporation.net/become-a-b-corp/how-to-become-a-b-corp (accessed January 13, 2018).

Companies are put on certain assessment “tracks” according to their firm profile; a large firm with 1,000+ employees and suppliers in 10 different countries will have a markedly different assessment than one with 25 employees with operations wholly contained in a single geographical area. This is important considering that firms are increasingly becoming global, and it is often when their operations are outsourced overseas and become less visible that many social harms manifest—human rights abuses, poor working conditions, etc. The B Impact Assessment does seek to measure a company’s commitment to eradicating this sort of behavior from its entire supply chain, and because of the increasing reliance on outsourced work, it is worth briefly discussing how it attempts to do so. This discussion will also help bring to the fore some of the ways in which the assessment might be improved.

A study published by Joanna Bauer and Elizabeth Umlas in September 2017 examined B Lab’s conception of, and subsequently the assessment’s measurement of, human rights concerns in light of the framework provided by the UN’s Business and Human Rights (BHR) movement. The researchers found several areas of assessment that they found helpful and reflective of issues on the broader business and human rights agenda. For example, Bauer and Umlas suggest that “[t]he precarious work and living wage metrics of the B Impact Assessment...could be considered cutting edge even when compared to the leading corporate sustainability reporting standard, the Global Reporting Initiative (GRI)” (Bauer and Umlas 2017, 299). The level of specificity in B Lab’s data requirements “responds to concerns of labor rights activists, across many sectors, from stable and long-term employment to precarious work” (Bauer and Umlas 2017, 299).

Additionally, under its Community section, B Lab “assesses the extent to which a company contributes to addressing social issues in the community, such as access to basic

services and capital” but does not, they found, “contain meaningful measures of negative impacts that BHR advocates would expect to see, such as information on land grabbing, forced displacement and violations of the right to housing and a clean environment or violence by police or private security companies in connection with the company’s operations” (Bauer and Umlas 2017, 300). However, they do still give attention to some areas that would be considered best practices by the BHR movement. They ask, for example, “What is the average tenure of your relationships with Significant Suppliers?”; “Is the payment of a fair wage (based on fair trade standard or local living standard) to workers for a majority of significant suppliers verified or certified?”; and “Has your company advocated for specific positive institutional, industry or regulatory reforms at local, state, national or international levels?” Such questions may not appear immediately relevant, but they connect to human rights concerns in meaningful ways. BHR advocates suggest that fewer and longer relationships are typically best in relation to workers’ human rights in global supply chains, and they also stress importance of responsible lobbying now that corporate pressure to weaken environmental and labor standards has become so strong (Bauer and Umlas 2017).

That being said, the assessment’s human rights shortcomings are clear. As Bauer and Umlas state, many of the questions are “tick-box” questions—i.e. “which of the following do you do?”—that don’t require further qualitative evidence or disclosure. Furthermore, the assessment tends to focus on policies and processes, not on actual impacts: “In reality, it must be noted, this standard falls short in practice, as conventional companies, with notable exceptions, report on policies and processes and rarely on negative incidents or impacts” (Bauer and Umlas 2017). The one section that does ask companies to disclose their negative impacts, the Disclosure Questionnaire, “is unweighted and thus does not affect the

certification determination” (Bauer and Umlas 2017, 303). However, B Lab does conduct background checks before certifying an entity, so they may, at least in theory, reject a company based on what they find.

Ultimately, Bauer and Umlas conclude that the certification process makes “little explicit reference” to human rights and that several key human rights indicators “are marginalized in the B Lab assessments,” though they do suggest that the seeds are present and that B Lab merely needs to expand on them (Bauer and Umlas 2017, 306). This does touch on another issue, though, to be taken up in the concluding chapter, which has to do with extent to which strong human rights and sustainability standards are achievable at scale within a highly competitive industry. It appears that B Lab would like its framework to be infinitely scalable, but it is not clear how compatible these two goals are. I will discuss this later, but now must return to detailing the certification process.

Following completion of the assessment, a company schedules an Assessment Review, during which they are asked to upload supporting documents for a number of their responses. They then complete the review, which may involve various back-and-forth steps of compiling and submitting additional documentation. The company must score at least an 80 out of a possible 200 points on the assessment review in order to be eligible for certification. After all of this, they submit a Disclosure Questionnaire, which allows them to confidentially disclose any sensitive information to B Lab. In some cases, this may warrant further transparency or the implementation of certain remedies prior to certification. To finalize the certification, B Lab conducts background checks on the company.

Table 1 *Sample B Impact Assessment Questions*

Category	Sample Questions
<p>Governance Evaluates a company’s accountability and transparency. Focuses on the company’s mission, stakeholder engagement, and overall transparency.</p>	<p><i>What portion of your management is evaluated in writing on their performance with regard to corporate social and environmental targets?</i></p> <p><i>Does the company have a formal process to share financial information (except salaries) with its full-time employees?</i></p>
<p>Community Assesses a company’s impact on its community. Focuses on areas like supplier relations, diversity, involvement in the local community, charitable giving, and nature of the product or service.</p>	<p><i>What percent of management is from underrepresented populations?</i></p> <p><i>Are full-time employees explicitly allowed any of the following paid or non-paid time-off hours options for community service?</i></p>
<p>Workers Assesses the company’s relationship with its workforce. Measures areas like compensation, benefits, training, ownership opportunities, and work environment.</p>	<p><i>Do you have a worker health and safety committee that helps monitor and advise on occupational health and safety programs (please choose N/A if the company does not use warehousing or manufacturing facilities)?</i></p> <p><i>What percent of the company is owned by full-time workers?</i></p>
<p>Environment Evaluates a company’s environmental performance through its facilities; materials, resource, and energy use; and emissions. It also considers a company’s supply chain and whether its products or services address environmental issues.</p>	<p><i>What percent of energy used is from renewable on-site energy production for corporate facilities?</i></p> <p><i>Does your company monitor and record its universal waste production?</i></p>

Once all of the performance requirements are met, the company must oblige by B Lab’s legal requirements, which varies based on the company’s structure and place of registration. Most companies will also need to amend their governing documents during this phase, as well as engage key board members and investors. Benefit corporations, of course, automatically fulfill this requirement.

The final step is signing what B Lab calls the “Declaration of Interdependence” and the “B Corp Agreement,” which signifies that a company is prepared to comply with B Lab’s requirements. At this stage, companies also pay their initial annual fee, which is relative to the size of their business. This ranges from \$500 for companies with revenue between \$0-\$149,999 to \$50,000+ for companies with over \$1B in revenue.

Each year, ten percent of B Corps are randomly selected for an in-depth Site Review, of which they are made aware ahead of time. B Corps that are wholly-owned subsidiaries or public companies are subject to a mandatory Site Review during each two-year certification term. B Lab conducts the review itself, and its goal during the reviews is to “verify the requirements of the Certification and further confirm the accuracy of affirmative responses in the company’s B Impact Assessment.”¹⁹ The Site Review typically takes between 6-10 hours depending on the business. There is limited information available on just how in-depth B Lab’s audits are, though one B Corp, RoundPeg, described their experience as having three parts: on-site document review, facilities tour, and employee interviews (Pinchevsky, 2015). Returning for a moment to the issue of international human and labor rights, it does not appear that B Lab audits foreign third-party manufacturers or suppliers directly. It is safe to assume that “on-site” and “employee” in this case refer to the company’s headquarters and the employees within it; B Lab does not interview contracted employees who might be working in factories overseas. However, as mentioned above, the assessment does ask about a company’s suppliers (for example, whether the payment of a living wage is certified/verified) and this could be partly verified through the document review.

¹⁹ B Lab. “Performance Requirements.” Bcorporation.net. www.bcorporation.net/performance-requirements (accessed January 14, 2018).

Every two years, a Certified B Corp is required to update their assessment. They must at least maintain the 80-point minimum score, and during each recertification additional documents may be requested as verification of certain answers. The biennial requirement is designed to make sure that as a business grows and changes, they do not abandon their social and environmental commitments. The B Impact Assessment is constantly changing and being updated, allowing companies to check themselves against the most up-to-date corporate standards.

B Lab has become truly global, as there is now a B Lab in Canada, the UK, Chile, Uruguay, Brazil, Colombia, Kenya (East African headquarters), Taiwan (Asian headquarters), Australia, New Zealand, and Amsterdam (European headquarters), and certified B Corps in many more countries.²⁰

C. Review of Benefit Corporation Literature

Benefit corporations are perhaps the least understood business entity in the United States. Though legal scholars have started paying attention to benefit corporation legislation and its possible implications, hardly any empirical studies exist that examine the inner workings of firms in this category. The legal literature has largely taken the form of a two-sided debate. One side suggests that benefit corporation legislation is a positive step toward eliminating directors' obligation to shareholder wealth maximization, and the other side suggests that such obligations do not even exist. Regardless of perspective, this literature is by and large speculative—it considers questions like: what new challenges might benefit

²⁰ In South America, B Lab works in partnership with “Sistema B.”

corporations pose to corporate law, how might they be treated in the courts, and what possible externalities might they have.

A search of “benefit corporation” within seven of the top management and organizational studies journals turns up four titles dealing directly with benefit corporations.²¹ This is not to say that they are not being written about—a Google Scholar search at the time of writing turns up 5,410 mentions—but most of the articles that have benefit corporations as their primary focus are being published in law journals. Virtually no systematic qualitative or quantitative studies exist that examine non-legal aspects of the benefit corporation.²² That being said, some scholars have analyzed benefit corporation statutes as a sort of obligatory, legally-mandated corporate social responsibility (CSR), so some of the empirical CSR literature may be relevant when thinking about benefit corporations.²³ However, given the lopsided attention given to benefit corporations by legal scholars, this literature review will primarily discuss the legal conversation surrounding the form, which helps to clarify where empirical research is needed to either validate or reject some of the more prevalent claims.

Most commentators on benefit corporations tend to focus on any combination of the following three categories, albeit with substantial overlap: *necessity*, *accountability*, or *governance*. “Necessity” refers to the evaluation of whether or not benefit corporation legislation is even needed; in other words, does it really permit actions that are not already

²¹ The following journals were searched on August 25, 2017: California Management Review, Academy of Management Review, Administrative Science Quarterly, Strategic Management Journal, Journal of Management Studies, Organizational Studies, and Journal of Leadership and Organizational Studies.

²² To my knowledge, Nancy Kurland has published the only empirical study dealing with the non-legal implementation of the benefit corporation form, which was an in-depth study of one firm. See Kurland 2017.

²³ See Hiller 2013; Sarason and Hanley 2013.

permitted in traditional corporate forms. “Governance” refers to the consideration of various aspects of a firm’s management and operation that may be affected by benefit corporation legislation. Articles focusing on “accountability” examine, from a legal perspective, how, if at all, benefit corporations will actually be held to the standards they subscribe themselves to. Again, there is a significant need for more empirical data, particularly when it comes to these last two categories. The absence of such data on accountability is somewhat expected, since the form is relatively new; however, the absence of empirical data on questions of governance is rather surprising, given that four to six years is ample time for changes in governance to manifest.

1. Necessity

Virtually every legal article concerning benefit corporations considers, to some degree, the debate around whether or not they are actually necessary. This debate is undoubtedly centered around the question of whether or not directors are as constrained by principles of profit-maximization as they are often purported to be.

Some legal analysts refer to shareholder primacy simply as a myth (Stout 2012; Chu 2013; Blount and Offei-Danso 2012). In other words, they contend that “United States corporate law does not, and never has, required directors of public corporations to maximize either share price or shareholder wealth” (Stout 2012, 3-4). In their view, those who believe that shareholder primacy is a legal *obligation* are misreading corporate law and are failing to give sufficient weight to the “business judgment rule”, which already protects the same sorts of decisions benefit corporations are designed to protect (Greenfield 2015). Interestingly, both sides of the debate focus significant attention on the same few precedents: *Dodge v. Ford*; *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*; *eBay Domestic Holdings, Inc. v.*

Newmark; and, although not a court case, the Unilever takeover of Ben & Jerry's. In fact, it is difficult to find an article that does not mention at least one, if not all of these. Because these are examined in such detail in the rest of the literature, yet another in-depth analysis of them is not useful; however, it is worth briefly examining how each side views each of these precedents.

Dodge v. Ford perhaps represents the origin of the shareholder primacy debate. Henry Ford wanted to use excess capital in a way that he felt was more beneficial to society in lieu of distributing cash to shareholders. When shareholders sued, the case went to the Michigan Supreme Court and the court ruled in favor of the shareholders.²⁴ While a landmark case for proponents of the benefit corporation, other scholars disagree with its centrality in corporate law, suggesting that there are few cases in the 100 years since the ruling that support shareholder sovereignty over director sovereignty (Koehn 2016). Lynn Stout, who has been outspoken on the myth of shareholder value, indicates that in the vast majority of subsequent rulings, courts have deferred to the “business judgment rule”—which gives directors significant autonomy in day-to-day decisions—rather than requiring that firms always and in every scenario maximize shareholder wealth (Stout 2012). Indeed, many other scholars point this out, as well (Murray 2012; André 2015; Resor 2012). Further questioning its centrality, Haskell Murray suggests that had Henry Ford even *tried* to veil his generosity as beneficial to shareholders—as opposed to openly admitting to basing his decision off non-shareholder interests—the courts may well have even ruled in his favor (Murray 2012).

²⁴ *Dodge v. Ford Motor Co.*, 170 N.W. 668, 684 (Mich. 1919).

At the same time, virtually none of these scholars deny the existence of a shareholder value *norm*: “The lack of enforcement of the shareholder value norm does not mean that it does not exist” (Murray 2012, 12). Even though courts have deferred to the business judgment rule in the overwhelming majority of cases and many states have enacted constituency statutes explicitly permitting the consideration of non-shareholder interests, shareholder wealth maximization is still seen as the “American corporate polestar” (Resor 2012, 98).

In addition to the prevalence of the norm, another justification for benefit corporations is derived from the uncertainty that still exists in corporate law. For example, Felicia Resor suggests that even though most states now have constituency statutes, these tend to be rather vague and do not offer much sense of direction. She concludes, therefore, that “benefit corporation legislation circumvents the shareholder wealth maximization norm by requiring changes to a corporation’s internal corporate law and to a state’s statutory law,” which establishes “more legal clarity for social enterprise[s]” (Resor 2012, 106). Similarly, Murray admits that corporate law in most states is not entirely clear, so risk-averse directors and lawyers may simply tend to favor shareholder interests. This lack of clarity, he posits, “is something that proponents of benefit corporation legislation can correctly point to as troubling” (Murray 2012, 17).

The *Revlon* case, while also addressing the question of shareholder wealth maximization, addresses the issue in a different context: an acquisition scenario. In what Mitch Nass calls “the most concrete limitation to a corporation that wants to advance interests other than their shareholders’ financial well-being,” Delaware courts ruled that during the inevitable sale or dissolution of a company, the directors must act to “bring the

target’s shareholders the best available price for their equity” (Nass 2013, 879).²⁵ Again, there is debate over the situations in which this rule is triggered, further adding to directors’ uncertainty. William Clark and Elizabeth Babson note that although some commentators have relegated *Revlon* to an anomaly—thus downplaying its relevance to questions of social enterprise—the fact is that there remains ambiguity about the rule. Furthermore, they contend that “to ignore the impact of director duties in a sale would be glaring oversight” (Clark, Jr. and Babson 2012, 837). Alicia Plerhoples echoes the same sentiment as Murray, suggesting that this ambiguity continues to feed into the risk-aversion of directors and corporate managers as they consider acquisitions. When the *Revlon* rule takes effect, she contends, “is important to the future of many social enterprises” (Plerhoples 2011, 246). Leo Strine, chief justice of the Delaware Supreme Court, feels that benefit corporations confront the *Revlon* question head-on: “By way of a concrete example, one of the most important consequences of the Delaware [PBC] statute is that it makes clear that the *Revlon* doctrine does not apply to benefit corporations” (Strine, Jr. 2014, 245).

eBay Domestic Holdings, Inc. v. Newmark touches on yet another aspect of the shareholder primacy question. In an effort to protect what it felt was its unique community-centered culture, craigslist erected defensive measures to prevent *eBay*, a minority shareholder, from fulfilling some its monetization goals that were misaligned with what the founders of craigslist perceived as the company’s values. *eBay* sued and won; the court ruled that the defensive measures were not reasonably related to the promotion of stockholder value (Clark, Jr. and Babson 2012). The court explained: “[h]aving chosen a for-profit corporate form, the craigslist directors are bound by fiduciary duties and standards that

²⁵ *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.* 506 A.2d 173, 182 (Del. 1986).

accompany that form...[which] include acting to promote the value of the corporation for the benefit of the stockholders.”²⁶

This ruling, unsurprisingly, is heralded by many benefit corporation proponents, but the same sorts of arguments apply as in the cases above. Murray asserts that because this was not an issue of everyday decision making, craigslist’s decisions were not subject to the business judgment rule, and that this precedent, in reality, is only relevant in very narrow contexts (Murray 2013). He also compares it with *Dodge v. Ford*, suggesting that, like Henry Ford, the craigslist founders flat-out confessed to eschewing shareholder value; again, had they done this more carefully, the ruling may have been much different. However, the confined context of the case is not so much of a problem to other scholars. Janine Hiller contends that despite its unique facts, “it is in a line of cases that can give a director pause before taking non-shareholder interests into consideration in corporate decision making, and it highlights the application of shareholder wealth maximization not just to publicly held corporations but also under certain circumstances to closely held corporations [like craigslist]” (Hiller and Shackelford 2018, 16). This last point is particularly important, as the vast majority of benefit corporations are, at present, privately held.

The last event worth mentioning is Unilever’s purchase of Ben and Jerry’s in 2000. Following a hostile takeover bid by Unilever, to which the founders were opposed, the board of Ben & Jerry’s allegedly felt obligated to complete the sale because it resulted in a large shareholder payout (Koehn 2016). Ben & Jerry’s is central to the story of the B Corps and benefit corporations because of its clear commitment to social values throughout its life;

²⁶ eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1, 33-34 (Del. Ch. 2010).

however, when used as an example of why new legal forms are necessary, it often meets strong criticism. Antony Page and Robert Katz, in an article published in the *Stanford Social Innovation Review* in 2012, fervently deny that Ben & Jerry's actually had to sell, calling into question why "[c]orporate law has been fingered as the culprit in the Ben & Jerry's sale, which has become the poster child, proof text, and Exhibit A for the proposition that the traditional business corporation is fundamentally inhospitable, if not outright hostile, to social enterprise" (Page and Katz 2012, par. 5). Haskell Murray concurs, suggesting that the story is often "simplified and exaggerated" and that "even given the enhanced scrutiny applied in the takeover context, there is serious doubt as to whether Ben & Jerry's *had* to sell to Unilever" (Murray 2012, 16). Page and Katz argued that Ben & Jerry's had erected all sorts of defensive measures to protect them from this sort of scenario—for example, they had lobbied for constituency statutes in Vermont and had adopted a "poison pill" which, in short, makes hostile takeovers unattractively expensive—and, ultimately, the problem was that "Ben & Jerry's didn't get its defense quite right, not that some flaw in corporate law required the sale" (Page and Katz 2012, par. 31).

Opposing them are the Ben & Jerry's founders themselves, who have publicly stated on multiple occasions that the law required them to sell despite their ardent desires not to.²⁷ Also opposing them are the founders of B Lab, who, it is worth noting, commented extensively on the Page and Katz article.²⁸ In response to Page and Katz's call for proponents of benefit corporations to "identify real and unavoidable instances of the Ben & Jerry's

²⁷ See e.g. Dembosky 2010; Hannah Pool, "Question Time with Hannah Pool," *The Guardian*, July 31, 2008. www.theguardian.com/business/2008/jul/31/5.

²⁸ The three founders of B Lab—Jay Coen Gilbert, Bart Houlahan, and Andrew Kasoy—wrote an in-depth response in the comment thread of this article, complete with Jay Coen Gilbert's personal email address and phone number. Page and Katz responded directly on the thread with a detailed response of their own. The exchange can be found at the URL in note 58.

scenario,” the B Lab founders suggest two: (1) if Ben & Jerry’s were incorporated in any of the roughly 20 states in which no constituency statutes exist; and (2) if Ben & Jerry’s justified any corporate decision on the benefits that might accrue to society and not shareholders (Page and Katz 2012).²⁹ In other words, they contend that even if the Ben & Jerry’s sale was not necessary, there are feasible contexts in which it would have been, which serve the purpose of justifying the new legal form anyway.

Ultimately, what the debate over shareholder primacy in the benefit corporation literature illustrates is that while the new corporate form may not be absolutely legally *necessary*, there is sufficient uncertainty about how corporations are supposed to act in a variety of circumstances. What benefit corporation legislation appears to do, even if it does not permit any new types of corporate behavior, is explicitly clear up some of the uncertainty that virtually all scholars, regardless of where they stand, admit exists. In so doing, it purports to better align entrepreneurs, directors, and investors; whether or not, and how, it may do this is a large part of the question that sits at the center of this study.

2. *Governance*

The extant literature that touches on questions of benefit corporation governance tends to cluster around the issue of clarity: does it give sufficient guidance to boards of directors? While some scholars praise benefit corporation statutes for going beyond constituency statutes and *requiring*, rather than merely *permitting*, the consideration of stakeholder interests, others feel that this requirement is too open-ended.

²⁹ For B Lab founders’ comments, see comment thread

Steven Munch suggests that the “real disadvantage of the benefit corporation may be that it does not do enough...to encourage mission fulfillment, to guide directors and officers, or to assist prospective investors” (Munch 2012, 188). In other words, it does not make it clear to those engaging with the form how they are to act. Haskell Murray concurs, calling the lack of guidance one of the form’s “primary problems” and contending that the form requires directors to serve multiple stakeholder groups, yet does not instruct them on how to do so (Murray 2012, 27). In his view, it is not even clear how it is possible to serve *two* masters, let alone seven or more (Murray 2012). Munch agrees, suggesting that it may not be a bad idea for the law to require benefit corporations to identify which particular stakeholder group they will strive to serve (Munch 2012). Several others echo their concerns with the multiple stakeholder problem (Blount and Offei-Danso 2012; Koehn 2016).

In his prescription for how to improve the benefit corporation, Munch touches on several other key aspects of governance that relate to the issue of clarity. If it is not clear in what ways and to what degree directors must consider their social obligations, they could be aided in a number of ways. He makes several suggestions. For starters, all states should require benefit directors and, taking that even further, they should require benefit corporations to enlist additional benefit directors as the company grows, eventually leading to the organization of an entire benefit committee (Munch 2012). Additionally, the law could stress the importance of the social goals by imposing financial controls; the benefit corporation could follow its European equivalents in imposing dividend caps, or could require that the “issuing of any real financial return is contingent upon first producing a clear, measurable social return” (Munch 2012, 192). Munch also thinks the law needs to explicitly address when, how, and to what extent a company’s social purpose is considered in business

decisions—something that could be achieved, for example, through the use of “stakeholder assessments” (Munch 2012; Sneirson 2007).

Leo Strine Jr., Chief Justice of the Delaware Supreme Court, views the way in which benefit corporations guide director decisions as more, in a sense, internal. While admitting that it is a rather modest step in the right direction, he thinks that the benefit corporation does create a good bit of clarity, despite not being explicitly expressed in the statutes:

I am not as cynical as some, and I believe that a substantial segment of corporate directors think that it is important to consider and respect the best interests of employees, consumers, communities, and society, even when a corporation must be sold. Giving these directors a clear legal duty to do what their conscience already calls them to do has a behavioral value I do not think should be trivialized (Strine, Jr. 2014, 246).

As I will note in Chapter 3, using the benefit corporation to concretize, or make legitimate, the “social conscience” of a founder appears to be a primary driver of adopting the form; Strine’s comments should not be dismissed as idealism.

3. Accountability

Even if a benefit corporation took it upon themselves to develop an explicit system of governance in response to the issues mentioned above, the question would still remain: what is keeping them accountable? In theory, accountability is supposed to be derived from the benefit enforcement proceeding and the enhanced transparency requirements, both discussed earlier. However, both of these mechanisms have met various forms of criticism.

The primary criticism levied against the benefit enforcement proceeding is that it is a right of action only reserved for shareholders: “[A]lthough directors have a duty to consider

each of their various stakeholder groups, they are only legally accountable to one: shareholders” (Munch 2012, 189). Thomas White points out that stakeholder interests are “left at the mercy of shareholders” and, despite their ability to do so, there is nothing that suggests a shareholder *must* enforce stakeholder interests in this way (White 2015, 346). Indeed, to date, no such instance has occurred.

Furthermore, there is substantial uncertainty about how the courts will rule in such a scenario and, to some, the range of possible options are not so appealing. Justin Blount and Kwabena Offei-Danso suggest that a court would have two options: either it engages in micromanagement of the corporation and substitutes its own judgment for that of the managers, or it defers to something akin to the business judgment rule (Blount and Offei-Danso 2012). As Blount and Offei-Danso point out, the drafters of the Model Legislation themselves suggest that the latter is the most likely option; however, this contradicts what they suggest elsewhere, namely that the shareholder right of action in benefit corporations was designed to provide “teeth” to the enforcement of expanded interests (Blount and Offei-Danso 2012, 37; Clark, Jr. and Babson 2012). If it is to provide “teeth,” the outcome would arguably have to be more strict than the mere application of the business judgment rule, which, from the shareholder perspective, leaves them in no different position than they would be in in a standard corporation (Blount and Offei-Danso 2012). Some commentators suggest that benefit corporations may even provide more ways for managers to mask their self-interested decisions, leading to more director entrenchment (Murray 2012).

There are other aspects of uncertainty, as well. If courts do in fact engage more actively, rather than merely applying the business judgment rule, Blount and Offei-Danso further contend that benefit corporations “might suffer from the problem identified by Adolf

Berle long ago—when a corporation is accountable to everyone, it is accountable to no one” (Blount and Offei-Danso 2012, 10; Berle, Jr. 1932). In other words, there is no real indication of which stakeholders are the most important, and thus “no stakeholder could ever be sure how their rights would measure against those of the others and in whose interest any conflict would ultimately be resolved” (Blount and Offei-Danso 2012, 10). If, for example, a minority activist shareholder brings a benefit enforcement proceeding on behalf of a particular stakeholder group, the court could, in theory, decide to favor their interests above the rest and rule in such a way that adversely affects all the other shareholders (Blount and Offei-Danso 2012). All of these possibilities serve to muddy the waters of how exactly the legal accountability mechanisms will actually work.

Legal considerations aside, several others question the extent to which the transparency standards imposed on benefit corporations are sufficient to provide accountability. Thomas White criticizes the Model Legislation for providing an “ineffectual set of instructions” for the annual benefit report—the principal means of transparency—and suggests that a “hefty portion” of what the annual benefit report requires is non-financial information, about which the market is an inadequate assessor (White III 2015, 348). We should not expect the market to hold benefit corporations accountable by way of their benefit reports.

Assuming for a moment that the market did have such an effect, the problem still remains that the benefit reports are, in the eyes of some observers, often incomplete, if not outright non-existent. Mitch Nass contends that B Lab, the most popular of the third-party standard setters, produces scorecards “that provide the public with only a cursory understanding of a company’s social responsibility” (Nass 2013, 885). These points are well-

taken. B Lab only releases aggregated data for its certified companies and does not disclose how companies answered all of the questions. To some degree, this is understandable, though they could arguably provide a bit more transparency into company assessments.

Additionally, his assertion that benefit corporations frequently fail to deliver on their requirement to make their annual benefit reports available on their websites appears to be true, as well.³⁰

Others have pointed out more problems with the reporting process. Steven Munch feels that it provides a “clear opportunity for selective reporting, if not outright misconduct” (Munch 2012, 194). Blount and Offei-Danso charge that the reports do not add much value since they do not have to be audited, and there are no adverse consequences associated with a negative report (Blount and Offei-Danso 2012). A company could report a total and utter failure to pursue its general public benefit, yet face no punishment; in fact, one could argue they may even be praised for their honesty and full transparency. On more theoretical grounds, Briana Cummings suggests that reporting might even encourage the opposite of the desired effect: “Disclosure does not necessarily force introspection and internal change. On the contrary, evidence suggests that disclosure requirements, when tied to market pressures or other threats of sanctions, can impede innovation and adaptation” (Cummings 2012, 612; citing Snyder 2007, 595).

Not all scholars think that benefit corporations fall short, though. Michelle Stecker insists that even though the debate rages on, “with accountability and transparency mandates embedded in the legislation, a broad array of third-party watchdogs, and the B Lab

³⁰ While empirical statistics do not exist, it was clear throughout the course of sampling for this study that many benefit corporations had not complied with this requirement. It should be noted however that Public Benefit Corporations—i.e. those registered in Delaware—are not legally required to do this.

certification gaining more traction, the Goldilocks of safeguards has been attained” (Stecker 2016, 379). Similarly, Brett McDonnell suggests that the statutes have struck a “sensible balance which largely manages to avoid being either too strong or too weak, and thus gives benefit corporations a way to commit to pursuing public benefits while not scaring off managers and entrepreneurs with the threat of ruinous lawsuits” (McDonnell 2014, 58-59).

A few scholars have also begun to examine yet another dimension of accountability—internal accountability—which is particularly relevant to this study (Kurland 2017; Cummings 2012). The contributions of Briana Cummings will be examined in detail in Chapter 3, but a brief mention of their work is worthwhile here. Cummings feels that the accountability schemes adopted by the legislation are “ill-suited to the regulation of social welfare objectives” but that by fostering “bottom-up and horizontal mechanisms,” benefit corporations can foster an environment conducive and accountable to these goals (Cummings 2012, 578). Building off of this, Nancy Kurland explores one firm’s transition to a benefit corporation and reveals that “a company can be held accountable for delivering requisite public goods when external mechanisms are accompanied by an organization’s internal commitment to self-awareness, learning, and measurement” (Kurland 2017, 519). Crucial to any sort of internal accountability, of course, are the employees of the firm, whose role will be explored later.

4. Conclusion

Clearly, the bulk of benefit corporation literature focuses on legal questions. Non-legal literature on benefit corporations is virtually non-existent and, as such, scholars have pointed out several questions that still need to be addressed. How are daily decisions affected? How do investors respond to a benefit corporation form, and is it compatible with

raising capital? What is the most significant motivating factor for an existing business to adopt the BC form, and how does individual leadership impact the decision? (Hiller 2013) These are the sorts of questions that motivated this study and are indicative of the gaps it hopes to begin to fill. After briefly detailing the methods used for data collection, the rest of this paper will be dedicated to exploring three hypotheses that touch on various aspects of these questions.

D. Methods

Due to the fact that there are so few empirical studies having to do with benefit corporations, a qualitative exploratory study was fitting (Stubbs 2017; Belz and Binder 2017; Blaikie 2000). This study used semi-structured interviews with 12 registered benefit corporations in the United States, spanning a range of industries and geographic locations (see Table 2).

Prior to contacting any companies, I submitted my Interview Guide, Confidentiality Agreement, and Research Plan and received clearance from the UC Santa Barbara Internal Review Board. In total, I approached 41 benefit corporations via email to participate in the research. These companies were chosen through the following process. Fortunately, I was able to find a list of over 4,000 registered benefit corporations. I started with companies that were in my immediate geographical vicinity (MD, VA, DE) and visited their websites to make sure that they were still active. If their website was still active, I looked at their staff and LinkedIn pages to get an idea of how many employees worked there, as I was ideally looking for medium-sized companies. I also checked their social media pages for recent activity. Finally, I checked to see whether or not the company had a Crunchbase account and whether or not they listed any external funding, since I knew that funding was an initial area

of interest. After exhausting the most promising opportunities in my region, I repeated this process for companies in MA, NY, and CA. It should be noted that not all of my participants came from this process; a few participants came from snowballing with the help of other participants. Additionally, not all companies “checked every box” – but I ultimately pursued interviews with them for other reasons. For example, one founder was influential in passing benefit corporation legislation in his state and another was a well-recognized thought leader in this space.

In my initial email to them, I explained that the study was meant to explore the “on-the-ground” impacts of becoming a benefit corporation and I gave them the interview questions ahead of time. I made sure to make clear to potential participants that the interview guide represented “jumping-off points” and that other questions were likely to come up during the interview. I also assured them that their anonymity would be preserved, however several participants indicated that they would not mind being mentioned by name, as they felt that being transparent was part of upholding their corporate values. Of the 41 companies I reached out to, 16 companies responded. Interestingly, the response rate from non-B-Corp benefit corporations was 18%, compared with 54% from B-Corp benefit corporations. This might suggest that B Corps, though not legally required, are more committed to transparency than benefit corporations, who have adopted increased legal transparency standards. It is important to note that this may indicate a non-response bias.

I carried out interviews with 10 of the 16 companies that responded, 3 of which were in-person at the company offices and the rest were either over the phone or via video communication. Through these 10 participants, I was put in touch with two others who ended up participating, as well. Participants were either founders, counsels, or director-level

employees who held particular knowledge about the company’s legal status and, if applicable, its B Corp status.

Table 2 Study Participants

Reference*	Sector	No. of Employees	State Registered	Founded	Participant Role	B Corp?
A	Software	~25	DE	2012	Founder	Yes
B	Software	~55	DE	2012	Founder	Yes
C	Software	~15	NY	2006	Founder	Yes
D	Financial Services	~65	VA	2006	VP	Yes
E	Financial Services	~45	DE	2014	Counsel	No
F	Financial Services	~75	MA	1993	Director	Yes
G	Financial Services	~5**	DE	2016	Founder	No
H	Education	~200	DE	2013	Counsel	Yes
J	Consumer Goods	~35	DE	2012	Founder	Yes
K	B2B Products	~55	VA	1964	President	Yes
L	Food	~45	VT	1981	Manager	Yes
M	Consulting	~125	VA	2006	Founder	Yes

* Letters will be used to in interview participant citations in the coming chapters

** Company had just completed financing and is expecting to grow to 50-60 employees by end of 2018

Interviews typically lasted between 30-40 minutes and were conducted from October-December 2017. I recorded all interviews with consent and transcribed them shortly afterwards. Due to the varied nature of the participating companies, no two interviews followed the exact same script. In interviews with companies that had been a benefit corporation during capital raises, for example, I focused more heavily on this aspect than I did with companies that had not raised outside funding since becoming a benefit corporation. All participants discussed their backgrounds, how and why they decided to become a benefit corporation, and whether or not they feel it has had any day-to-day impact on their company’s operations. I also asked all of the companies that were also certified B Corps

about their experience with this, directing a great deal of focus towards the assessment and the impact of being a B Corp on the hiring process.

Again, because I approached this as an exploratory study, I was unsure exactly which questions it might be able to shed light on or what sorts of hypotheses it might be able to generate. I read and analyzed the interview transcriptions several times in order to develop a list of nine initial hypotheses and insights—shown in Table 3—and ultimately determined that the most interesting findings had to do with funding, hiring, and accountability. These are three areas that are mentioned quite often in the existent literature, but towards which little empirical effort has been directed. I developed three follow-up questions having to do with these areas and sent them out to participants via email, who had indicated during their interviews that they were willing to answer additional questions as they came up. Most participants did not answer these follow-up questions; however, they did generate a few additional responses.

In grappling with these initial hypotheses, it occurred to me that much of what was going on centered around the theme of *communication*, whether it be with potential funders, current shareholders, customers, or employees. I wondered whether signaling and screening theory—with its emphasis on mitigating information asymmetry problems through credible communication—might be a lens through which I could better explain and expand upon these hypotheses. Referring to Table 3, I ultimately set out to see how signaling and screening might allow me to explore *H2*, *H7*, and *H8* in more detail.

Table 3 Initial Hypotheses

Fundraising	<i>H1: Confusion seems to be the norm amongst traditional and institutional investors.</i>
	<i>H2: Being a benefit corporation may make fundraising more difficult, but it could also be a valuable tool in finding investors who are best fit for the long term.</i>
Mission-Embedding/Protection	<i>H3: Many founders see registering as a benefit corporation as a defensive move</i>
	<i>H4: Being a benefit corporation has helped make some founders feel like they can pursue their mission agenda more unapologetically, without having to constantly justify it</i>
	<i>H5: Registering as a benefit corporation appears to be much more a method of concretizing a founder's personal values than a method of introducing an external value system into the company</i>
B Corp	<i>H6: B Corp founders would like to see the B Impact assessment become more personalized</i>
	<i>H7: Being a B Corp is a salient part of the personnel process, and helps companies attract more motivated, values-aligned job candidates</i>
	<i>H8: Going through the biennial assessment process not only serves as a valuable time of reflection, but also helps companies stay true to their mission and informs them of additional actions they could be taking</i>
Market Positioning	<i>H9: Making this social or environmental commitment can help companies carve out a valuable market niche</i>

II. SIGNALING AND SCREENING IN BENEFIT CORPORATION FINANCING

Even though no empirical studies exist that examine how investors will perceive and react to the benefit corporation, scholars have acknowledged this as critical to the future of the form. Haskell Murray suggests that the question remains “whether significant numbers of investors will invest in a corporation that chooses as its primary master something other than shareholder wealth maximization” (Murray 2012, 53). Similarly, Leo Strine Jr. posits that the ultimate success of the form will depend on “the existence of a sufficient base of investors who not only mouth the belief that corporations should be managed for the best interests of all they materially affect, but in fact act on that belief when real world investing and voting decisions have to be made” (Strine, Jr. 2014, 245). Others have speculated further. Daryl Koehn, for example, argues that benefit corporations will likely have difficulty attracting and retaining capital due to the uncertainty of priorities in takeover scenarios and the reality that even socially responsible investors demand a reasonable return, thus forcing managers to succumb to the same pressures (Koehn 2016). None of these claims, however, has been the subject of any empirical scrutiny.

This is a particularly important area to investigate, especially in light of the increased prevalence of venture capital in the United States. In just the first quarter of 2018, more venture capital was invested than in the totality of 2009; if this pace continues, 2018 will shatter 2017’s record of \$82.9 billion dollars invested (Pitchbook-NVCA 2018). At the same

time, impact venture capital funds—which invests in companies that provide some social or environmental benefit—is also on the rise, though it represents a fraction of the total market. Impact VC firms have raised around \$13 billion since 2001, with \$10 billion of that being raised between 2010-2017 (Rheingold 2017). To put it into perspective, the venture capital industry as a whole has raised about \$238 billion in the same seven-year stretch (Pitchbook-NVCA 2018). Venture capital is unique in its orientation, as it is almost explicitly built for the short-term; in other words, investors want exits—be they acquisitions or IPOs—and they want them relatively quickly. The lopsided presence of non-impact funds, however, means that many social entrepreneurs end up turning to more “traditional” venture capital funds to finance their businesses, just as many of the participants in this study have.

In any entrepreneur-investor relationship, alignment of interests and priorities is central. Indeed, “alignment” attracts quite a bit of attention in entrepreneurship and investment literature (Das and Teng 2001; Peter Wirtz 2011; Collewaert and Sapienza 2016). Differences can lead to tension from competing demands; in the social enterprise space, these tensions most often arise in the form of conflict between traditional business demands and social missions. This is another well-explored area of the literature (Smith, Gonin, and Besharov 2013; Dees 2012; Margolis and Walsh 2003; Tracey and Phillips 2007). Social entrepreneurs dedicated to preserving their social missions long-term, then, seek investors whose values and priorities reflect their own; regardless of how they happen to balance these interests, they ideally want investors who share their perspective. The question relevant to this chapter is: can the benefit corporation help play matchmaker?

A. Preview of the Argument

This study begins to examine how being a benefit corporation might affect fundraising. I argue, based off of 12 interviews with benefit corporation founders and counsels, that being a benefit corporation acts as a screening mechanism to help social entrepreneurs better find values-aligned investors. The argument can roughly be broken down in the following way:

- (1) Social entrepreneurs seeking funding have an information asymmetry problem, in which the information they lack is a potential investor's *degree of social commitment*
- (2) Because the benefit corporation introduces uncertainty by calling into question a shareholder's primacy, an investor will stay away from it unless they either (a) care to some degree about the stated mission or (b) do not think the form matters
- (3) However, due to the robust board approval required in a benefit corporation for big decisions (like a sale or the abandonment of the status), investors are disincentivized from investing on the basis of (b)
- (4) Therefore, being a benefit corporation will aid in creating alignment by screening out (some of) those investors who are least willing to make social-financial trade-offs

The bulk of this chapter is dedicated to exploring this argument in depth and, to be clear, deals exclusively with benefit corporations. As will be shown, *uncertainty* is a key piece of the argument here, which is derived chiefly from the legislative framework.

Another clarification is also necessary. This argument is premised on the assumption that the founder of a given benefit corporation *wants* to find legitimate, long-term alignment with his or her investors and that they are dedicated to preserving the mission. Of course, this is not always the case. It is not difficult to imagine that behind closed doors, founders could disclose their true priorities to investors, and investors could thus be given reason to feel that

the form actually will not matter so much. Confident that they are investing in a like-minded founder with a group of other like-minded investors, they will not have much reason to doubt their primacy. As discussed in the previous chapter, shareholders are the only individuals who are able to hold management accountable; if no one desires to do so, the benefit corporation form will not act as a screen.

In order to give weight to this argument, I must show the following: (1) that there is in fact an information asymmetry problem that stems from the social entrepreneur's desire for values alignment; (2) that the benefit corporation, in the eyes of many investors, is characterized by uncertainty; (3) that this uncertainty is enough to push some investors away; and, (4) that investors are unlikely to invest on the basis that the legal form does not matter. After briefly providing some background on screening theory, the remainder of this chapter is dedicated to substantiating these four points.

B. Signaling and Screening Theory

In 1970, George Akerlof published *The Market for "Lemons"*, a seminal paper that opened the floodgates for considerations of asymmetric information in the marketplace. In it, he related quality and uncertainty through what is now a well-known example: the used-car market. In the example, the seller of a car knows far more about its quality than the buyer; only the seller knows if the car is in good condition or is a "lemon." A buyer, therefore, has to guess the quality. To borrow from Tim Harford, who has elaborated on this example, consider that a car in good condition is worth \$5,000 to a buyer, but the buyer thinks there is a fifty-fifty chance that the car is a lemon (Harford 2006). Because the car might turn out to be a piece of junk, the buyer might only be willing to pay somewhere around \$2,500. The seller would find this offer fair if he or she also felt there were fifty-fifty odds that the car is a

lemon, however this is not the case—the seller has more information. If offered \$2,500 for what the seller knows is a lemon, the seller would jump at the opportunity to sell. In such a case, though, the buyer is then alerted to the fact that the car is a lemon.

So, what happens? No seller wants to sell a good car for less than \$5,000, but no buyer is willing to pay that price for a car that might be a lemon. In the end, the only cars that get sold are lemons to the few buyers willing to buy them. The market breaks down entirely. Harford notes that “[l]ess extreme assumptions about the problem lead to less extreme breakdowns of the market, but the conclusions are similar: if some people know more than others about the quality of a product, then some high-quality products may not be traded at all, or not be traded very much” (Harford 2006, 111).

Following Akerlof’s exploration into the problems of asymmetric information, Michael Spence introduced the idea of “signaling” a few years later in 1973, when he argued that the market actor with the information might be able to credibly communicate it to the market actor without the information—in effect, sending a “signal” (Spence 1973). His primary example was the job market. When hiring someone, employers are purchasing a “lottery”; they are not able to directly observe a candidate’s specific productive capacities up front. The employer, therefore, agrees to pay a wage relative to their expectations. In this instance, a good job applicant has the information that they will be a quality worker but has no way to credibly communicate it to the employer. This might lead to good employees being paid the same as bad employees—but would-be good employees are not satisfied with this, so they want to distinguish themselves. One way they can do this is by, for example, obtaining an education that will set them apart. However, and this is critical, the education only acts as an effective signal if the cost of attaining it is negatively correlated with

productivity. In other words, the cost of obtaining the education (this could mean tuition, mental energy, time, etc.) decreases as an applicant's productivity increases, and vice versa. This condition is necessary because it makes the signal too costly for the bad applicant to obtain, which means that only good applicants will have the education. The education, then, retains its value as a signal of a good applicant.

Before moving on to discuss screening, with which this chapter is primarily concerned, it is worth briefly discussing benefit corporations in the context of signaling. Much of the literature on benefit corporations discusses how the form sends a signal. Alicia Plerhoples, for example, says that “[t]his signaling may attract directors, investors, and employees committed to the dual mission” (Plerhoples 2015, 109). Similarly, Brianna Cummings suggests:

[T]he legislation aims not only to lock in assets to benefit corporations' dual commitments and prevent greenwashing, but also to help these businesses raise capital—at least from some sources—by signaling to socially responsible investors, consumers, donors, and potential employees and business partners that a certified benefit corporation is in fact producing social and environmental returns worthy of financial support (Cummings 2012, 591).

References to benefit corporations as “signals” appear, at least implicitly, to be getting at what Michael Spence was talking about. Investors (information seekers) who are looking for mission-driven enterprises (information holders) can use the corporate form as a way to weed out those who might be “all talk.” However, this proposition lacks empirical support and, even in theory, is underdeveloped. For it to fit what has now become generally accepted as an effective signal, it would have to be shown that the cost of obtaining benefit corporation status is negatively correlated with mission commitment. As discussed above, this condition

would have to hold in order to dissuade those who are not committed from electing to choose the form. We have little reason to believe that the legislation works this way.

Furthermore, we would also have to be given reason to believe that mission-driven investors are currently lacking information about mission-commitment. Generally, impact investors—those who claim to care most about mission components—invest in companies that exist to solve some social or environmental problem. The mechanism by which such companies address a certain problem is built into their business model. It is not within the scope of this study to comment on this with certainty, but it is unlikely that this class of investors feels they are lacking sufficient information to assess mission-commitment. The products or services they are investing in *are* the commitment. To be clear, this is not to say that benefit corporations have no value to impact investors—two participants even said it is a “huge benefit”—it is merely to say that impact investors likely face less of an information asymmetry problem.

On the other hand, socially responsible investors (SRI) who may not be as concerned with investing in mission-driven business models but who are concerned with things like environmental, social, and governance performance (ESG) could view benefit corporations as a quick-and-easy filtering device of sorts. Let us examine this possibility and see if benefit corporations could actually be considered a signal in such a scenario. We will assume that any company—socially-committed or not—can become a benefit corporation.³¹ If merely being a benefit corporation makes a company eligible for an SRI investment that they otherwise would not have been, it follows that the SRI investor from which they receive the

³¹ This should be obvious. There are plenty of companies that are benefit corporations but that make no mention of it and do not have an obvious social or environmental component. Furthermore, there is virtually no external barrier to adopting the benefit corporation form. If a company acquires the necessary internal approval, all they must do is submit the paperwork and pay a small filing fee.

investment is not so socially-committed. If they were, being a benefit corporation would not be enough to qualify the company for investment. Due in part to the enforcement and accountability shortcomings discussed in Chapter 1, a committed SRI investor would conduct more due diligence than simply taking the corporate form at face value.

In this example, we can question whether the SRI investor can even be considered to be lacking or seeking information; in reality, all they want to do is to be able to “check a certain box.” Conversely, the committed SRI investor would view being a benefit corporation as one potentially qualifying criteria among many. This may, in some instances, help a benefit corporation make a better case for itself, but the extent to which it would do so is not at all clear, since the cost of adopting the form could be quite low for an entrepreneur who is not deeply committed. The committed investor *is* facing an information asymmetry problem, but for this reason is unlikely to use the benefit corporation to solve it. It should be noted that this is a cursory analysis and this study is not in a position to comment definitively either way; all of this is merely meant to suggest that the benefit corporation does not have much strength as a *signal*. Instead, it appears that being a benefit corporation acts much more effectively as a *screen*.

Whereas Spence thought about how those with information could communicate it, Joseph Stiglitz considered how those without information might be able to uncover it. He initially considered screening in the context of the insurance industry, which he first discussed in a paper presented in 1973.³² Insurance is one of the industries in which the buyer actually has more information than the seller; customers know their own health, and therefore their likelihood of needing to file claims, far better than the insurers do. Stiglitz wondered:

³² The paper was published a few years later; see Stiglitz 1976.

how do insurance companies entice consumers to reveal this information about themselves?

One way might be to offer different options. If the insurer offers another plan that reduces the premium but increases the deductible, customers would reveal their information when they chose a plan. Turning again to Tim Harford, he explains: “Low-risk customers would be attracted to that kind of deal, because the insurance is cheaper and they don’t expect to claim very often anyway, but high-risk customers would rather pay the higher premium because they expect to claim frequently, so a high deductible will cost them a lot” (Harford 2006, 119).

A screening mechanism forces the buyer’s hand. In the case of benefit corporation fundraising, investors are the buyers. The social entrepreneur is selling a stake in the company, but has a particular need to entice potential investors to reveal some inside information about themselves—namely, how committed to the company’s mission they are and to what extent they are willing to give more weight to non-shareholder interests. Just like a signal, a screen must also involve a cost; in order for the benefit corporation to be an effective screen, it must impose some sort of cost on the investor. In this case, I suggest that while there is little immediate cost, there is a significant future cost, namely whatever trade-offs end up occurring between the financial and mission-oriented bottom lines. While the benefit corporation itself does not guarantee that any of these trade-offs will even occur, all that is necessary in order for it to act as a screening mechanism is that its costs are *perceived*. This perception gives rise to investor uncertainty, which, as we will see below, plays a critical role in the effectiveness of the screen.

Importantly, social entrepreneurs do not *always* face the problem of missing information. Some investors may have a track record that speaks for itself; maybe, for

example, they are impact investors with a reputation for being “founder friendly” and a solid history of investing in mission-driven companies that balance multiple stakeholders. This could be enough to eliminate any doubt the social entrepreneur might have.

However, as is the case with many of the participants in this study, founders will often need to accept funding from investors who do not fit this profile. Oftentimes, even self-proclaimed impact investors will not fit this profile, as one participant noted: “My experience in general has been that for some impact investors who would call themselves that, they are cutthroat about how much money they want to make” (Participant B 2017). In many instances, then, a social entrepreneur seeking long-term mission alignment will likely be missing information about their prospective investors. How will a particular investor view trade-offs that may not be financially optimal in the short-term? How will they act in an acquisition or takeover scenario? Faced with an opportunity to be an early-stage investor in a promising business, an investor might claim to be more mission-conscious than they actually are in order to get a foot in the door, which could cause real tension later on.

The social entrepreneur needs to know more “inside information” about the investor, and the benefit corporation can help them do so.

C. The Argument for Benefit Corporations as a Screen

Again, in order to give weight to this argument, I must show the following: (1) that there is in fact an information asymmetry problem that stems from the social entrepreneur’s desire for values alignment; (2) that the benefit corporation, in the eyes of many investors, is characterized by uncertainty; (3) that this uncertainty is enough to push some investors away; and, (4) investors are unlikely to invest on the basis that the legal form does not matter.

1. Information Asymmetry

The first step of building the argument for benefit corporations as a screen is to illustrate that there is in fact an information asymmetry problem. Social entrepreneurs cannot ever *really* be sure how strongly investors share their emphasis on mission principles. Because the current legal framework is built to prioritize profit, “entrepreneurs with a mission-driven business may be reluctant to accept outside capital from investors who may not share their long-term vision for social and environmental responsibility” (Clark, Jr. and Babson 2012, 824). Showing that this problem exists, of course, relies on showing that social entrepreneurs are seeking social commitment alignment; if they were not, then there would not be information they desired to uncover, and there could not be said to be an information asymmetry problem of this sort.

There are three categories into which interview participants’ answers generally fell when asked about their motives for becoming a benefit corporation: (a) “mission defense”; (b) communication to shareholders; and, (c) flexibility and justification for mission-driven decision-making. From these answers, it follows that there is some degree of uncertainty among benefit corporation founders about how they will align with their investors on future issues—otherwise, these motives would likely not be strong enough to warrant becoming a benefit corporation. This uncertainty indicates both a lack of critical information and a desire to find alignment.

(a) “Mission Defense”:

“One goal was to actually put in place legal protection...the legal mission protection that benefit corporations allow, and specifically the definition of a mission we could preserve in a sale” (Participant H 2017).

“You don’t want someone to take it over and turn it into just a for-profit company”
(Participant J 2017).

“If you care about protecting your mission, you have to do 100 different things. You need to bake it into everything you do, and it seemed like changing our status was one of the many things that I could do to increase the odds that our mission would be protected...The main thing for me was it was a bit more of a defensive move to make sure that I could protect against a company trying to acquire us that I really thought was bad for kids. And I wanted to be able to say ‘No’ to them even if they were offering more money than another company” (Participant B 2017).

In each of these statements, it is clear that founders are dealing with some level of uncertainty that stems from not knowing how their investors will act in certain scenarios. Whether or not the benefit corporation is successful in preserving and prioritizing the mission is irrelevant here; what matters for the sake of this argument is that founders perceive an information asymmetry problem.

(b) Communication with shareholders:

“One of the reasons was a communications goal. Less from a public relations point of view and more internal communication—communication with current and prospective investors. So that we could say to all of those people, ‘Hey, this is a mission-driven company and we are going to prioritize the achievements of that mission more than the average startup that you have joined or invested in” (Participant H 2017).

“When any business begins and you’re sort of in the period when you’re looking for money from angel investors, you’re looking for true believers. And this happens to be a business model that from the very beginning identified that it wanted to create a public good, make part of our society better, provide a solution to a vexing problem. So, you’re either interested in a big dream or you’re not...That having been said, it is really important from the very

beginning, that we've said, 'This is a company that prioritizes shareholder value and giving people return on investment...this is not philanthropy'" (Participant A 2017).

Both of these quotes indicate a simultaneous desire to communicate more information to shareholders while also to prompting shareholders—current or prospective—to communicate information back. In each case, the founders clearly felt a need to collect more information—otherwise they would not have found it necessary to employ the benefit corporation as a communications tool. To what extent is an investor “interested in a big dream” or willing to “prioritize the achievements of the mission”? These founders sought answers to these questions, indicating an information asymmetry problem.

(c) Flexibility and justification for mission-driven decision-making:

“It certainly allows us a lot more flexibility especially when we want to pursue more non-traditional courses of action” (Participant E 2017).

“Before it felt like it was my little project—the mission part—and after [we converted] I felt like the board is now responsible for upholding our social mission and, you know, sharing responsibility. And that just makes me more comfortable about making sure the board did talk about and address issues related to the mission” (Participant B 2017).

“Absolutely. Absolutely, yes, [it has helped me push decisions in favor of the mission]. Now it's expected, actually. We are expected to do both. So, if we are not doing enough of one or the other, that is a challenge. It is a direct challenge. So, I think it helps us find a good balance” (Participant J 2017).

While these responses are more reflections on how the benefit corporation has made founders feel emboldened rather than reasons why the form was initially adopted, they are still indicative of asymmetric information problems. Founders are essentially unsure of how mission-driven their shareholders are willing to be, so there is a certain level of discomfort with pushing the mission too hard. Such a move might generate unwanted tension, so

founders err on the side of caution. However, with the legal backing behind them and their shareholders' consent, the "air is cleared"; founders have revealed more information about their investors. If founders have converted after accepting outside capital, they are revealing more information about their current shareholders as they go through the process of gaining shareholder consent, and also—as we are about to see—are setting the stage to reveal more information about possible future investors.

2. *Investor Uncertainty*

The second step in this argument is showing that the benefit corporation is characterized by uncertainty in the investment community and that this is enough to turn some investors off. If investor decisions were not affected whatsoever by the benefit corporation form, it would be an insufficient screen. Recall this segment of the argument: If there is uncertainty around the benefit corporation form, and investors tend to shy away from uncertainty, then we can expect investors to stay away from it unless (a) they care to some degree about the mission or (b) they do not think that the form matters. However, they are unlikely to invest solely on the basis of (b) because of the robust board approval necessary for certain decisions, which raises doubts about their primacy. To substantiate this line of reasoning we need evidence of the following: that there is uncertainty, that this uncertainty is enough to "weed out" certain investors, and that investors are unlikely to think that the form does not matter. If we can illustrate all of these things, the argument for benefit corporations as a screen will come into focus.

As discussed earlier, the existing benefit corporation literature illustrates the uncertainty around the form within the legal community. The participants in this study

expressed little doubt that the benefit corporation is, at present, not well-understood within the investment community, either.

“The other traditional investors, they just didn’t know about it. So, I had to explain what it was and tell them that my attorney wasn’t worried” (Participant B 2017).

“I have had conversations with people who are investing with us, who say this is something that is very appealing to them. But I don’t know that on a broader level there is a lot of understanding what it is...it could definitely use sort of a push forward on a more traditional and institutional investor level” (Participant D 2017).

“There was maybe a lack of understanding with a lot of our shareholders. And that’s pretty endemic to the Wall Street environment. They don’t understand PBCs at all” (Participant G 2017).

“If you’re speaking with a traditional CPG investor, a tech investor—they may not even know about it. Not too many people know about it” (Participant J 2017).

“We were the first [omitted] to convince major early-stage funds that we should become a public benefit corporation. And, in fact, our outside counsel—who we relied on and still rely on for legal advice but also for understanding the funding market—said, ‘You guys, I’m not sure you want to touch this. I’m not sure you’re going to get the response you want. And I’m not sure they are going to invest in your next round if you do’” (Participant H 2017).

All of these quotes indicate some degree of uncertainty on behalf of investors, but to illustrate the benefit corporation’s effectiveness as a screen, we have to show that it “forces the buyer’s hand.” In other words, that it forces the buyer to reveal some deeply held preference that otherwise he or she wouldn’t have. Several participants indicated experiences along these lines when asked if they felt that being a benefit corporation turned off any investors.

“I’m sure [it has turned off some investors], but those investors we don’t want to be with. But absolutely, I’m sure it has. And I think when people don’t know, or people think you’re doing something outside of a profit motive, it probably scares them. It doesn’t scare me, I wasn’t raised that way, and I don’t want to be so-called in bed with those people” (Participant J 2017).

“It’s challenging when your solution is a finance solution. The people that you’re dealing with primarily are Wall Street types or finance types. And the folks [in those fields] who care are few and far between...so it is difficult to find like-minded investors for the business. You have to kiss more frogs—that’s the answer. They have to be like-minded and they have to understand the business, and oftentimes it is difficult to find investors who believe we can actually do what we are doing” (Participant G 2017).

“[Recent rounds] have been predominantly impact investors, actually. I talked to people who weren’t, and it may have scared off a couple of investors but I’m like, ‘Good riddance, you aren’t going to like me anyway if that little bit scares you off’” (Participant B 2017).

These social entrepreneurs engaged in talks with investors who were interested in their business, but who were eventually put off by, to some extent, the benefit corporation status. Although we cannot say with certainty, it is possible that some of these investors would have wanted to invest, all else equal, if the business had not been registered as a benefit corporation. In this way, hidden information about them was revealed.

The final piece of the argument is showing that those who decided to invest did so because they were more open to making the trade-offs that come along with a strongly mission-driven enterprise, and not because they thought the legal form would prove irrelevant. Justification for this claim is derived from the legal structure itself.

For venture capitalists, exits are all that matter (see *e.g.* Cumming and MacIntosh 2003; Sahlman 1990; Gompers and Lerner 1999)—and it is in exit scenarios that the benefit corporation induces the most uncertainty, particularly in the context of a sale. The Model Benefit Corporation Legislation requires a “minimum status vote”—typically two-thirds of shareholders eligible to vote—in order to amend the articles of incorporation, abandon the benefit corporation status, or approve a merger or reorganization that would terminate the benefit corporation status (Robson 2015). Given the robust voting approval necessary to either convert away from a benefit corporation or to approve a sale to a non-benefit corporation, investors who are purely profit-maximizing are likely to be uncertain about how such situations will play out. Indeed, the legal literature, as discussed earlier, has illustrated that what benefit corporation statutes might do most effectively is clarify explicitly that, even in the case of a sale, a benefit corporation need not seek to *only* maximize shareholder payout. Potential investors who are not particularly interested in mission preservation may be said to suffer from a problem of asymmetric information, as well, where the missing information is the degree of social commitment of other shareholders. Facing such a problem of information asymmetry, investors who are not interested in long-term mission preservation are unlikely to invest under the assumption that the benefit corporation form will not matter.

D. Conclusion

In this chapter, I have shown the following:

- (1) Social entrepreneurs face an information asymmetry problem, where the missing information is the degree of social commitment of an investor;
- (2) That the benefit corporation is characterized by uncertainty;
- (3) That this uncertainty is enough to turn some investors off; and,
- (4) That some investors, facing uncertainty, are unlikely to invest under the assumption that the benefit corporation form is irrelevant.

From this, it follows that those investors who *do* decide to invest are more likely to care, to some degree, about the mission. It is in this way that the benefit corporation acts as a screen, thus helping social entrepreneurs better find long-term alignment.

The corollary of this argument, of course, is that being a benefit corporation might make fundraising with traditional investors more difficult. Even in a relatively small group of interview participants, several founders felt that being a benefit corporation pushed some investors away. In theory, this means a smaller pool of willing investors, which increases the effort and amount of time needed to complete a funding round. On the other hand, it may make securing investment from impact investors more likely, though this study is unable to comment on the extent to which it might do this or whether this makes for an easier process overall.

A couple further clarifications are in order. Again, this argument is premised on the assumption that the social entrepreneur *wants* to find mission alignment and s/he is committed to long-term mission preservation. This is by no means the case for all benefit corporation founders. Furthermore, how well the benefit corporation functions as a screen is a matter of degrees. It does not ensure that any and all investors will have the same priorities, nor does it guarantee all investors will share similar emphasis on the mission. Social

entrepreneurs, especially those in closely-held private companies—which all of the companies in this study are—still need to evaluate their investors across a range of categories and carefully select them from the earliest stage. Being a benefit corporation can help a social entrepreneur dig a bit deeper and reveal information about an investor that may not have otherwise been exposed until later in their relationship, but it is certainly cannot do this on its own.

III. INTERNAL ACCOUNTABILITY IN BENEFIT CORPORATIONS & B CORPS

By now, it should be obvious that accountability is a crucial feature of the benefit corporation; without an adequate mechanism to keep companies aligned with their stated values and missions, the legislation’s efforts to reform corporate behavior will likely prove futile. To this end, the mechanism that has been legally built into the entity follows what Briana Cummings calls a “transparency-based accountability model”—one that relies heavily on various levels of disclosure, either to the third-party standard-setter, as discussed earlier, or to the public via the annual benefit report (Cummings 2012, 580).³³ She argues, however, that this is the wrong approach for corporations pursuing a social purpose. For such pursuits, these methods might not only be ineffective, they may actually be detrimental.

In response to these concerns, which are discussed in detail below, she suggests that it is the “addition of bottom-up horizontal mechanisms for ‘mission accountability’ [that] may help foster the capacity and internal motivation necessary for benefit corporations to achieve their public benefit obligations” (Cummings 2012, 578). The question we should be asking,

³³ Recall, also, that for Public Benefit Corporations (i.e. those registered in Delaware), annual reports must only be disclosed to shareholders and disclosing to the public is optional.

then, is does being a benefit corporation aid in, or make more likely, the creation of such an internal accountability mechanism? This chapter is devoted to exploring this question in light of this study's interviews and Cummings' article, which has become an oft-cited piece of the literature.

It should be noted that Briana Cummings centers much of her argument around B Lab—which, again, is the entity that certifies B Corps. Benefit corporations, if they so desire, need not have *any* affiliation with B Lab. She uses B Lab as an example because they are the most prominent and visible third-party standard setter, but only companies that wish to be certified by them are subject to their audits. However, due to the prevalence of certified B Corps in this study's sample, as well as the centrality of B Lab to her analysis, this chapter deals extensively with B Corps. In fact, I argue that being a benefit corporation does very little in terms of influencing behavior and cultivating internal accountability, but that being a B Corp does.

In the first part, I outline the main features of Cummings' argument, which concludes with suggesting that we should reconceptualize three aspects of benefit corporation accountability: (1) the assessment, (2) the role of the third-party auditor, and (3) the incentive for complying.

In the second part, I use examples from this study's participants to argue that—despite Cummings' theoretical and juridical reading of how benefit corporations and B Corps are likely to function—B Lab in many ways currently embodies her first two “reconceptualizations.” In all fairness, Cummings' article was published in 2012, just two years after the first benefit corporation legislation was signed and just five years after the first

B Corp was certified, so my intention here is to essentially “check in” on progress and point out the ways in which her vision is being realized.

The third part expands on this by discussing her third pillar of reform—the incentive—and simultaneously advancing an argument for how being a B Corp may make all three of these reconceptualizations more likely. I argue that being a B Corp acts as a signal during the hiring process and, when combined with an effective screen, helps companies create a more values-aligned workforce, thus aiding in the creation of bottom-up internal accountability mechanisms.

A. The Argument for Bottom-up Horizontal Accountability

The accountability mechanism built into the benefit corporation arose out of a trend towards increased transparency in the U.S. corporate arena. The reliance on transparency to quell the bad behavior of society’s organizations has its roots in the securities laws that arose out of the 1929 stock market crash (Sulkowski and White 2010). In the last few decades, it has been reinforced by the “palpable public demand” for greater transparency that resulted from the accounting scandals of the 1990s and the economic collapse in 2008, and has been legally strengthened through legislation like the Sarbanes-Oxley Act in 2002 and several others that followed (Langevoort 2005, 965; Cummings 2012). Similarly, as mentioned in Chapter I, transparency in corporate behavior owes much of its prominence to the labor movements of the 1990s, in which activists pushed back against the use of sweatshops in manufacturing chains. Such movements were merely one example of the attempts to transfer this trend of increased disclosure and reporting over to areas of social and environmental accountability—which is precisely what the benefit corporation appears to be trying to do (Cummings 2012).

1. *Problems with the Current Accountability Structure*

The benefit corporation follows a model that has been termed SAAR—social auditing, accounting, and reporting—the major components of which are (1) “verification by third party auditors”; (2) “an annual, publicly disclosed report”; (3) an incentive mechanism (Hess 2001; Cummings 2012). Briana Cummings suggests that the SAAR “embodied in the benefit corporation legislation relies not just on (1) third-party audits and (2) public disclosure, but also on two additional pieces: (3) performance-based sanctions tied to market pressure and (4) ‘objective,’ standardized, and quantitative performance metrics” (Cummings 2012, 599).³⁴ In addition to joining other critics in questioning whether the market can adequately impose accountability-enforcing sanctions, Cummings argues that this approach is particularly ill-suited for “achieving meaningful accountability to mission” and that “because there are important distinctions between a social bottom line and a financial bottom line, the benefit corporation legislation misconceives both for what and to whom benefit corporations should be held accountable” (Cummings 2012, 603).

Regarding *for what* benefit corporations should be held accountable, Cummings sees two problematic mismatches. The first stems from the relatively short-term quantitative processes intended to measure the performance of a social goal, which is inherently long-term and notoriously difficult to quantify, not to mention constantly changing (Cummings 2012). Reducing performance to quantifiable targets misses quite a bit of critical information. The methods used and the data collected determine what can be measured; what, then, is a benefit corporation ultimately holding itself accountable for if its methods and data do not

³⁴ This statement should be qualified. Benefit corporations are not subject to audits unless they are also B Corps, or some other certified entity that utilized audits. See note 34, as well.

allow for an intimate assessment of its stated social ends? The second mismatch results from the apparently “value-neutral” standards that benefit corporations are held to, supposedly allowing them to value all stakeholders at once, despite the fact that their missions are value-laden (Cummings 2012). The legislation does not acknowledge that measuring performance for one stakeholder group can be entirely different than how it should be measured for another. Oftentimes, stakeholders have competing interests or differences in opinion on how a certain goal should be achieved; by giving no indication of how to prioritize groups, benefit corporation legislation “trivializes possible conflicts among them” (Cummings 2012, 606). These conflicts may be merely interpersonal, or sometimes they may even represent competing missions—so, for which goals should the benefit corporation be held accountable?

Benefit corporation legislation also confuses *to whom* such entities should be held accountable. Its framework for enforcing its accountability mandates includes three broad categories of actors: shareholders and directors (who can sue), the independent third-party standard-setter (who can withhold certification), and the public (who, acting in response to the corporation’s behavior, can abandon them as a customer) (Cummings 2012).³⁵ But the legislation appears to leave out an explicit framework for holding the corporation accountable to what are arguably its two most crucial constituencies: (1) “the more targeted beneficiaries of corporation’s ‘specific public benefit’ and (2) the employees of the corporation” (Cummings 2012, 613). Cummings argues that those who are supposedly most affected by the company’s specific public benefit pursuits have a “greater moral claim...to be

³⁵ Again, although Cummings states the legislation “gives an independent third-party auditor the power to grant or withhold certification,” this is not necessarily true (see Model Benefit Corporation Legislation § 401: 929-931). If a benefit corporation is seeking to become or has already become a B Corp or another type of certified entity, then this is true; however, benefit corporations do not *need* to be audited or certified (See <http://benefitcorp.net/faq>). Furthermore, Public Benefit Corporations need not even make their report public.

involved in defining standards of performance” (Cummings 2012, 609). More practically, these constituencies also may be able to more effectively set standards of performance, since they are closer to the problems and the implementation of the intended solutions. It is somewhat puzzling that the only stakeholders who the legislation explicitly includes in the accountability process are those who are furthest away from the mission—those who are “outsiders”: courts, shareholders, certifying organizations, and the diffuse public (Cummings 2012, 610).

The benefit corporation, in other words, strictly employs methods of “upward” accountability, effectively ignoring internal and “downward” mechanisms and, as Cummings and others argue, possibly even interfering with them. Exclusively relying on upward mechanisms can hinder accountability to oneself and to colleagues in two ways (Cummings 2012; Broadfoot 1996). It may not only undermine the service deliverers’ ability to define their own mission, but it also may—once the mission is defined—undermine their ability to achieve it (Cummings 2012; Sugin 2007). As she shows through examples in the healthcare and education sectors, market-based sanctions tend to actually hinder the free flow of information and “impede innovation and adaptation” rather than promote it (Cummings 2012, 612; O’Day 2002). For an organization seeking to serve a triple bottom line, this is a particularly problematic structure:

To the extent that combining disclosure requirements with performance-based sanctions does in fact encourage organizations to suppress information, focus on short-term results, and do the minimum necessary to comply with external requirements, they work to the detriment of the intended beneficiaries (“stakeholders”) of a social project. Adding quantitative performance measures into the mix adds another wrinkle (Cummings 2012, 612).

This additional “wrinkle” goes back to the previous comments about quantitative measurements; when reporting standards, like B Lab’s, are “focused on easily quantifiable, short-term results, they discourage the pursuit of goals that are less easily quantified or that are not measured at all” (Cummings 2012, 612). Such measurements not only miss the most important information, they may also shift the priorities of the organization away from its long-term goals and more towards meeting more short-term baseline expectations.

Cummings’ indictment of the benefit corporation accountability mechanism is justified. The legislation does not create a proper role for the stakeholders who are most important to the successful delivery of a social mission, and in many ways, it can actively work against them. In short, benefit corporations need to be more introspective; for social ventures that are deeply dedicated to mission achievement, reliance on external mechanisms could very well lead them astray.

2. An Alternative Approach to Accountability

In response to these shortcomings, Cummings advocates for an alternative approach to accountability that redefines both for what and to whom benefit corporations should be accountable. In applying this new approach, she argues that three primary areas need to be “reconceptualized”: the assessment, the role of the external auditor, and the incentive.

Rethinking “For What” and “To Whom”

Instead of holding themselves accountable for achieving rigidly defined results and procedures, Cummings suggests that benefit corporations should adopt an “adaptive learning” framework—one that is “concerned with assessing, first and foremost, an organization’s capacity for organizational learning” (Cummings 2012, 614; Ebrahim,

Battilana, and Mair 2014). Under such a model, organizations are not only held accountable to their fixed results and procedures, but also for (1) “establishing and following processes for defining what those results and procedures should be and how they should be measured” and (2) “continuously adapting organizational efforts to achieve them” (Cummings 2012, 615). This framework suggests that processes and adaptations are ends in and of themselves, not merely means of attaining some previously identified goal or satisfying some generic external standard. Indeed, the very nature of social goals requires that this be the case; determining how to best achieve social goals and measuring progress towards them are notoriously elusive projects. Thus, organizations seeking success in this arena need “enough flexibility so that resources can be deployed away from social missions that are ineffective or no longer necessary” (Katz and Page 2010, 92-93; Cummings 2012).

Under Cummings’ approach, effectively restructuring to whom benefit corporations should be accountable requires creating room for three additional groups: the corporation itself, its professional peers, and its intended beneficiaries (Cummings 2012). Cummings joins Alnoor Ebrahim in suggesting that external accountability must have an internal counterpart, one that is motivated by “felt responsibility”; otherwise, any external mechanism is unlikely to be successful (Ebrahim 2010, 3; Cummings 2012, 617). In addition to a company’s internal accountability, though, they also derive a sense of responsibility from their professional network. Cummings notes scholars as far back as Émile Durkheim, who developed a theory of “moral conduct...grounded in...networks of professional and personal ties” (Furger 1997, 447; Cummings 2012, 618; Durkheim 2014). Such networks are better not only for preserving intrinsic motivation, but also for developing the best metrics of performance and for promoting adaptive learning (Cummings 2012). Lastly, but certainly not

least, any accountability framework must foster accountability to those whom the corporation seeks to benefit.

Institutionalizing New Notions of “For What” and “To Whom”

It is to embed these new notions of “for what” and “to whom” that Cummings advocates for reconceptualizing the assessment, the role of the third-party auditor, and the incentive. To illustrate how the current system falls short in these three categories, she refers primarily to B Lab and its certification processes.

The assessment, she says, should become more of a “formative evaluation,” rather than a summative one (Cummings 2012). The former focuses more on improving practices: “[R]ather than asking, ‘Are you doing X?,’ formative evaluation asks, ‘Is X working?’ and, if you are not doing X, ‘How can you be helped to do X?’” (Cummings 2012, 620) B Lab’s assessment measures how a company has performed relative to preset benchmarks, but it does not give sufficient attention to *why* a company has underperformed or how it can improve (Cummings 2012). To be clear, she does not argue that summative evaluations are entirely useless, just that in order to be effective, they should (1) not be tied to sanctions, (2) not rely exclusively on quantitative metrics, and (3) be complemented by formative evaluation (Cummings 2012).

A new-and-improved role for the third-party auditor would be that of both an institutional intermediary and an “organizational catalyst.” By acting as such, the auditor “could foster more flexible adaptation to professionally developed industry-specific standards,” rather than merely enforce externally-developed standards (Cummings 2012, 621). According to Cummings, an institutional intermediary is unlike B Lab in three key

ways: (1) instead of checking compliance, it encourages the industry to put its own internal systems in place; (2) it fosters professional accountability by pooling knowledge between members of an industry; and, (3) it asks not just about previous performance, but also vision, difficulties, possible solutions, and self-evaluations (Cummings 2012, 622). In short, it prompts organizations to adopt a more active and reflective attitude about their own accountability. The third-party auditor can become more effective also by becoming an “organizational catalyst” through partnering the external regulator with individuals in the organization (Cummings 2012). These individuals “mobilize change by developing experiments, analyzing their effects, and reporting on them to the external regulator” and act as the primary contact for those who wish to come forward with problems (Sturm 2006; Cummings 2012, 624–25). In both of these ways, the third-party auditor could more effectively contribute to fostering adaptive learning within benefit corporations.

The third element that Cummings feels should be restructured is the incentive. The desire to avoid externally-imposed sanctions as an effective incentive for increased performance has scant empirical backing and, at present, is little more than a “presumption backed by common sense” (King and Lenox 2000, 700; Cummings 2012, 624). Cummings’ suggestion for reconceptualizing the incentive is worth quoting at length:

As a substitute for external sanctions, incentives are needed that can reduce the risks and increase the rewards associated with identifying problems, gathering data, and engaging in regular self-evaluation; that can increase the motivation deriving from a sense of personal responsibility and adherence to professional expectations; and that can, at the same time, effectively deter irresponsible conduct (Cummings 2012, 626).

She suggests that intrinsic motivation and “informal social regulation” might be mechanisms through which this sort of incentive can be cultivated. Regarding the latter, she cites Renée de Nevers, who argues that peer pressure and shaming—or “management by embarrassment”—“can often push companies to adhere to normative standards” (Nevers 2010, 224). Regardless, Cummings says, “the key is to decouple the lethal combination of sanctions and external standards” (Cummings 2012, 626). To be clear, Cummings does not think that sanctions are entirely useless—certainly they have a role to play—she just believes that tying them to self-reported quantitative metrics produces perverse incentives.

3. Conclusion

This section has explored Briana Cummings’ argument for more bottom-up, horizontal accountability structures within benefit corporations. I started by outlining why she believes that the currently legislated accountability mechanisms are unlikely to be successful and how, in many ways, they may even undermine companies’ social pursuits. Then, I detailed her alternative approach to accountability, which is designed to foster “adaptive learning” processes and can be achieved by reconceptualizing three key aspects of accountability. She concludes her argument with the following:

[A]ccountability for benefit corporations should rely more heavily on bottom-up development of explicitly subjective standards, developed jointly by the organization itself, the industry as a whole, and key stakeholders, and backed by internal and professional sources of accountability. Such an accountability model would focus on measurement not just of fixed inputs or procedures, but also of structure and practices that foster adaptive learning; and it would rely on external regulators to fill a more capacity-building rather than compliance-driven role (Cummings 2012, 627).

Ultimately, Cummings is right. Her argument is captured quite nicely by one of this study's participants:

“I just had this conversation with someone yesterday, the sort of cost-benefit around using the B Impact Assessment. The benefit is it's a third-party and it provides some kind of quality control from being assessed around a common set of standards. The cost of that, is we could be recycling the hell out of things and even offering good family leave and doing all sorts of nice things for our employees, and we could still be a predatory for-profit [omitted] company, and there would be no control for that provided in the assessment if none of the questions are tailored to our tiny little area of the industry. And I think that is just generally a concern in the B community, is how do you control for that? It is typically at the margins of what is your specific industry that a true benefit or lack of benefit can be assessed, and there is no way that B Lab is in a position to put together 30,000 different assessments. But we think about that a lot and how to make sure that we have internal control for our particular public benefit”

(Participant H 2017).

The challenge, of course, is how to legislate the sort of “internal control” talked about here. It is not clear how effectively, if at all, this can be made into enforceable law—something that companies can be forced to do. What is promising about this quote, coming from one of the “B” community's “flagship” companies, is that it at least indicates that the community is grappling seriously with the accountability issue. The big question is—for companies truly dedicated to achieving mission success—does being a benefit corporation or a B Corp (or both) make the creation of a strong internal accountability mechanism any easier or more likely? Cummings does not seem to think so.

The rest of this chapter is dedicated to exploring this question. The next section provides some examples of the ways in which Cummings' alternative approach is already

being realized, based on the interviews conducted as part of this study, and considers to what degree being a benefit corporation or a B Corp aided in the creation of these internal systems.

B. Current State of Accountability in B Corps: The Assessment and the Third-Party Auditor

Before going any further, it is necessary to delineate the two different types of accountability at issue in this discussion: what we might call day-to-day accountability and mission accountability. The former deals with the more generally applicable standards of operation that are the primary focus of B Lab's assessments—things like recycling practices, employee benefits, regular information sharing, volunteering policies, etc. The latter deals with the much blurrier and notoriously difficult task of keeping oneself properly focused on a mission that is simultaneously much larger and more specific. In other words, one that represents a grand vision for solving a particular problem. Again, the difference between these two is illustrated clearly in the quote on the previous page.

Cummings does not draw an explicit distinction here, but it appears that her main argument is that the current benefit corporation framework is not adequately suited toward *mission* accountability and, furthermore, that the nature of B Lab does not help get us much closer. To put it differently: B Lab, by focusing on the measurement of day-to-day accountability using quantitative metrics, falls short of ensuring and encouraging mission accountability.

The rest of this chapter deals exclusively with the impact of being a B Corp on both types of accountability. This is in part because my sample only includes two companies that are benefit corporations and not B Corps, but also because many interviewees indicated that

they do not feel that being a benefit corporation has changed the way they behave. It is, more than anything else, a way of cementing values that would have driven the organization regardless of its legal status:

“I do think we would be doing a lot of what we are doing anyway just by virtue of our personal values” (Participant C 2017).

“No, [it hasn’t pushed me to do more than I otherwise would] because I am personally pretty freaking extreme on the mission side” (Participant B 2017).

“You know, because it is inherent in what we do and who we are, I don’t think things have shifted tremendously...I think that, as a matter of how it has changed our company practices, we were already there” (Participant D 2017).

“It hasn’t had any impact. We were going to have a company that did well and did good no matter what” (Participant J 2017).

“I don’t think that [decision] would have been any different had we not been a benefit corporation. That said, we are a benefit corporation because it is who we are. And maybe that is all just part and parcel” (Participant H 2017).

The same cannot be said for being a B Corp, however, which appears to be quite influential in establishing practices that otherwise may not be a part of the company:

“[T]he audit process, it forces us to ask questions that we might not have asked. It forces us to ask those questions again and again over a period of time. It gives us an opportunity to compare ourselves and learn from what other people are doing. And every time we have done the audit we have come across a question that says, I don’t know, ‘Do you offer paternity leave as well as maternity leave?’ And I go, ‘Darn it, I don’t think we do, but we ought to. I mean that’s easy. So let’s get that in the handbook.’ Or, you know, ‘Do you discuss financial

results with all of your employees once or twice a quarter? Well, we haven't done that so regularly but maybe we should now.' And then we did" (Participant A 2017).

"The certification and recertification has definitely helped to keep us accountable. And going through that process every two years definitely makes sure that are not just slapping a label on it and calling it a day...it has, in certain circumstances, given us a little extra push to do something, you know, like a major recycling competition instead of just recycling" (Participant C 2017).

"Every two years when we do the assessment, it's always a check. I'm like, 'Alright, we got to clear the hurdle again.' And it does enter into—because we have been through it twice—we kind of know the things we have to keep an eye on. So, one of my things I'd like to get done in the next 12-18 months is go visit our suppliers. I go to some of them, but I'd like to go visit more of them, because I know that will come up on the assessment" (Participant K 2017).

"It's a great process. We scored really, really high but we still saw areas where we were like, "Oh, we could be doing this, and we should be doing this" (Participant D 2017).

"Basically, you'll look at the score on B Lab and in any area we aren't killing it, we don't feel good about that. So, we dig in deeper and try to rectify that wherever we can. And I think it is really important to have the outside eye on what you're doing. Because sometimes you get stuck on what you're doing that you don't even notice your failures. It is a reflection for sure, and then actions follow that because we care" (Participant J 2017).

"Every year we use the assessment to renew and come up with new ideas to address. Whether it be—I'll give you an example. With the whistleblower policy, it is something we don't have but something we have looked at. Flexible work options are something we looked at. I am just picking random things. So, what we do is we will go through the assessment and we will come back and look at the certain sectors—I don't know how familiar you are with the assessment—you have governance, community, environment, workers, etc. And we will go in

and see what are some things we can talk about and maybe make some changes. I'll give you another example. We never did an employee engagement survey. We did that last year. This year B Corp issued a diversity and inclusion challenge. We did not officially partake in it—but because of it, we are going to be going through unconscious bias training in a couple weeks” (Participant F 2017).

Most of these quotes are indicative of the sort of top-down, external compliance mechanism Cummings believes either fails to facilitate adaptive learning or even undermines it. Where Cummings’ argument falls short, though, is that she seems to assume that this is all B Lab does—they ask whether a company is complying, the company answers, and then they both move on and maybe some changes result. But this does not appear to be what is going on; B Lab embodies her “reconceptualizations” far more than she gives them credit for.

1. B Impact Assessment as a Formative Assessment

In terms of shifting the assessment from a summative one (“Are you doing X?”) to more of a formative one (“How is X working?” or “If you aren’t doing X, how can you be helped to do X?”), B Lab may not explicitly frame the questions this way, but it does seem to have the same effect. It is not the case that these companies answer the questions and, as long as they receive a passing score, move on; many of them do show a real willingness to improve for the sake of improving. The assessment prompts the sort of change and reflection that Cummings feels a summative assessment lacks. At least in these cases, the companies seem to be undergoing their own formative assessments—either by taking what they have learned from the audit process and “digging in deeper” or by combining the assessment with some sort of experimentation. For example:

“At various points we have tried to figure out different staffing models. And some of those models had quite a lot more part time work, and therefore folks would not have had our full-time benefits and would not have had equity in the company. But I do believe that the fact that there is a significant portion of the questionnaire that is devoted to employees being equally protected, has helped keep us on the track of prioritizing that” (Participant H 2017).

“We have gotten more out of the certification than, honestly, I anticipated we would have. It gives you ideas. One thing we are doing now that came out of the assessment is paid volunteer time off. We will take full days off for all our 140 employees to go out into the community. And now we have a separate group with an annual budget that takes internal and external donation requests and they are also in charge of drumming up community action on our behalf. That came out of the assessment” (Participant L 2017).

“We use the assessment as a roadmap to better ourselves...We started off and what we did was create three committees that I kind of say are our building blocks. They are all manned by volunteers from the employee workforce. And the membership changes every couple of years—there is a rotation so it doesn’t get stagnant. The three committees are environment, governance, and social/charitable. Each committee has its own responsibilities in harmony and cooperation with what B Corp is trying to do...so we used that and that’s how we started...being a B Corp directly impacted how we set up those committees” (Participant F 2017).

Consider also this quote from Richard Stammer, a senior executive vice president at Cabot, who wrote a Harvard Business Review article about his experience as a B Corp:

At Cabot, B Corp certification inspires Cabot to constantly innovate to create even more social and environmental benefits while simultaneously boosting our B Corp score and was integral to projects like Real Farm Power, a closed-loop system that leverages partnerships to deliver renewable energy, nutrient management and improved air quality. Now, after three

years of operation, Real Farm Power generates enough electricity so that cows in our cooperative provide the electricity needed to churn our butter. (Stammer 2016).

These quotes are indicative of more reflective formative assessment processes—the type that is more likely to facilitate an adaptive learning environment that will not only ensure compliance with day-to-day accountability but is also better suited for ensuring mission accountability. Again, the question to ask here is to what extent being a B Corp led to the creation of these processes. To shed light on this, it helps to understand the extent to which B Lab already embodies Cummings’ suggested role for the third-party auditor and how it already impacts the creation of her reconceived incentive.

2. B Lab as Institutional Intermediary and an Organizational Catalyst

Briana Cummings argues that the third-party auditor should take on the roles of an institutional intermediary and an organizational catalyst. She suggests that institutional intermediaries are unlike B Lab in three key ways: (1) instead of checking compliance, they encourage the industry to put its own internal systems in place; (2) they foster professional accountability by pooling knowledge between members of an industry; and, (3) they ask not just about previous performance, but also vision, difficulties, possible solutions, and self-evaluations (Cummings 2012). Remember, the purpose of this new role is to change “for what” and “to whom” the company is accountable. Points (1) and (2) make a company more accountable to its professional peers, and point (3) makes it accountable for engaging in reflective processes rather than for meeting externally-prescribed quantifiable standards.

While not necessarily industry-specific, B Lab certainly does facilitate collaboration and the pooling of knowledge. Sometimes this collaboration happens within an industry, and B Lab does allow B Corps to be filtered by industry on their website. Additionally, the

annual ‘Champions Retreat’ is worthy of mention here, as well. The last retreat, which took place in Toronto in October 2017, welcomed over 550 B Corp members for “three exciting days of collaboration, movement building and celebration.”³⁶ Testimonials from previous attendees all illustrate the collaborative atmosphere.³⁷ Similarly, the 2017 Champions Retreat for the Australia and New Zealand region was centered around the question, “What can we do together that we can’t do apart?”³⁸ B Lab does strive to cultivate a community, not merely a trusted certification, and their members certainly feel it:

“They share with us a lot of their information that we think is useful...and as a member of the community I feel very supported. I feel like they are accessible and available...It is absolutely a collaborative environment” (Participant A 2017).

“Someone being a B Corp is saying that you do the things you say you’re doing and being transparent about it, but a lot of it is just saying, ‘I’m this company in this industry doing this myself, and I want to be aligned with other similar companies putting mission into profit. And I want to use business as a force for good with others because combined we can make a difference, like make the law change. And I want to commiserate, and work with, and collaborate with other companies.’ So, for me that sense of community was really important across multiple businesses—building community both locally and nationally. I went to the very first B Corp retreat with like 40 people, and I’ve been to a lot. I’ve only missed one in 10 years” (Participant M 2018).

“We are more than happy and very pleased to support the B Corp community locally, and then we also try to get to the Champions Retreat. We also go to the B Corp Leadership Development conferences” (Participant K 2017).

³⁶ B Lab. “B Corp Champions Retreat.” www.champions-retreat.bcorporation.net/ (accessed April 19, 2018).

³⁷ B Lab. “Champions Retreat.” Bcorporation.net. www.bcorporation.net/become-a-b-corp/why-become-a-b-corp/champions-retreat (accessed April 19, 2018).

³⁸ B Lab. “Champions Retreat Alice Springs 2017.” Bcorporation.com.au. <http://bcorporation.com.au/blog/champions-retreat-alice-springs-2017> (accessed April 19, 2018).

What’s more—and this happened after Cummings’ writing—B Lab now allows companies to add “Thematic and Industry Data” to their assessments, which according to their website are “focused metric sets based on frequently cited impact themes and industries.”³⁹ These data sets not only make the assessments more industry-specific, but also demonstrate that B Lab is working to aggregate industry concerns and suggestions in a way that can be helpful to all the firms within it, thus strengthening its role as an institutional intermediary.

It is important to realize that all of the statements above are made either by CEOs or high-level executives, which contributes to how well we can conceive of B Lab as already taking on the role of an organizational catalyst. Recall:

‘[O]rganizational catalysts’ are ideally individuals who know the culture of the organization being regulated and, critically, possess ‘clout’ in the organization—that is, someone with high status, high social and intellectual capital, sufficient resources, ‘direct lines of communication...[to] chief executives,’ and who is otherwise strategically placed within the organization to mobilize learning and change by communicating with peers in their cultural/professional language...[They] mobilize change by developing experiments, analyzing their effects, and reporting on them to the external auditor (Cummings 2012, 624 citing Hopkins 2007).

How well does B Lab already serve this role? Consider the ways in which internal experiments and practices already make, or are planning to make, their way back to B Lab and its community:

“Being a part of this community and having a voice in this community, it allows us to do a lot of what we were already doing, but on a much larger scale. So, the audience that we can speak to—you know, we have taken what we consider to be pretty innovative workplace practices

³⁹ B Lab. “Thematic and Industry Data.” B-analytics.net. <http://b-analytics.net/content/thematic-industry-data> (accessed April 23, 2018).

and have taken them outside and spread them to other businesses. And now those employees can be impacted and helped the way ours have been. So, you know, once we are a part of this community, we can reach a much larger audience” (Participant L 2017).

And, this, from one of the first institutions of its kind to become a B Corp:

“We are in contact with B Lab. We are part of the sort of ‘B Hive’ community. We have a ‘B-Keeper’ who is on my team, and she interacts with them quite a bit” (Participant D 2017).

Again, showing at least the desire for a back-and-forth with B Lab regarding more mission-specific qualitative measurements:

“We would love to start asking for their help in regularly measuring impact the way we measure impact. Which is, how, what kinds of influence has our technology had on violence in institutions? How effective has it been at saving taxpayer dollars? And, most importantly, what evidence do we have to suggest that it is delivering better outcomes for people?” (Participant A 2017).

Of course, it is not the case with every B Corp that they engage in, or have a desire to engage in, a heavily collaborative relationship with B Lab. Perhaps this is where Cummings’ argument derives its strength; the auditor should go further to *require* more collaboration. Attendance at the retreat is not mandatory. Communication with B Lab outside of assessment periods is not mandatory. B Corps can, and many times do, get away with doing the absolute minimum. Companies must *want* to perform well in order for B Lab to foster the sorts of internal and horizontal accountability Cummings seeks. However, even if an initial commitment tapers off, being a B Corp still might hold an internal accountability mechanism in place.

C. Signaling, Screening, and the Improved Accountability Incentive

Recall that intrinsic motivation and “informal social regulation” are two mechanisms through which Cummings believes a new-and-improved compliance incentive might be created. Such an incentive “reduce[s] the risks and increase[s] the rewards associated with identifying problems, gathering data, and engaging in regular self-evaluation” and “can increase the motivation deriving from a sense of personal responsibility and adherence to professional expectations” (Cummings 2012, 626).

By returning to signaling and screening theory and applying it to the hiring process, we can better understand how the B Corp might impact the creation of this new-and-improved compliance incentive. The argument here follows the same general arc as the argument from the previous chapter. From both sides—employer and potential employee—there must be reason to believe there is an information asymmetry problem. The social entrepreneur wants employees who are deeply committed to the social goals of the company, and the values-driven employee want to work for a company that embodies his or her values. Neither side can ever know for sure the other party’s degree of commitment. To help reveal more information, the social entrepreneur must send a costly signal while simultaneously employing a screen that is costly to a potential employee. How does being a B Corp impact this matchmaking process and how might it impact future internal accountability?

1. The B Corp as a Signal

What would it mean for the B Corp to be an effective signal to values-driven job seekers? The B Corp would have to credibly communicate to job seekers some information

about the firm that they were previously lacking. We will assume that social entrepreneurs want values-aligned employees and that such employees exist on a spectrum—some care very little about values-alignment, others care a lot. Those who care a lot are seeking as much information as possible about the firms at which they might work, and the social entrepreneur has an incentive to figure out a way to attract them.

Timothy Judge and Robert Bretz, Jr. from Cornell University, in a study on the effects of work values on job choices, found that “individual value orientations have an important influence on job seekers’ decisions when information about organizational value systems are known” (Judge and Bretz, Jr. 1991, 21). Organizations seeking values fit, then, want to get this information into the hands of job seekers. Researchers have also focused on the nexus of corporate social performance (CSP) and recruitment. Several studies have indicated that companies with stronger CSP tend to be more attractive to potential employees (Aiman-Smith, Bauer, and Cable 2001; Kim and Park 2011; Luce, Barber, and Hillman 2001). Furthermore, others suggest that by attracting more applicants, “CSP may increase selection system utility and an organization’s ability to hire top performers,” (Jones, Willness, and Madey 2014, 384; Boudreau and Rynes 1985) but, as Jones, Willness, and Madey point out, “the extent to which job seekers actually possess information about CSP and how they come to obtain it are largely unknown” (Jones, Willness, and Madey 2014, 384). The B Corp may be a means by which job seekers can simultaneously obtain and expand on such information.

In order to be effective, though, values-aligned job seekers must perceive the B Corp as being costly to the organization employing it. There is no direct evidence that this is so, however it is reasonable to suggest that job candidates who mention B Corps in their

interviews as a motivating factor for applying actually know what the B Corp is. If they have done their research, they have likely seen that in order to be certified a company must pay an annual fee relative to their revenue, as well as submit to regular evaluations and site visits. That the B Corp status is oftentimes salient during the hiring process is clear. Robert Cheetham, CEO of Azavea, has said that “9 out of 10 interviewees listed Azavea’s B Corp status as why they were interested in the job.”⁴⁰ Similarly:

“It is funny because the millennial crowd, they definitely are aware of it. And they definitely pick up on it...so when we put that in an ad or on Indeed, that is going to put us in a different bucket from an employee perspective” (Participant K 2017).

“It does come up. The younger generations—I’ve heard from a couple of candidates that is part of the reason they want to work here” (Participant F 2017).

“The most recent example...I was talking to our HR Director, and we actually had this same conversation. I said, ‘Do you think that this B Corp stuff impacts people’s decision to apply here?’ And she said, ‘I had this conversation with one of our employees and he said that he—now he might be an outlier—but he had done research ahead of time on all of these companies he was applying to, and he read up on us and B Corp and that made his decision’” (Participant L 2017).

But does the fact that the B Corp has attracted applicants who otherwise may not have applied necessarily mean it is attracting more values-aligned employees? Several participants in this study seemed to perceive some sort of link:

⁴⁰ B Lab. “Attract and Engage Talent.” Bcorporation.net. <https://www.bcorporation.net/become-a-b-corp/why-become-a-b-corp/attract-and-engage-talent> (accessed April 27, 2018).

“Yes, we leverage it [during hiring]...[and] we hire people who care. It’s not just that they are good at their job. They have to actually care about the mission, they have to care about doing good” (Participant J 2017).

“It allows us to attract and keep terrific talent, people who are motivated and interested” (Participant A 2017).

“If you want to attract and retain talent who care about these issues, then you better do it” (Participant M 2018).

Many others, although they do not mention values- and mission-alignment as explicitly, have expressed that the B Corp allows them to attract “better” talent (some of the following quotes are testimonials from B Corps not affiliated with this study):

“It has definitely helped...[we] have always been well-known as a company for our culture, but it has given us more exposure and has helped us quantify that...We just hired a new Director of HR. We put out a job posting just within the state. We had over 50 people apply for that position, which is huge for us. And the level of talent we were getting was incredible. And time and time again the B Corp and our culture were mentioned when we brought people in. When we post jobs now, we are getting a high number of highly qualified people. I have been here for 6 years, and that’s happening now more than ever” (Participant L 2017).

“We’ve been able to attract a group of people that you wouldn’t usually find in an office supply company of our size: highly competent, engaged, hard working.”⁴¹

⁴¹ Sean Marx, Give Something Back. “Attract and Engage Talent.” Bcorporation.net. <https://www.bcorporation.net/become-a-b-corp/why-become-a-b-corp/attract-and-engage-talent> (accessed April 27, 2018).

“We found our customer service manager through the B Corps Jobs Board. Because of her unique combination of talents we have seen our customer satisfaction and retention markedly improve.”⁴²

All of this gives us reason to believe that the B Corp can act as an effective signal. Values-aligned job seekers search for more information about potential employers, and employers are incentivized to find a way to credibly communicate their social and environmental commitments to them. After all, they want to find the highest quality, best-aligned employees—and several B Corps feel that their certification has helped them do that.

But in what ways might the B Corp underperform as a signal? For one, it is not clear that its cost is apparent to job seekers. Companies and B Lab alike would benefit from making this more obvious. For one, B Lab might want to include testimonials about how difficult the certification process is. One participant in this study, for example, described it as “onerous,” and while that may not be attractive to potential B Corps, it makes the perceived cost of the signal that much more significant.

More importantly, however, the B Corp presents such obvious benefits to its employees that it might become hard to distinguish which employees are claiming to be values-aligned just so that they can secure better workplace benefits. To guard against this, being a B Corp must also help a company employ an effective screen.

2. Screening as a B Corp

⁴² Bob Altieri, One Village. “Attract and Engage Talent.” Bcorporation.net. <https://www.bcorporation.net/become-a-b-corp/why-become-a-b-corp/attract-and-engage-talent> (accessed April 27, 2018).

The previous section showed how job seekers can use the B Corp to reveal more information about potential employers, but ended with an important consideration about the lack of information flowing in the other direction: how can employers be sure that it is a values-fit, and not merely better benefits, that attracted a job seeker to their company? The mention of the company's B Corp status in an interview provides some assurance; after all, it shows that the employee has taken the time to research and understand what a B Corp is, indicating some level of interest. This time represents a cost. Of course, it is a slight cost—hardly one that would make the B Corp status an effective screen.

In order to truly be effective and desirous, it would seem that the B Corp would not only need to help companies attract more highly qualified talent, but also help them attain them in a way that ensures a certain degree of mission commitment. This could be achieved through various mechanisms, like offering a below-market salary (so long as it is clear that the difference is being redirected in a way that is consistent with values and mission) or requiring a certain amount of mission-related volunteer hours. The loss in salary represents a far more significant cost to someone who does not care about the mission, thus screening out those who are only there for workplace benefits. Requiring volunteer hours works in a similar way; it is a small cost for those who care, and a much larger one for those who do not.

By simultaneously helping to legitimize their social performance and bring more talent through the door, the B Corp may make it more likely that a company is able to secure high-quality, values-aligned talent at a below-market rate.

3. Signaling, Screening, and Accountability

How does all of this tie into accountability and, more specifically, Briana Cummings' notion of an improved incentive? For one, I have illustrated how the B Corp can be used as both a signal and a screen to attract and acquire more intrinsically motivated talent—one of the mechanisms through which Cummings thinks a more internal, self-regulatory accountability might take shape. Additionally, recall that she also mentions the importance of informal social regulation, which might take the form of “management by embarrassment.” We might think of B Corps in this way as providing what behavior economists call a commitment device – “a way of ensuring that you’ll live up to your promises” (Surowiecki 2014, par. 4). Typically, B Corps are thought of as making a commitment to the public and to the marketplace, but this commitment device might even be more effective when directed inward. In other words, managers do not want to let their employees down:

“Now, if you really want to keep them and keep them happy, then you better stay true to your mission...[and] you have to give to the folks in the company for them to believe that you’re going to not just talk the talk, but walk the walk” (Participant A 2017).

“Because we had this B Corp status and this commitment to everybody who we have brought on board here, it was really important to us to structure that acquisition in such a way that everybody could, you know, could have a job with the new structure and continue doing the work that they had been doing and enjoying. And we could have done that differently. We could have sold off to the highest bidder, to somebody who wasn’t interested in our team, and we chose to do it differently in a way that made sure we were taking care of everyone as much as possible” (Participant C 2017).

“When employees come in, if we don’t have the culture that aligns with [the B Corp seal], then we lose” (Participant K 2017).

It might also be the case that if managers know they are getting high quality talent at a discounted wage, they will be even more inclined to make sure they are meeting their employees' values expectations. This requires not only making visible to employees how the difference between their "discounted wage" and "potential wage" is being spent—e.g. on robust volunteer programs, extended paternal leave, or mission-oriented company trips—but also incorporating employees into the assessment process and maintaining transparency throughout the organization.

The participation of a values-aligned workforce on the assessment is valuable for a number of reasons. For one, to the extent that it prompts deeper engagement in a variety of areas, it puts more minds at work thinking about possible solutions and what "could be." It also addresses the concern of selective or embellished reporting, as values-driven employees are likely more willing to flag potentially incorrect information. And, third, it serves as a layer of transparency in and of itself, providing employees answers to questions like: "What multiple is the highest compensated individual paid as compared to the lowest-paid full-time worker?"—a question that may be particularly important to highly-talented employees who know they could acquire a higher salary elsewhere.

Ultimately, a company seeking to utilize the B Corp as a screen during the hiring process could introduce any number of "costs." A reduced salary is perhaps the most obvious, but it is not necessarily mission-aligned; the volunteer requirement example might be better for companies seeking to develop more aligned workforce. However, any of these methods, if done correctly, serve to strengthen the principle of "management by shaming" in their own unique ways. Ensuring that internal stakeholders are satisfied, challenged, and are

doing work aligned with their values thus becomes the central driving force behind the company staying true to its stated mission and values.

D. Conclusion

Briana Cummings' central argument is that for mission-driven enterprises, external accountability mechanisms, especially those tied to quantitative assessments and sanctions, are insufficient. Instead, B Lab—as one of the most popular third-party standard-setters—should foster more internal and intra-industry accountability. To do so, she suggests rethinking “to whom” and “for what” benefit corporations should be held accountable.

Key to both of these categories is employees—a stakeholder group that B Lab appears to impact in nontrivial ways. I have shown how their assessment has led to employee-run committees and guided employee structure. I have shown how the best employee practices, through B Lab's position as an institutional intermediary, have spread to other companies within its purview. I have illustrated how, by setting a standard, being a B Corp pushes managers to keep their employees happy and motivated.

Cummings desires a “for what” that involves accountability for internal processes and regular self-evaluation, and a “to whom” that involves the corporation itself, its professional peers, and its intended beneficiaries. B Lab, it seems, gets us much closer to realizing all of this. What has resulted from their efforts is a network of incentives and support structures that make internal accountability more likely. Between employing the B Corp to attract and retain values-aligned employees, utilizing the assessment to prompt deeper internal engagement, attending B Lab retreats, encouraging internal transparency, and strengthening

“management by shaming,” employees and processes emerge as the “to whom” and “for what” B Corps are held accountable.

Of course, it is a problem that the intended beneficiaries are not explicitly included here. The hope is that the B Corp, carefully employed as a signal and working in concert with a screen, as well as with all of its other features, will help create a mission-driven workforce that is encouraged to engage more closely with its intended beneficiaries and bring them into the fold. B Lab’s commitment to constant evaluation and progress—evidenced for example by the Thematic and Industry Data sets discussed earlier—hopefully makes this more likely, as well.

IV. CONCLUSION

This paper has touched on several aspects of the benefit corporation, but centers around just two of them: funding and accountability. While speculation abounds, hardly any empirical studies actually explore these areas, much less explain them through a theoretical lens. This study set out to be one of the first to do so. This section will summarize the key findings, as well as discuss limitations and implications for future research, before closing with a few remarks about the future of the corporate form.

A. Summary of Findings

Chapter Two introduced signaling and screening theory and applied to benefit corporation fundraising. At present, very little is known about how investors perceive the

form and how electing the status might impact funding. B Lab advertises that many benefit corporations have raised capital from prominent venture capital firms⁴³, and as mentioned earlier there is plenty of speculation about how traditional and impact investors are likely to react to it, but beyond that not much work has been done. This study started to explore the fundraising experiences of various benefit corporations to see what insights emerge.

Applying signaling and screening to benefit corporation fundraising, I argue that benefit corporations are a more effective screen than they are a signal, and that social entrepreneurs can employ the benefit corporation as a screen to better find long-term alignment with investors. When fundraising, a social entrepreneur who is deeply committed to his or her mission faces an information asymmetry problem, where the missing information is the degree of social commitment of an investor. In an investing ecosystem where investors run the gamut from heavily impact-driven to purely driven by short-term profits, social entrepreneurs want to be able to best locate an investor on that spectrum. Becoming a benefit corporation can help them do so by introducing a certain level of future uncertainty, from which an investor is more likely to shy away if he or she is unwilling to make any trade-offs between financial and social bottom lines. Crucially, the screen must be costly to the investor if it is to be effective; this uncertainty and the perceived financial trade-off that may ultimately result is that cost.

Chapter Three switches to a different issue entirely: accountability. This chapter leans heavily on Briana Cummings' assessment of benefit corporation accountability, and essentially argues that her analysis of the legislation itself is accurate, but that she does not

⁴³ B Lab. "Benefit Corporations Raising Capital." Benefitcorp.net. <http://benefitcorp.net/benefit-corporations-raising-capital> (accessed May 14, 2018).

quite give B Lab the credit it appears to deserve. Importantly, B Lab has been evolving rapidly and many of her criticisms may have been accurate at the time of her writing, so much of the chapter amounts to “checking up” on where they are now in light of her suggestions. The chapter goes on to argue that while being a benefit corporation by itself does very little to ensure accountability—internally or externally—being a B Corp may make the creation of bottom-up, horizontal accountability mechanisms more likely.

Again, I use signaling and screening theory to explain how this might be so. As a signal, there is evidence that the B Corp helps employers attract higher quality, values-aligned jobseekers. It lends a certain amount of legitimacy to the firm’s socially responsible claims and at least serves as an initial signal that the company is not merely “talking the talk.” The caveat, of course, is that employees could seek out B Corps merely because they are typically better places to work, which would not necessarily aid firms in finding values- and mission-aligned employees. This is where screening comes in. In order to effectively screen out these employees, the firm has to impose some sort of cost on the employee, ideally one which is mission-related—for example, a volunteering requirement with an aligned nonprofit.

Being a B Corp is not necessary in order to impose this sort of mission-related cost, so its real value here is how it acts as a signal. Essentially, I suggest that it helps bring higher-quality, values-aligned employees in the door and gives weight to a firm’s social performance claims, thus making aligned employees more willing to take on an associated cost. Once a part of the company, horizontal accountability becomes more likely in two ways: (1) through B Lab’s current structures, which now have more talented, values-driven

employees engaging with them; and (2) through “management by shaming,” which is essentially management’s drive to keep their values-driven workforce happy.

Crucial to the success of any for-profit social enterprise is alignment with investors and the development of a strong accountability mechanism. In sum, this paper argues that being a benefit corporation does help cultivate the former, but that—without also being a B Corp—it is unlikely to help with the latter.

B. Limitations

The primary limitations of this study stem from the sample size and the method employed. As with all interviews, researchers are at the mercy of their interviewees, who can be as selective with information as they wish and are relying on their own memories and perceptions. When entrepreneurs told me, for example, that they think that being a benefit corporation turned off some investors, that is merely their perception of the situation and cannot necessarily be taken as fact. This study also solely relied on the perspectives of founders and executives and did not involve interviews with investors or other employees. Additionally, there are thousands of benefit corporations and B Corps, of which this study only represents twelve—and, furthermore, likely represents some of the most mission-driven among them. Only two benefit corporations in this study were not B Corps, and one of those two was in the process of becoming one; teasing out what might be due to the B Corp versus what is due to the benefit corporation, therefore, is a particular challenge in this study.

C. Contribution and Future Research

The primary contribution of this piece is that it is one of the first studies that utilizes empirical data and theoretical considerations to better understand benefit corporations. At

present, such studies are few and far between. Much has been written about accountability and fundraising has certainly emerged as a primary area of interest, but hardly any work has been done explore these areas outside the legal literature.

This study contains information that social entrepreneurs hopefully find useful when embarking on fundraising and hiring employees. Ultimately, the success of the benefit corporation as a screen in fundraising hinges on how visible and prominent the legal status is throughout the process, as well as the costs associated with it. The higher the perceived cost, the better aligned a social entrepreneur and his or her investors are likely to be. Furthermore, social entrepreneurs who wish to develop more organic and horizontal accountability should consider becoming a B Corp or something similar and attaching a mission-related cost to their employment offers. This is likely to help cultivate a workforce that will help keep the firm accountable to its stated ends as it grows and faces increasingly complex trade-offs. Of course, in order for the benefit corporation or the B Corp to function as described in this paper, the sort of alignment discussed here has to be *desired*. Neither the benefit corporation or the B Corp will do any of these things on their own, and it would be wholly unreasonable to suggest that they should be able to.

A significant amount of further research is needed to both confirm the hypotheses coming out of this study and to expand our overall understanding of benefit corporations. Funding should be investigated more from the investor side, as this study only includes the perspectives of the entrepreneur. How valuable is this form to impact investors? How salient is it to shareholders when they are making decisions? Is conflict more likely in boardrooms when mission and finances must be considered, and does this affect relationships amongst shareholders? Additionally, we cannot know if the screening potential of benefit corporations

is actually useful without checking in several years down the line to see whether or not entrepreneurs feel that it has aided in establishing effective long-term alignment.

Accountability should be explored more from the employee side, as well. Do employees feel that a company's visible commitment to social standards makes it easier to hold management accountable?

Also, on a more general level, more information is needed about the effectiveness of B Lab's audits. How effective are they and how well do they evaluate a company's second- or third-tier employees and suppliers? Although they may check that suppliers are certified or verified, do they have a standard for which third-party certifiers are acceptable? How far down into a company's supply chain does B Lab's audit credibly go? Effective auditing has proven elusive in the "race-to-the-bottom era," but it is no doubt an important part of any accountability framework. Such considerations are important to the success of the "B movement" in general as production and sourcing increasingly moves out of sight and, too often, out of mind.

D. Closing Remarks

The benefit corporation as a legal innovation is a modest step towards embedding social responsibility into the U.S. corporate world. Its chief accomplishment, perhaps, is that it represents a recognition on behalf of legislators that some sort of change is needed. The benefit corporation, however, is not that change; hopefully it is only a first step toward reforming corporate law. It would have to become significantly stronger and be accompanied

by much more robust enforcement mechanisms; it is unlikely this will happen any time soon, if at all.

In terms of shifting corporate behavior, B Corps are undoubtedly more effective, and B Lab is continuing to grow at an exciting pace. In a 2016 interview with Fast Company, Jay Coen Gilbert, one of the founders of B Lab, said that they have been witnessing increased interest from some of the country's largest companies: "We've been getting more inbound traffic from Fortune 500 companies over the last six to nine months. I'm not sure what's triggered it, but there's been a palpable increase in energy from these folks" (Schiller 2016, par. 8). This raises a lot of concerns, chief among them being how B Lab's efforts and the B Corp seal do not get diluted by these large multinationals—but B Lab does not plan to relax their standards for anyone. Though certifying a bunch of Fortune 500 companies would mean a large influx of operating revenue for B Lab, that's not what they are concerned with: "Our measure is not whether a business gets certification in the next 12 months. We're much more concerned with playing the long game, so the next generation of Fortune 500 companies rises into that status with stronger impact governance. Remember, two-thirds of [that list] is different from 20 years ago, so things can change" (Schiller 2016, par. 14).

Of course, this brings up an entirely new question—is all of this compatible with being a public company? Only one benefit corporation is a public company, and it's a for-profit college. There are a few publicly-traded B Corps, most of them listed on exchanges outside the U.S., but the most interesting case certainly is Etsy. The online craft retailer was a B Corp that went public in 2015 and was long known for the centrality of its values to the way it conducted and ran its business. But things took a turn after they went public, as they

were then “evaluated just like any other company traded on the stock market” (Gelles 2017, par. 8). This was despite their efforts to incorporate their values into their IPO approach:

True to form, Etsy found ways to make its initial public offering inclusive. It marketed shares to small investors and Etsy sellers and tried to concentrate shares in a smaller than usual number of institutional holders. Besides upholding the company’s egalitarian ethos, the effort had a strategic rationale. The hope was that such a shareholder base might insulate Etsy from some of the short-term pressures of the market (Gelles 2017, par. 18).

It didn’t work. As Etsy’s stock fell, much of what had made it so special eventually dissolved as a new focus on profitability took over—they even dissolved their “Values-Aligned Business” team. An employee said that “Etsy had the potential to be one of the great ones, but it looks like they are cutting anything that is not essential to the business. This is a cautionary tale of capitalism” (Gelles 2017, par. 12). When Etsy received word that, as a B Corp, they would be required to convert their legal standing to a benefit corporation, they made the decision to let their B Corp status lapse.

While we do not know the internal workings of how Etsy came to this decision, it is possible that they did so out of fear of a mission-related shareholder lawsuit. In the “Risks Related to Our Business and Industry” section of their 2017 Annual Report, they list the following, among others: (1) “Our business could be negatively affected as a result of actions of activist shareholders,” and (2) “Adherence to our values and our focus on our mission and long-term sustainability may negatively influence our short- or medium-term financial performance” (Etsy 2017, 22). The second immediately follows the first and includes a paragraph about the decision to relinquish its B Corp status because they chose not to convert to a benefit corporation. While losing one of its flagship companies is a blow to B Lab, the

silver lining is that they may have made the decision because they perceived it as possibly having a real impact—primarily due to one of the embedded accountability mechanisms: the benefit enforcement proceeding.

Etsy serves as a reminder of how complex this problem is. Sustainability and responsibility might simply be incompatible with scale, at least in the way we presently conceive it. It could be that decentralization is the only path toward a “sustainable economy and environmental survival”—that “as long as large corporations have as much power as they have, there will always be huge economic and social injustices” (Edmondson 2014, 250-251).⁴⁴ Many of the changes made at Etsy have been internal and cultural, but perhaps more troublesome is what happens in areas like sustainability and human rights as a company goes through the same growth stages. All of these issue areas are connected: “Supply chain responsibility relates directly to the problem of ‘too big’ since it raises the question of whether fully sustainable sourcing is even possible for large conventional corporations. In other words, besides the risk of becoming outsized for the communities they serve, in the effort to meet growing demand for their products and services, conventional companies can also become too big to respect human rights” (Bauer and Umlas 2017, 312).

B Lab needs to keep this possibility in mind as they emphasize the importance of scale and public markets in their movement. It might be that cultivating a stronger economy of responsibly-managed miniature-, small-, and medium-sized enterprises is B Lab’s greatest value added to society—and we have seen some of the ways their interventions might be helping us achieve that.

⁴⁴ Edmondson is here quoting entrepreneur and key member of the Social Venture Network, Judy Wicks.

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