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**\*1007** BENEFIT CORPORATIONS: A CHALLENGE IN CORPORATE GOVERNANCE

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*Benefit corporations are a new form of business entity that is rapidly being adopted around the country. Though the legislation varies from jurisdiction to jurisdiction, most statutes are based on a model proposed and promoted by B Lab, itself a nonprofit corporation. The essence of these statutes is that, in making business judgments, the directors of a benefit corporation must consider the impact of their decisions on the environment and society. The model legislation, though, may create serious governance issues for the directors of benefit corporations that operate under these laws. This article analyzes the model legislation and identifies its weaknesses, particularly with respect to governance issues.*

**I. INTRODUCTION**

An enduring question in corporate law is whether the law should encourage corporations to act in a more “socially responsible” way; that is, to sacrifice, or at least have the ability to sacrifice, some profit to achieve some social good, such as a healthier environment. [FN1] On this view, the directors of a socially responsible corporation could opt to power the corporation’s factory or offices with renewable sources of energy, even if the cost exceeded that of a carbon-based fuel, and **\*1008** not have to account to anyone for having made this choice. Although corporate law likely already allows directors to make such a decision, [FN2] some nagging doubt persists in at least some jurisdictions as to whether directors can pursue a course of action that does not maximize shareholder value. [FN3] In addition, corporate **\*1009** management faces non-legal incentives to maximize profits and stock price, such as executive compensation that is contingent on those matrixes.

While this doubt could be safely resolved with a rather simple amendment to the business corporation statute in those jurisdictions where it persists, [FN4] a dedicated cadre of “social entrepreneurs” has embarked on a more ambitious path, to create a new form of for-profit corporation in which acting in a socially responsible fashion is not just an option for the electing corporation, but rather is its mission. Such corporations, which are sometimes called “benefit **\*1010** corporations,” [FN5] are distinct from traditional corporations in a number of respects and represent a radical transformation of corporate law--a transformation reflected in legislation [FN6] that has been introduced in twen-

ty-three states to date. Most of this legislation is based on a model act that is discussed more fully below and referred to herein as the ““Model Legislation.” [FN7]

It should be noted that benefit corporations are not nonprofit corporations and are not formed under nonprofit corporation statutes. Traditionally, outside of governments, nonprofit corporations have carried the weight of making the world, or at least the United States, a better place. Apparently, however, the entrepreneurs behind the benefit corporation movement are dissatisfied with limitations of the nonprofit corporation. Such entities have difficulty raising capital because, by statute, they cannot pay dividends or otherwise make distributions to their supporters, who often become the “members” of the nonprofit corporation. [FN8] Moreover, nonprofits are typically limited in their scope; they are religious organizations, educational institutions, food banks, safe houses for abused women, etc. and often are exempt from federal income taxes under section 501(c)(3) of the Internal Revenue Code. The idea behind benefit corporations is more ambitious: to motivate for-profit business corporations to have a positive impact on society and the environment in addition to earning profits. The vision of its proponents may be that with the promise of at least some return, investors may invest in such entities and, gradually, as more and more corporations sign on to the benefit corporation model, society and the environment will benefit. For zealots of the concept, profit maximization then may become the exception, rather than the rule, in the for-profit world.

The benefit corporation movement follows a growth of socially responsible investing (“SRI”) in the last three decades or so. As of 2010, companies that had been, on some basis, identified as socially responsible represented roughly 10 percent of all domestic assets under management, approximately \$2.3 trillion, much of it in mutual funds. [FN9] SRI varies from manager to manager, but investors who are committed to a certain sort of socially responsible investing are likely to find a manager or fund that meets their criteria. [FN10] SRI represents a classic market solution to the demand of investors for a certain type of investment. For the advocates of the benefit corporation, however, SRI is insufficient. Arguably, the businesses that garner SRI funds may not be as socially responsible as they \*1011 could be, and state law (in the form of a benefit corporations statute) could provide the bridge to even more socially responsible behavior by requiring directors to take into account social and environmental concerns with every decision that they make.

The directors of a benefit corporation thus have both a difficult and envious task--difficult because they must choose between the often conflicting choices of “doing good” and making a profit, and envious because they have the freedom to spend other people's money to further social goods that they favor. As Delaware Chancellor Strine put it so colorfully: “[Benefit corporations exist in] a fictional land where you can take other people's money, use it as you wish, and ignore the best interests of those with the only right to vote.” [FN11] While it is well understood that directors of benefit corporations will face decision points when they will have to choose between profit maximization and a socially preferable alternative that is, at best, less profitable, [FN12] it is less well appreciated that directors will have to choose *among* socially preferable alternatives. This wide array of choices may prove problematic for conscientious directors of a benefit corporation. In this article, I hope to shed some light on the complexities that they face.

After a critical evaluation of the Model Legislation which, though modified from state to state, is the basis for benefit corporation legislation in the states that have such legislation, I turn to a subject that has not been addressed in the growing literature [FN13] on benefit corporations: what can we learn from scholarship on decision making about how directors are likely to behave under these circumstances? In short, the research suggests that the resulting board

decisions may not be optimal. This serious shortcoming in the Model Legislation argues in favor of modifications to it, modifications that have been resisted by its proponents. I then consider the wisdom of proposing legislation authorizing the creation of two new types of socially responsible corporations, one patterned after the Model Legislation and one providing for the flexibility suggested in this article. [FN14] I conclude\***1012** with some thoughts on whether the Model Legislation can achieve the ambitious goals that its proponents seek or whether a different approach may be more effective.

## II. BENEFIT CORPORATION LEGISLATION

As of early 2013, legislation authorizing the creation of a benefit corporation had been adopted in fourteen jurisdictions. [FN15] Nine other states and the District of Columbia considered, but failed to adopt, such legislation. [FN16] In at least one state (Colorado), the legislation was introduced in three consecutive legislation sessions, finally with success. [FN17] These various legislative initiatives were not coincidental, nor the work of grassroots organizations. Rather, they represent the efforts of an entity called B Lab. Understanding B Lab sheds some important light on benefit corporation legislation.

Founded by three former corporate executives, [FN18] B Lab itself is a nonprofit corporation whose mission, according to its website, is “to use the power of business to solve social and environmental problems.” [FN19] It seeks to achieve its mission\***1013** in two ways. First, B Lab promotes the adoption of its Model Legislation that allows the formation of benefit corporations; and second, B Lab certifies a qualifying corporation as a ““Certified B Corporation,” meaning that the corporation has met B Lab's standards as a socially responsible corporation. [FN20] Certification, which is described on the B Lab website, [FN21] involves a multi-step process, starting with a self-assessment by the applicant of its “overall impact ... on its stakeholders.” [FN22] This initial submission is followed by a review by the B Lab staff, the submission of supporting documentation, and the payment of a fee to B Lab. If the applicant is not a benefit corporation at the time of its application, a statement on the website indicates that it must become one as a condition to certification. [FN23] As of this writing, the B Lab website listed 794 corporations and limited liability companies as Certified B Corporations, [FN24] some of which are profiled from time to time on the site. [FN25] In addition to being listed and possibly promoted on the B Lab website, a Certified B Corporation may, of course, promote itself as such. [FN26] These privileges may enhance the ability of the corporation to market its goods and services and to attract capital.

The Model Legislation promoted by B Lab has been the basis for all of the benefit corporation legislation adopted to date, although the adopting states have all made modifications, some significant. Set forth below is description of, and commentary on, the key provisions of the Model Legislation. I have footnoted some significant alterations adopted by various states.

### A. BENEFIT PURPOSE

The Model Legislation requires that the benefit corporation [FN27] have, as a corporate purpose, “creating a general public benefit,” [FN28] which is defined as “a material\***1014** positive impact on society and the environment, taken as a whole, assessed against a third-party standard, from the business and operations of a benefit corporation.” [FN29] The Model Legislation permits, but does not require, the benefit corporation to have, additionally, a purpose of

creating one or more “specific public benefits,” [FN30] which is defined in a rather peculiar fashion. [FN31] The Model Legislation lists six activities as specific public benefits, including providing low-income or underserved individuals or communities with beneficial products or services; promoting economic opportunity for individuals or communities beyond the creation of jobs in the normal course of business; preserving the environment; improving human health; promoting the arts, sciences, or advancement of knowledge; and increasing the flow of capital to entities with a public benefit purpose. A seventh specific public benefit is sort of a catch-all: conferring any other particular benefit on society or the environment.

The use of the term “create” in the Model Legislation is ill-advised. The Model Legislation provides no guidance as to what it means to “create” a general or specific public benefit. It is unclear, therefore, whether a corporate policy to donate a certain amount of money or percentage of profits to certain causes would satisfy the “creation” requirement. A more apt term may be “pursue.”

From a drafting perspective, the deficiencies with this section do not end with the create/pursue problem; several other problems are readily apparent. First, the catch-all provision makes the other items just examples of a specific public benefit; legislation typically does not include examples to define terms. It probably would be sufficient to include only the catch-all. Second, promoting economic opportunity for individuals seems more like a private benefit for the individuals who are provided the opportunity than a public benefit. Third, the idea of “creating” a public benefit (whether general or specific) is elusive. [FN32] With respect to the environment, for instance, the typical benefit corporation can, at best, operate so as to minimize its environmental impact, but can it have a “material positive impact” on the environment? Perhaps a corporation engaged in the business of cleaning up toxic waste dumps or manufacturing scrubbers for coal-burning utilities fits the bill, but that accounts for few corporations and, incidentally, none of the corporations listed as benefit corporations on B Lab’s website as of the writing of this article. Fourth, the specific public benefit \*1015 of “preserving the environment” is particularly odd in view of the fact that every benefit corporation must have the general public purpose of operating so as to have a material positive impact on the environment. Arguably, preserving the environment is passive in comparison to operating to have a material positive impact on the environment.

More fundamentally, the purpose section is an example of the narrowness of the Model Legislation. Social entrepreneurs are precluded from forming under the Model Legislation--and promoting their entity as a benefit corporation--if they prefer to pursue *only* a specific public benefit. [FN33] It may be that the community in which the entrepreneurs wish to incorporate is in desperate need of increased employment and the entrepreneurs are motivated to address that need by restarting a factory in the community. They realize that the operation of the factory will not have a “material positive impact on the environment” and determine that the benefit corporation legislation is therefore unavailable to them. This is an unfortunate byproduct of the rigid approach of the Model Legislation; the drafters could have provided that benefit corporations have a general public benefit purpose or a specific public benefit purpose or, if a benefit corporation so chooses, both.

## B. ASSESSMENT: THE ANNUAL BENEFIT REPORT

The Model Legislation has two important assessment features. First, the benefit corporation is required to produce, file with the state, and make publicly available an annual benefit report that describes how it pursued the general

public benefit (and any specific public benefit included in its articles) and the success of that pursuit. [FN34] Second, the assessment must be with reference to a third-party standard that (a) is developed by a third party that is independent of the benefit corporation [FN35] and (b) is “comprehensive,” “credible,” and “transparent,” [FN36] as more fully described in the Model Legislation. These are among the \*1016 most rigid provisions in the Model Legislation and, not surprisingly, are the provisions most often altered in adopting legislation. [FN37] There is no requirement in the Model Legislation that the benefit corporation use the services of a third party to prepare or audit the annual report, and some benefit corporation legislation makes that explicit. [FN38]

In any case, the Model Legislation here, too, is rigid. Not only must the corporation issue an annual report, its contents and form are dictated by the Model Legislation. The cost of the report is, of course, borne by the benefit corporation, which may not be well situated to bear such an expense. Moreover, the production of an annual report may be rather pointless, at least as far as the shareholders are concerned, because most benefit corporations are likely to be closely held and the shareholders will be well aware of the corporation's policies and actions that bear upon its general and specific public benefit purposes. If such a report is of importance to shareholders, they can of course require it as a condition to their investment in the entity.

On the other hand, arguably the public and other corporate stakeholders (e.g., the community in which the corporation operates, its employees, its suppliers, etc.) have an interest in knowing whether the benefit corporation is positively affecting the environment and society and whether it is achieving its specific public benefit (if any). Presumably, the benefit corporation should be accountable to the public and its stakeholders if it is organized as a “benefit corporation.” [FN39] But this raises relevant empirical questions, such as whether members of the public or corporate stakeholders are likely to consult a benefit corporation's website to inspect such a report, and, if so, whether they are likely to do so in sufficient numbers to justify the legislative mandate. The Model Legislation seems to assume an affirmative answer to these questions, but such an assumption is intuitively doubtful. Of course, even if not mandated to do so, a benefit corporation certainly could prepare and make available such a report and may do so if, for instance, the directors believe that a report would facilitate \*1017 attracting capital. [FN40] If the corporation fails to issue a report, that failure, itself, may be useful information to the public and corporate stakeholders who seek the information. Moreover, a benefit corporation could include such a requirement in its articles, if it so chooses, as sort of a “bonding mechanism,” essentially guaranteeing its sincerity and commitment to the benefit corporation model. [FN41] Finally, whether a corporation operates in a socially responsible fashion or not is an assessment that a compensated third party, such as B Lab, may make and, indeed, does make with its “B Corporation” certification. [FN42] Other entities provide various certifications, such as the “FEED” certification or “Green Seal,” that signal the company's commitment to social or environmental objectives. [FN43] Such a certification may be more significant to investors and the public than a prolix report.

Even the possibility of an annual evaluation, at least in many cases, is highly problematic. The nature of a general public benefit may require attention to the long term. For instance, how can a corporation evaluate the effect of its operations on the environment? Take a typical Certified B Corporation, BBWoof, Inc., a Maryland benefit corporation. This company, which operates under the name “The Big Bad Wool,” sells pet food and supplies. It also seeks to serve as “a community resource for companion animals and their guardians.” [FN44] The company promotes its policy of carrying “eco-friendly pet supplies, Fair Trade items, and merchandise sourced from local and North American companies, with preference given to small manufacturers and minority owned companies.” [FN45] Assuming that it adheres to these policies, how could it--or anyone--evaluate its impact on society and the environment,

taken as whole? Arguably, buying and reselling such merchandise (indeed, any merchandise) would have a negative effect on the environment, albeit less of a negative effect than would the purchase of eco-unfriendly or remotely sourced products. So, BBWoof, Inc. must find a third-party standard that allows it to quantify the effect of its activities over the past year. Its annual report, called its “B Consumer Report” on its website, discloses a “composite score” of 94.2 and an environmental score of 10.7 “points earned,” with a “value” of 55 percent. [FN46] Unfortunately, the report includes no \*1018 information on what these scores mean, so it is useless. It is also unclear from the report whether the assessment was based on a third-party standard and, if so, on which standard. Regardless, the underlying problem of measurement remains--how did Woof's business affect the environment during the year?

While Woof's impact on the environment and society is difficult to describe, it is even more difficult to quantify. Nevertheless, B Lab has recommended that a benefit corporation's annual report do just that, suggesting the company include “quantifiable” targets and results related to its mission and “consistent variables of measurement which allow comparisons to previous years.” [FN47] The quest for precise quantification is likely to give rise to simplistic measurements. For instance, in the case of Woof, the company might seek to calculate the positive environmental impacts of purchasing merchandise from North American sources as compared to, say, Asian sources. To meet the need for quantification, it might estimate the difference in carbon emissions between a shipment from Asia as opposed to one from North America. As difficult as such a calculation may be, that would not be the whole story. Woof would also have to calculate the difference in environmental impact between the Asia source and the North American source. Perhaps the North American sources assemble products from raw materials and parts imported from, say, Africa. Perhaps, on balance, purchasing from the Asian source would have less of an impact on global warming. These, and possibly other, complexities make Woof's task costly, time consuming, and, in the end, nearly worthless. Woof, after all, is in the business of selling pet supplies, not making complex calculations of its impact on the environment and society.

At best, then, the annual benefit report is a costly exercise with minimal, if any, value. At worst, however, it may drive overzealous managers to structure their operations to achieve certain scores on an annual assessment, even if those managers doubt the validity of those scores. Put differently, just as teachers who are skeptical of standardized testing may “teach to the test” to assure high scores by their students (and corresponding rewards to the teachers), managers may do likewise once a measurement regime is adopted. This will be especially true if management's compensation is based, at least in part, on achieving high scores on the annual assessment. A predictable, but unintended, consequence of such a regime is that managers may eschew a more socially responsible course of action if doing so results in a lower score. For instance, concern about negative scores for using a remote supplier may cause a manager to use a local supplier whose labor policies the manager finds objectionable. While the benefit corporation model may free up managers from the need to maximize profitability, it may bind them to an equally inflexible policy of maximizing some social responsibility score that, in the end, neither measures social responsibility nor assures \*1019 socially responsible decision making. As one commentator noted, focus on short-term, quantifiable results has the effect of discouraging “the pursuit of goals that are less easily quantified or that are not measured at all.” [FN48]

Proponents of benefit corporation legislation may argue that a third-party “audit” resolves much of the measurement difficulties described above. The argument might go something like this. Regardless of the difficulties of making business decisions and taking into account the environmental and societal impacts of those decisions, benefit corporations have to account publicly for those impacts. With that in mind, benefit directors will make the sound environmental and social decisions; having to report on them will help shape the decisions and outside “auditors” will

serve as checks on managers seeking to game the system. This rationale is detective, however, because benefit corporations are not required to hire outside social auditors and benefit corporations that are Certified B Corporations are “audited” by B Lab only in the loosest sense of the word. B Lab anticipates site visits only once in ten years and, in the interim, relies on reports and data from the benefit corporation for assessment purposes. Moreover, one might doubt whether B Lab would “decertify” a failing B Corporation; its website does not disclose what process, if any, exists for decertification and, of course, decertification would result in diminished fees to B Lab.

Even if an industry of social auditors were to emerge, it would be of questionable value. We can reasonably anticipate that competition among such auditors will result in reports favorable to the benefit corporation that requested and paid for the report. The weakness of current third-party business auditors--business accounting firms and credit rating agencies come readily to mind--should lead to skepticism about social rating agencies, especially since social rating agencies do not face the risk of civil liability in the same way that business accounting firms [FN49] and, potentially, credit rating agencies do. [FN50] Because the Model Legislation precludes monetary liability for officers, [FN51] directors, [FN52] and the corporation [FN53] for failing to pursue or create a general or specific public benefit, the social rating agencies are further insulated from the risk of monetary liability. Benefit corporations can be expected to shop for social rating agencies that \*1020 are likely to give favorable ratings. It is no answer to say that if social entrepreneurs have gone to the trouble to create a benefit corporation they are unlikely to game the system: such a view ignores the perceived value of benefit corporation status [FN54] and the risk that, even acting in good faith, benefit corporations may seek out favorable rating agencies.

### C. BENEFIT ENFORCEMENT PROCEEDING

The Model Legislation addresses, weakly, the consequences a benefit corporation may face if it fails in its general or specific public benefit purposes. [FN55] Section 305 provides a new cause of action--a “benefit enforcement proceeding”--which may be brought directly by the corporation or derivatively by a shareholder, a director, a 5 percent owner of an entity of which the benefit corporation is a subsidiary, or other persons “as specified in the articles or bylaws.” [FN56] The action may be brought against the benefit corporation or its directors or officers for: “(i) failing to pursue or create a general public benefit or a specific public benefit set forth in its articles; or (ii) violation of a duty or standard of conduct under [the provisions of the Model Legislation].” [FN57] The Model Legislation provides, in other sections, that the benefit corporation and its directors and officers will not be liable for monetary damages for failing to pursue or create a general public benefit or a specific public benefit set forth in its articles, [FN58] so the initial question raised by section 305 is what remedy would be available to a successful plaintiff. This question is addressed below, following a consideration of some problems raised by the text itself.

The first such problem is in clause (i): what does the section mean when it speaks of “failing ... to create a general ... or specific public benefit”? Surely the drafters could not have meant that if, for instance, a benefit corporation had as its specific public benefit alleviating poverty in its community that the corporation would be liable if poverty persisted. The word “create” seems misplaced. As to “pursue,” could the plaintiff’s claim be defeated if the benefit corporation made some efforts to achieve its general or specific public benefits? It may be that \*1021 the drafters intended to impose liability only if the benefit corporation failed to make a “good faith” effort to achieve these benefits, but it so, a new question is raised: what does it mean to make a good faith effort to, say, alleviate poverty in a community?

Perhaps the best judges of the effectiveness of the corporation's efforts are the supposed beneficiaries of its benefit purposes. Nevertheless, they are denied standing under the Model Legislation, unless the articles of incorporation or bylaws of the benefit corporation otherwise provide. [FN59] If granted standing, the action is nominated as a “derivative action.” [FN60] This is odd, because a derivative action is one brought on behalf of the corporation, with any recovery inuring to the benefit of the corporation. Persons who are not shareholders of the benefit corporation would have little incentive to bring such an action. Regardless of who can maintain an action, the question of remedy looms large.

It seems somewhat unlikely that a court would order a benefit corporation to take certain actions that the plaintiff believes would enhance the achievement of the general or specific public benefit, because that would require the court to monitor the board's conduct, which a court is unlikely to do. [FN61] An alternative remedy would be to remove the directors for cause, a rather drastic remedy, which would be particularly difficult to impose because corporate law provides shareholders with a direct remedy of removal for cause. [FN62] If a corporate shareholder fails to invoke the statutory remedy of removal for cause or fails to obtain the necessary votes to effectuate a removal, it is difficult to see a court invoking its discretionary equitable authority to order removal. There may be other measures that a plaintiff might seek, such as corporate governance changes, but these are unlikely to accomplish very much.

Alternatively, benefit corporation statutes might provide, as the Model Legislation does not, for enforcement by the state attorney general. In the case of traditional nonprofit corporations, state attorneys general currently have standing under common law (and, in some states, by statute [FN63]) under the doctrine of *parens patriae* to sue to enforce the entity's charitable purposes. [FN64] Because, strictly \*1022 speaking, benefit corporations are not nonprofit corporations, it is unlikely that a court would recognize standing on behalf of a state officer to sue the organization for failing to achieve its stated public benefit purposes. Moreover, unlike nonprofit corporations, a benefit corporation has shareholders who can sue directors for failing to pursue the corporation's purposes and who can remove directors (or fail to re-elect them) if the directors are derelict in their duties. The lack of such remedies accounts for the existence of the *parens patriae* cause of action in other contexts. While benefit corporation legislation could empower the state attorney general to police benefit corporations, no state has so acted. Like providing a cause of action to non-shareholders, such a provision would be politically unappealing, resisted by social entrepreneurs and by the attorneys general, who would surely view this as an unwanted addition to their responsibilities.

One commentator has suggested that benefit corporation statutes expressly provide for the award of monetary damages. Drawing on work by Lawrence Mitchell, Steven Munch argues that non-shareholder constituents should have standing to pursue damage actions if they “can show injury to a “legitimate interest.” [FN65] Leaving aside the vagueness of this standard, it poses a political problem: would such legislation draw the support of social entrepreneurs, who would themselves be directors subject to damage actions and/or have to recruit people to serve as directors? Would social entrepreneurs embrace yet another avenue for litigation? It seems that entrepreneurs would be wary of electing benefit corporation status if it exposed them, the entity, and its directors to litigation from remote “stakeholders.”

The suggestion, however, is interesting because it again highlights the rigidity of the Model Legislation. Not only does the Model Legislation expressly preclude the remedy of monetary damages in a benefit enforcement proceeding, it fails to expressly allow benefit corporations to choose to be governed by such a regime. Just as current law in most

states allows a corporation to exculpate directors from monetary damages for breaches of the duty of care, [FN66] the benefit corporation acts could allow benefit corporations to opt to be answerable in damages to non-shareholder constituencies. Such an election would serve as another bonding effect, enhancing the seriousness of the corporation's commitment to its public purposes. If a robust market for the shares of benefit corporations should develop, this bonding effect provides a means by which benefit corporations can compete for investors. Of course, some investors may shy away from corporations with such a provision, fearing that their investment is exposed to diminution from illegitimate, or even legitimate, claims. But others may be attracted to the commitment demonstrated by the corporation, and the articles could limit the amount of damages available in such an action. Perhaps a whole new legal regime will develop, administered by a special arbitration association devoted \*1023 to resolving claims against benefit corporations. The Model Legislation, with its inflexibility and apparent hostility to private ordering, precludes the development of such a legal regime.

Although the limited benefit enforcement proceeding provisions appear to have the intention of providing comfort to directors and shareholders that outsiders will not be able to sue the corporation or its directors, the Model Legislation is drafted in such a way that a claim by non-shareholder constituents based on breach of contract is possible (and, in some jurisdictions, likely). It is conceivable that an expressed specific public benefit is so narrowly drawn that its beneficiaries are limited and identifiable. Such individuals may claim that they are the intended beneficiaries of a contract between the shareholders and the directors, as reflected in the articles of incorporation. [FN67] If so, then the failure of the directors to pursue that specific public benefit may give rise to a claim by those intended beneficiaries, assuming that they could prove damages. Suppose, for instance, that the articles of incorporation of a benefit corporation included a specific public benefit of improving the housing facilities of a specific public housing development. If the directors ignored that specific public benefit, had the resources to do otherwise, and the residents of the development could demonstrate harm that the benefit corporation could have avoided, perhaps the residents could maintain a cause of action against the benefit corporation as a third party contract beneficiary, [FN68] notwithstanding any limitations in the statutory provisions relating to benefit enforcement proceedings. The provision that exculpates corporate directors from monetary liability for breaches of the duty of care, [FN69] commonly found in articles of incorporation, would not apply here, as this is not a breach of fiduciary duty; however, a properly drafted indemnification provision may protect the directors, at least to the extent that the corporation has insurance or other resources to indemnify the directors. [FN70] Regardless, the benefit corporation itself may be liable.

#### D. BENEFIT DIRECTOR

Another important innovation of the Model Legislation is the requirement that a benefit corporation have a "benefit director," [FN71] Who must be independent [FN72] of \*1024 the corporation and whose responsibilities include preparing an opinion, for inclusion in the annual benefit report, as to whether the corporation "acted in accordance with its ... public benefit purpose[s] in all material respects during the period covered by the report" and, if it did not, "a description of the ways in which the benefit corporation or its directors or officers failed to comply." [FN73] The independence requirement is another example of the skepticism of the drafters of the Model Legislation; presumably a person with a financial stake in the corporation--owning, say, more than 5 percent of the outstanding shares--would be too conflicted to provide an unbiased assessment of the corporation's social responsibility. Consequently, the benefit corporation must recruit (and presumably compensate) an outsider to fulfill this function, no doubt a hardship to many well-meaning, closely held benefit corporations. [FN74]

The benefit director does not have an easy task because he or she would, presumably, have to review every decision made by the directors and officers to determine whether the decision furthered the benefit corporation's general and specific public purposes and, of course, if they did not, provide a description of those shortcomings. This outsider would, additionally, be a director of the corporation for all other purposes [FN75] and, thus, would have the duties and responsibilities of a corporate director. For the typical closely held corporation, having a non-owner outsider on the board, reviewing every decision, may be problematic, to say the least, so the public policy question is whether this cost is justified. The need for outsiders suggests that the market will give rise to a \*1025 cadre of professional benefit directors whose retention and compensation may depend on their willingness to give favorable opinions. The skepticism of the Model Legislation drafters is balanced by the operation of free markets: if owners are conflicted out, the market will supply "non-conflicted" directors at a price.

Assuming that an appropriate benefit director is selected, drafting the opinion will prove difficult. The drafters of the Model Legislation chose the language of legal opinions when they wrote that the opinion of the benefit director must address whether the corporation acted appropriately "in all material respects." This language is commonly used in legal opinions when the recipient of the opinion wants the confirmation that its counterparty fully complied with its contractual or legal obligations, understanding that the counterparty may have deviated from those obligations in an immaterial way. [FN76] In the context of the benefit director's opinion, however, this is an odd standard. Bearing in mind that every benefit corporation must have, as a general public purpose, "[pursuing] a material positive impact on society and the environment, taken as a whole," how could a person opine that the corporation acted in accordance with this purpose "in all material respects"? Unlike the typical legal opinion referred to above, the general public purpose does not delineate specific covenants or undertakings of the benefit corporation that a third party could match up against the actions taken by the corporation; rather, it sets forth a vague and general aspiration.

Any opinion that stated, in an unqualified manner, that the benefit corporation acted in accordance with this aspiration "in all material respects" would be a worthless opinion. What a reader might find useful, however, would be a simple confirmation from the benefit director that he or she has reviewed the corporation's annual benefit report and, in his or her opinion, it is accurate or that he or she is unaware of any facts that suggest that the report is inaccurate. In any case, the shareholders and/or other corporate stakeholders may prefer a different sort of presentation by the corporation or a different sort of opinion by the benefit director. For instance, the shareholders may wish to know how much money the corporation spent or how much in foregone revenues the corporation incurred in the course of pursuing the public benefits. While there is nothing in the Model Legislation that prohibits the benefit corporation from providing such information, or being required to do so by its articles or bylaws, such a report or opinion cannot substitute for the rigid specifications of the Model Legislation.

#### E. THE CONSTITUENCY PROVISION

Consistent with the philosophy of the Model Legislation that directors must, as opposed to may, consider the effect of an action, or of inaction, on a wide \*1026 range of stakeholders, the Model Legislation includes a "constituency provision." Section 301(a) of the Model Legislation requires the board of directors and individual directors to consider the effects of any action or instance of inaction upon:

(i) the shareholders of the benefit corporation; (ii) the employees and work force of the benefit corporation, its subsidiaries and its suppliers; (iii) the interests of customers as beneficiaries of the general public benefit or specific public benefit purposes of the benefit corporation; (iv) community and societal factors, including those of each community in which offices or facilities of the benefit corporation, its subsidiaries or its suppliers are located; (v) the local and global environment; (vi) the short-term and long-term interests of the benefit corporation, including benefits that may accrue to the benefit corporation from its long-term plans and the possibility that these interests may be best served by the continued independence of the benefit corporation; and (vii) the ability of the benefit corporation to accomplish its general public benefit purpose and any specific public benefit purpose. [FN77]

The Model Legislation also provides that directors may consider “other pertinent factors or the interests of any other group that they deem appropriate” and that they need not give priority to the interests of any person or group. [FN78] Section 301 inevitably means that directors are likely to face serious conflicts in making policy, with little guidance on how to resolve such conflicts. Although this problem is discussed below, a few other observations are in order.

First, the section mandates that directors only *consider* the effects of their action or inaction upon the various constituencies. What does it mean to consider something? Must there be a discussion at a board meeting of the effect of a proposed course of action on each constituency? If so, it seems inevitable that each board decision on whatever matter (whether or not related to its general or specific public benefit) will be accompanied by a pro forma preamble reciting that, in making a certain decision, the board considered the effect of that decision on the listed constituencies.

Second, this section may affect the usefulness of board decisions by written consents, which typically are used for routine decisions, especially in closely held corporations. For instance, if the chair of the board of directors circulates \*1027 a routine banking resolution for approval by the board, the board will not be able to consider the effect of doing business with that bank on its various stakeholders. The board will actually have to meet and, presumably, consider each constituency in turn. In short, by jettisoning the unanimous written consent, corporate governance in benefit corporations will look quite different than in the typical corporation.

Third, the Model Legislation requires the directors to consider the litany of factors not only when they act, but also when they *fail* to act. The meaning of this is unclear (and especially troubling), inasmuch as the provision specifically applies to each director individually. Suppose the benefit corporation has a specific public benefit of improving employment in its community and a director learns that a firm is considering relocating its operations to that community. Suppose further that a director of the benefit corporation knows that the relocating firm needs financing to accomplish the relocation. If the director does nothing, and the firm decides not to relocate because of a lack of financing, the director arguably has failed the test of section 301(a)(1). Had the director acted, the benefit corporation may have furthered its specific public benefit of improving employment in the community. In short, this section imposes an incalculable burden on directors that cannot be taken seriously.

Fourth, subsection (vi) is an anti-takeover provision, giving the board the freedom to resist a takeover proposal by determining that its long-term interests may be best served by its continued independence. Entrenchment may be inconsistent with the concept of a benefit corporation. Suppose that a social entrepreneur has determined that a benefit corporation is not sufficiently sensitive to the environment and proposes a hostile takeover. The incumbent directors,

seeking to retain their positions in the company, resist the takeover (whether by poison pill or otherwise) and justify their decision on the grounds that the long-term interests of the company are best served by remaining independent. Their success with that defense, which will be difficult for the suitor to overcome, may have a negative effect on the environment or on society or on any specific public benefit of the benefit corporation.

Finally, and perhaps most troublesome, the provision has the effect of freeing directors from accountability. Directors will always be able to rationalize a decision on the basis that it is in the interest of some constituency, especially since the interests of the various constituents are themselves in conflict. A decision to lower prices benefits customers and hurts shareholders. A decision to relocate operations may improve the local and global environment and benefit the community to which the relocation takes place, but harm shareholders, local employees, and current suppliers.

### III. THE DECISION-MAKING CHALLENGES FACED BY THE BOARD

The constituency provision not only creates internal, insoluble conflicts, but also creates potential problems with the general public benefit provision and with any specific public benefit. Suppose a benefit corporation with a specific \*1028 public benefit to promote the employment of underprivileged residents of Community B, where its headquarters are located, had a supplier in Community A before it became a benefit corporation. [FN79] A director proposes that the corporation drop its supplier in Community A and shift its business to a supplier in Community B, despite the fact that the new supplier is considerably more expensive, in the hopes that the new supplier will employ disadvantaged citizens. Notice the myriad of conflicts that arise from this simple, realistic hypothetical. First, the directors must consider whether the possible achievement of the specific public benefit outweighs the interest of shareholders in maximizing profits. Assume that they determine it does. They then must consider the effects of the change on their current supplier and the other constituents listed in the constituency provision. Assume that they determine that the change will have a material and detrimental effect on their current supplier, including the employees of the supplier, as well as on the shareholders of the benefit corporation. How do they resolve the conflict? One might simply conclude that the specific public benefit should prevail; as a matter of general principle, the specific should prevail over the general. [FN80] But suppose they resolve the question the other way, deciding that the increased cost and the detrimental effect on their current supplier and the shareholders of the benefit corporation outweigh the argument for changing suppliers. They then must consider how they would respond to a benefit enforcement proceeding that sought, say, a declaratory judgment that the board violated its fiduciary duty. In short, the demands that the Model Legislation places on directors of a benefit corporation are considerable.

Theorists in the area of decision making have observed that when faced with difficult decisions, decision makers often resort to “second-order decisions,” which Professors Sunstein and Ullmann-Margalit define as “strategies that people use in order to avoid getting into an ordinary decision-making situation in the first instance.” [FN81] In their taxonomy, strategies include rules, presumptions, standards, routines, small steps, picking, delegation, and heuristics. In the context of a director of a benefit corporation making a difficult decision, such as that described above, each strategy has the effect (to a greater or lesser degree) of avoiding the decision. Not all of these are relevant to the context of decision making in a benefit corporation, but rules, presumptions, standards, picking, and delegation seem to be. If the second-order decision is “rules,” a director or the board may adopt a rule to dictate a decision. For instance, a board may decide that when faced with alternatives, it will always choose the one with the least environmental impact. But

would such a rule be consistent with a board's fiduciary **\*1029** duties to consider the effect of its actions on each of the listed constituencies? The use of a “presumption” to that effect, which may be rebutted, ameliorates the problem to some extent, but the board would then have to identify the factors that would overcome the presumption, making this a less attractive strategy.

In contrast to hard and fast rules or presumptions, the board may adopt “standards.” For instance, the board may decide that each of its decisions should have a “positive effect” on the environment. Like presumptions, this strategy leaves considerable discretion to the board when it comes time to make the first-order decision and, for that reason, may be less appealing than adoption of a rule. On the other hand, the adoption of standards may facilitate decision making in a way that is consistent with the demands of a constituency provision.

The “picking” option is one that is particularly troublesome. Sunstein and Ullmann-Margalit observe that “[s]ometimes the difficulty of decision, or symmetry among the options, pushes people to decide on a random basis.” [FN82] The hypothetical situation posed at the beginning of this section may be one in which the directors feel compelled to “just pick.” The difficulty of the decision, and the fact that there is no single rule or presumption to help guide the decision, may encourage at least some directors to choose randomly, to toss a coin. While this may, in fact, be what the directors do, the minutes reflecting the decision would have to be couched in other terms, probably including a rote recitation that the directors considered the effect of their decision on each named constituency.

Finally, and perhaps most salient, is delegation--assigning the decision-making function to a person or committee. This option will be an attractive one to directors of a benefit corporation, who may be expert in making business decisions, but not so expert in evaluating the environmental or societal impacts of their decisions. This alternative is somewhat legally problematic, as directors cannot “abdicate” their statutory obligation to manage the business and affairs of the corporation. [FN83] But irrespective of whether delegation amounts to abdication as a legal matter, the mere temptation to delegate points to the difficulties imposed on directors by the dictates of the Model Legislation.

At least as troubling, research in the field of psychology suggests that board members faced with the inevitable conflicts that arise in managing a benefit corporation may be influenced by a range of factors external to the merits they should be considering. The classical view of decision making, called the “rational theory of choice,” posits that a person chooses from among alternatives to maximize that person's utility or, for a director of a benefit corporation, making that decision that strikes just the “right” balance of societal, environmental, and profit-maximizing goals. Psychologists have long recognized, however, that **\*1030** this view does not adequately explain how people actually make decisions; in fact, experiments have demonstrated that a host of other factors, some of which are discussed in this article, enter into the process. In the context of a corporate director, who obviously is not called upon to maximize his or her personal utility and, as a director of a benefit corporation, must not simply maximize the corporation's profits, other factors that affect decision making in general likely take on greater importance in this context. If a board member would face what psychologists refer to as “negative emotion”--for instance the guilt that may accompany a decision to choose the less environmentally sensitive alternative--avoidance of that negative emotion will affect the decision. If, for instance, the decision is whether to use a local supplier, thereby achieving the specific public benefit of improving job opportunities for low-income residents, or choosing a “greener” supplier outside of the community, a director who is emotionally committed to environmental protection may find it difficult to choose the local supplier and that may influence his or her decision. [FN84] Either choice in this dichotomy satisfies the fiduciary duty of the director

and is therefore unassailable; the upshot, however, is that *business* decisions ultimately are driven by *emotional* considerations. And why not, as the maximization of profit--or any other single factor--may no longer serve as the guiding principle for board decisions. What else, besides emotion, could inform a director's choice between two or more equally worthy--from a moral perspective--alternatives?

Other research, focusing specifically on situations in which the decision maker faces conflicting constituencies, is also troubling. Under such circumstances, a decision maker is motivated to resort to various decision avoidance techniques, such as buckpassing, procrastination, and escape, with the latter being the most extreme form of avoidance. [FN85] While decision makers may work toward compromise, with a view to pleasing the conflicting constituencies, this strategy becomes more difficult to pursue when there are multiple conflicting constituencies. If a director is inclined to conflict avoidance, he or she may well choose to pass the buck to, say, a committee of directors or even to senior management of the benefit corporation, consistent with Sunstein and Ullmann-Margalit's observation of second-order decision making. The delegation of decision-making authority would not have been made to a person or committee because of his or their superior expertise, which would be a defensible delegation, but may be made to avoid making a decision. This would be an unintended and an unfortunate, but perfectly understandable, consequence of the benefit corporation model. \*1031 In short, the benefit corporation model encourages board members to shirk their duties.

Psychologists (and other social scientists) also have recognized that, in decision making, people tend to have a bias to loss aversion. [FN86] This aversion to loss means, among other things, that when there are conflicting constituencies arguing their positions, the constituency that stands to lose from a decision will be more vociferous and motivated than the constituency that will gain from the decision. [FN87] The application of this phenomenon to benefit corporations may mean that a board of directors may find it difficult to shift its policies to favor one constituency when another will be made worse off, thus creating a bias for the status quo. [FN88] What may influence a director's decision, then, is not a weighing of the societal benefits, which is impossible in most instances in any event, but rather a response to "lobbying" efforts by a constituency or their advocates on the board that stand to lose from a decision. In this model, environmental advocates would argue more strenuously--and probably more effectively--against a shift to a less environmentally friendly supplier than they would advocate for a shift to such a supplier. In addition, it is likely reasonable to assume that individuals with a financial interest in the outcome of a decision would be more motivated to lobby for a favorable decision than people who have only a philosophical or moral stake in the outcome. But whether this speculation is accurate or not in any particular case or board decision, the essential point is that directors will face arguments that may be affected by a status quo bias and they, themselves, may be so biased. Moreover, these biases will be more pronounced because traditional profit-based decision making is subordinated and is eliminated as a simple refuge.

Psychological experiments have demonstrated a related phenomenon--the negative impact of having too many choices--that may also have an effect on corporate decision making. For instance, in one experiment participants who were primed to shop for a new CD player were presented a brand named model at a one-day-only sale price of \$99. [FN89] At this price, which the participants were told was well below list price, two-thirds of the participants said they would buy. Another group, similarly primed, was offered the same model at the same sale price together with the top-of-the-line model of another well-known brand at \$159. Under these circumstances, only 54 percent expressed an interest in buying either unit; 46 percent expressed an interest in waiting until they received additional information about the two models. The additional choice created a conflict that caused a substantial number of participants to

prefer the status quo, despite the fact that a substantial majority initially preferred \*1032 the \$99 unit to the status quo. A director faced with multiple socially appealing alternatives may well find it difficult to choose, deferring the decision. While deferring a decision is not per se problematic, the deferral certainly has the consequence, and attendant cost, of having to revisit the issue one or more times and possibly losing valuable opportunities.

Another famous study, presenting more alternatives, also highlights the problem of too many choices. In this study, consumers in a grocery store were presented with six different kinds of jams to sample. [FN90] Forty percent of the consumers sampled the jams and 30 percent purchased one of the varieties. When the number of jams was increased to twenty-four, more people stopped to sample (60 percent of the shoppers), but only 3 percent of those shoppers purchased one. Too many choices simply had a paralyzing effect on the sampled consumers. [FN91] Note that the consumers had a single variable to consider: how they judged the taste of the product. Imagine how much more difficult a decision would have been if they had to take into account the nature (including carbon footprint) of the company that produced the jam (assuming more than one producer), varying price, the effect that their purchase would have on the communities in which the jam was produced, etc. This difficult task is the one faced by the directors of a benefit corporation and, again, psychology research suggests that decision avoidance may be the norm.

While these studies involved students or consumers, another experiment involving neurologists and neurosurgeons confirms the distorting effect that adding alternatives has to the decision-making process. [FN92] In this study, the physicians were asked to decide which of multiple patients awaiting surgery should be first to receive an operation. One group of physicians had to choose between two patients, a woman in her early fifties and a man in his seventies. Only 38 percent of the physicians chose the male patient. A second group of physicians, however, was presented with a third choice, another woman in her fifties, comparable to the other female patient. Under these circumstances, 58 percent of the physicians chose the male patient. This experiment suggests that it was relatively easier to choose the female patient when there was only one, but when there were two, many decision makers were apparently too conflicted to choose either one and opted, instead, for an “easier” choice, avoiding choosing between two equally appealing female cases. Carrying the results of this experiment over to board decisions, one can easily imagine the board conflicted as between two \*1033 environmentally friendly suppliers and choosing, instead, a third supplier on the reasoning that it would benefit the local community. While unobjectionable from a legal perspective, such a decision may be troublesome from an environmental or profitability perspective.

Thus, just as an excessive number of choices has negative effects on consumer welfare, because consumers cannot process and compare the choices available to them, considering an excessive number of factors--as directors of a benefit corporation are required to do--is likely to lead to poorer quality decisions. This is so because when confronted with an increasing number of options and the information related to those options, decision makers are likely to consider a relatively small subset of the total choices otherwise available to them. [FN93] In other words, a director, like any decision maker, is likely to choose to focus on one or two of the multiple constituencies listed in section 301 as a basis for the decision, using some rule or presumption (a “second-order” strategy) to make the decision. Indeed, a director could hardly do otherwise under the circumstances. Moreover, other members of the board would do likewise, focusing on one or two factors to the exclusion of others. As a matter of simple logic, the “favored factors” are likely to vary across the board. It is easy to imagine a situation in which each director chooses a different factor or factors or a different rule or presumption to guide the decision--factors, rules, or presumptions that may, of course, conflict with one another. What sort of decision is likely to emerge from such a situation?

Given the insoluble conflicts that a benefit corporation director faces, the initial constituents of a benefit corporation--the promoter, management, and investors--are well advised to think through how these conflicts should be resolved, to identify precisely what management's obligations are. In this context, participants may recognize, for instance, that a director cannot simultaneously achieve the entity's general public benefit and the identified specific public benefit when they are in conflict. Suppose a social entrepreneur in a rust belt state identifies the salutary specific public benefit of reviving the manufacturing industry in the state. Suppose further that another entrepreneur--a traditional profit-seeking entrepreneur-- approaches our social entrepreneur seeking assistance (say in the form of reduced prices for a needed input) to launch an enterprise that will re-occupy an abandoned factory and employ a thousand workers. Our social entrepreneur, acting in good faith, believes that the project is sound and, more than anything else that he or she has seen, would further the benefit corporation's specific public benefit of reviving industry in the state. There is one **\*1034** hitch, however. The new enterprise would manufacture gas-powered lawn mowers, which would not have a material positive impact on the environment. Indeed, our social entrepreneur concludes that the factory would have a detrimental effect on the environment, not only with respect to the product it would produce, but also in the way the factory would be operated: it would use as a power source the local utility, which is coal-fired.

The directors' burden would be much relieved if they could prioritize the specific public benefit, and the Model Legislation seems to permit the directors to do so, if the articles of incorporation so provide. Section 301(a)(3) allows the board to give priority to "the interests of a particular person or group" if the articles state the "intention to give priority to certain interests related to [the corporation's] accomplishment of its general public benefit purpose or of a specific public benefit purpose identified in its articles." Organizers of a benefit corporation would be well advised to draft the articles of incorporation and take advantage of this provision if the corporation has identified a specific public benefit. Unfortunately, this prioritization may cover only a small subset of the difficult decisions that benefit corporation directors are likely to face and is, in any case, less than clear. In the context of the hypothetical posed in the preceding paragraph, suppose the articles provided that in making decisions, the corporation shall give priority to alternatives that promote local employment. Does this mean that environmental concerns can be ignored? If not, what weight should they be given? If they may be ignored, how can the corporation satisfy its obligation to "create" the general public benefit of a material positive impact on the environment? The Model Legislation provides no answers to these questions.

#### **IV. WHY NOT TWO LAWS?**

What I have written to this point might lead one to conclude, as have the supporters of the Model Legislation, that though flawed and inflexible, the Model Legislation does provide a template for the social entrepreneur who agrees with the philosophy of the Model Legislation. Moreover, despite its flaws, the Model Legislation provides the promise of at least some measure of uniformity across states so that investors and consumers have a sense of what it means to be a "benefit corporation." This branding effect would be lost, or at least significantly diminished, if more flexible benefit corporation statutes, varying widely from state to state, were to be adopted. The supporters of the Model Legislation conclude, therefore, that unless proposed state benefit corporation legislation substantially conforms to the Model Legislation, they will actively oppose it and lobby for the Model Legislation. [FN94] They argue that supporters of a more flexible form of socially responsible corporation are free to propose and lobby for that sort of legislation; they just cannot call the resulting entity a "benefit corporation." Indeed, California has adopted legislation

modeled on the Model \*1035 Legislation and a second act (actually introduced before the benefit corporation legislation), providing for the creation of “flexible purpose corporations” and reflecting some of the flexibility lacking in the Model Legislation. Though appealing, and despite the California solution, this argument is flawed.

First, a state legislature may reach the judgment that, for the reasons set forth here and elsewhere, [FN95] the Model Legislation is just not competently drafted. The requirement, for instance, that the general public benefit of a benefit corporation have material positive impact on *both* society and the environment may be viewed by the legislature as too narrow, deterring companies that are particularly committed to the environment, and unsure of what a material societal benefit means, from electing benefit corporation status. The legislature may wish to encourage such entrepreneurs to use the benefit corporation law. Or, the legislature may reach the judgment that the added expense to a benefit corporation of appointing a benefit director is not justified by the added value such a person would bring. [FN96] In short, a legislature may reach the good faith judgment that the benefits of uniformity and branding are not justified by the costs of the legislation.

Second, a state legislature might well be concerned that adding two new forms of business entities to the current mix (a Model Legislation benefit corporation and a more flexible socially responsible corporation) is unwise as a matter of public policy. The proliferation of business organizations is confusing to the public and the bar. In recent years, legislatures have added limited liability companies, [FN97] low profit limited liability companies (so-called L3Cs), [FN98] limited liability partnerships, [FN99] and limited liability limited partnerships [FN100] to the roster of business entities from which entrepreneurs and their lawyers may choose. Adding two new non-traditional corporations adds confusion without a corresponding benefit. A legislature may reasonably conclude that it makes sense to provide social entrepreneurs with an entity that requires the directors to consider nonprofit maximizing policies and, to signal to consumers [FN101] and investors that that is the case, call such an entity a benefit corporation. After all, the term benefit corporation is becoming more widely known and, likely, is associated broadly with the idea of social entrepreneurship. It is unlikely that the general \*1036 public would ever be familiar with the nuanced and varied (from state to state) legislation under which such corporations operate and would likely be confused by the difference between a flexible purpose corporation and a benefit corporation.

## V. CONCLUSION

Some have argued that benefit corporation legislation is unnecessary because current corporate statutes provide the necessary flexibility to allow social entrepreneurs to pursue non-profit maximizing strategies. This is probably correct, but it is beside the point. The purpose of benefit corporation acts is not just to free up social entrepreneurs from the perceived constraints of profit maximization, but to create a form that mandates non-profit maximizing behavior. The Model Legislation, which has been drafted to achieve that end, is at the same time too broad and too narrow. It is too broad because it seeks to accomplish too much. Requiring that each corporation has as its purpose a general public benefit in addition to any desired specific public benefit unnecessarily complicates the decision-making process of the board of directors. At the same time, the Model Legislation is too narrow. A social entrepreneur may have a minimal interest in profits and, indeed, so represent the venture to potential investors as one devoted to achieving a specific public benefit. For instance, suppose a social entrepreneur wanted to improve the quality of public school education in the community by creating an organization to supply building maintenance services to the public school system at reduced prices, thereby freeing up resources of the school district for educational purposes. People who share the goal

of improving public education may “invest” in the enterprise. It is understood, however, that the “investor” cannot expect a market return on the investment and, instead, should view the investment, at least in part, as a non-deductible contribution to achieve a favorable social outcome. Such an investor, however, may not want the goal of improving the public schools to be subordinated to a general public benefit or to the interests of other constituencies, such as employees, suppliers, etc. The Model Legislation is too narrow to permit this deviation; neither the social entrepreneur who created the benefit corporation, nor the board of directors that operates it, has the freedom to vary the rigid requirements of the Model Legislation.

The directors of a benefit corporation are charged with an impossible task, and both theory and empirical evidence suggest that the quality of their decision making will suffer as a result. The impetus behind benefit corporation legislation is that directors should act in a socially responsible fashion, but the means chosen by its proponents may not achieve that goal. At bottom, the proponents of the Model Legislation simply do not trust directors of traditional corporations to be socially responsible in their decision making; if they did, the benefit corporation legislation would be much simpler. It would allow, but not require, directors to factor in the effect of their decisions on other corporate constituencies and, more broadly, on society and the environment. Corporations could be **\*1037** encouraged, but not required, to disclose the extent to which non-profit maximizing considerations affected their decisions. Investors, armed with this knowledge, could direct their investment dollars accordingly. Socially responsible mutual funds are readily available, as are ratings of the social responsibility conduct of corporations. More flexible legislation would allow corporations to identify the specific public benefits that they will pursue. Directors overseeing such corporations would consider the extent to which their decisions further that specific public benefit in the same way that they consider the impact of their decisions on the “bottom line.” Conceivably, a corporate charter or other guiding document could quantify the cost, in terms of foregone profit or allocation of revenue, the corporation would bear to achieve that specific public benefit. In short, the proponents of benefit corporations have eschewed the powerful role that markets and private ordering could play in furthering the goal of greater social responsibility on the part of America's businesses.

A recent provocative article in the Harvard Business Review, *Creating Shared Value*, [FN102] points in a different direction from the Model Legislation, while addressing the same concern. The authors, a distinguished Harvard professor (Michael Porter) and a co-founder of a global social impact consulting firm (Mark Kramer), argue that business professionals must reconsider traditional business practices that seek to maximize short-term profits and, instead, seek to “create value for society by addressing its needs and challenges.” [FN103] They argue, persuasively in my view, that preserving local communities, improving worker conditions, adopting energy saving means of production, etc., which they term “creating shared value,” may result in greater long-term profitability. In example after example, they demonstrate how choosing what might be characterized as socially responsible policies resulted in stronger companies with better long-term prospects. A similar argument is made in recent books by John Mackey (of Whole Foods fame) and Raj Sisodia, titled *Conscious Capitalism*, [FN104] and Professor Lynn Stout, titled *The Shareholder Value Myth: How Putting Shareholders first Harms Investors, Corporations, and the Public*. [FN105] These and other commentators [FN106] believe that the prevailing ethos of maximizing short-term share prices **\*1038** harms businesses' long-term value. On this view, getting corporate managers to think long term is in the interests their businesses and of society. The problem that B Lab is seeking to address, then, may not a problem of law, but one of business strategy. In short, managers need to be more cognizant of how creating shared value (to use Porter and Kramer's terminology) or acting in the interests of long-term investors (as others argue) has the effect that benefit corporation legislation seeks to achieve. The real challenge, if they are right, is creating the cultural shift that is nec-

essary. It is, of course, beyond the scope of this article--and especially in a concluding section--to grapple with that question. Suffice it to say, the answer to creating more socially responsible corporations may lie in the classrooms of business schools and not in the halls of state legislatures.

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[FN1]. Many scholars recognize that the famous exchange of articles between Professors Berle and Dodd was critical in launching the debate on a corporation's social responsibility. The debate is set forth in three articles by Berle and Dodd. A.A. Berle, Jr., *Corporate Powers as Powers in Trust*, 44 HARV. L. REV. 1049 (1931) (arguing that corporate managers should be constrained in their decision making); E. Merrick Dodd, Jr., *For Whom Are Corporate Managers Trustees?*, 45 HARV. L. REV. 1145 (1932) (arguing, contra to Berle, that corporate managers only owe a duty to their stockholders to make a profit); A.A. Berle, Jr., *For Whom Corporate Managers Are Trustees: A Note*, 45 HARV. L. REV. 1365 (1932) (countering Dodd by arguing that corporate managers affect more than just their stockholders and constraints on their actions are justified). The debate has not abated. *See, e.g.*, David L. Engle, *An Approach to Corporate Social Responsibility*, 32 STAN. L. REV. 1, 7 n.26 (1979) (discussing the Berle-Dodd debate on corporate social responsibility); A.A. Sommer, Jr., *Who Should the Corporation Serve? The Berle-Dodd Debate Revisited Sixty Years Later*, 16 DEL. J. CORP. L. 33 (1991) (discussing constituency statutes and corporate social responsibility); C.A. Harwell Wells, *The Cycles of Corporate Social Responsibility: An Historical Retrospective for the Twenty-First Century*, 51 U. KAN. L. REV. 77 (2002) (giving an historical perspective).

[FN2]. The question as to whether directors of a for-profit corporation have a fiduciary duty to maximize shareholder value is a question that has been explored extensively in legal literature, much of it recent, and it would serve no purpose to revisit that question here. *See, e.g.*, STEPHEN M. BAINBRIDGE, CORPORATION LAW AND ECONOMICS §§ 1.4(b), 9.2, 9.3 (2002); WILLIAM H. CLARK, JR. ET AL., THE NEED AND RATIONALE FOR THE BENEFIT CORPORATION: WHY IT IS THE LEGAL FORM THAT BEST ADDRESSES THE NEEDS OF SOCIAL ENTREPRENEURS, INVESTORS, AND, ULTIMATELY, THE PUBLIC 7-41 (2012) [hereinafter WHITE PAPER], available at [http://benefitcorp.net/storage/documents/The\\_Need\\_and\\_Rationale\\_for\\_Benefit\\_Corporations\\_April\\_2012.pdf](http://benefitcorp.net/storage/documents/The_Need_and_Rationale_for_Benefit_Corporations_April_2012.pdf); LYNN STOUT, THE SHAREHOLDER VALUE MYTH: HOW PUTTING SHAREHOLDERS FIRST HARMS INVESTORS, CORPORATIONS, AND THE PUBLIC 29 (2012) (arguing that directors are not legally obligated to maximize shareholder value, asserting that "courts refuse to hold directors of public corporations legally accountable for failing to maximize shareholder wealth"); Jonathan R. Macey, *A Close Read of an Excellent Commentary on Dodge v. Ford*, 3 VA. L. & BUS. REV. 177, 179 (2008); Ashley Schoenjahn, *New Faces of Corporate Social Responsibility: Will New Entity Forms Allow Businesses to Do Good?*, 37 J. CORP. L. 453, 455-59 (2012); Judd F. Sneirson, *Green is Good: Sustainability, Profitability, and a New Paradigm for Corporate Governance*, 94 IOWA L. REV. 987, 1001-03 (2009) (doubting that the sparse case law on the subject supports the notion of profit maximization). *See also* articles cited in *supra* note 1, each of which deals, more or less, with this question. As the authors establish, there is little case law supporting the principle that directors act in breach of their fiduciary duty

if they fail to maximize shareholder value, and no case law that imposes liability on directors in a state that has a constituency statute described in *infra* note 3. But with regard to the lack of a duty to maximize shareholder value, see *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, 506 A.2d 173 (Del. 1986) (holding that when a corporation is being sold the directors must act to maximize the value of the company for the stockholders' benefit). If any doubt remains that a constituency statute does not adequately protect directors from liability, state law could easily and simply be amended to so provide. The supporters of benefit corporation legislation described in this article seek much more than to protect directors who elect to make socially responsible, but profit sacrificing, decisions; the supporters seek to require directors to make such decisions. It is, thus, inaccurate to argue, as some have, that benefit corporation legislation is needed because directors of traditional corporations are locked into a profit-maximizing paradigm. WHITE PAPER, *supra*, at 6.

[FN3]. Under the provisions of so-called “constituency statutes,” directors are free to consider the interests of corporate stakeholders other than shareholders when making business decisions. All but nineteen states have adopted constituency statutes, which vary from jurisdiction to jurisdiction. *See, e.g.*, 805 ILL. COMP. STAT. ANN. 5/8.85 (West, Westlaw through P.A. 98-108, with the exception of P.A. 98-104, of the 2013 Reg. Sess.) (stating directors “may ... consider the effects of any action ... upon employees, suppliers and customers of the corporation or its subsidiaries, communities in which offices or other establishments of the corporation or its subsidiaries are located, and all other pertinent factors”); N.Y. BUS. CORP. LAW § 717(b)(2)(i)-(v) (McKinney, Westlaw through L. 2013, chapters 1 to 57 and 60 to 110) (stating directors “shall be entitled to consider ... the effects that the corporation's actions may have in the short-term or in the long-term upon any of the following: (i) the prospects for potential growth, development, productivity and profitability of the corporation; (ii) the corporation's current employees; (iii) the corporation's retired employees and other beneficiaries receiving or entitled to receive retirement, welfare or similar benefits from or pursuant to any plan sponsored, or agreement entered into, by the corporation; (iv) the corporation's customers and creditors; and (v) the ability of the corporation to provide, as a going concern, goods, services, employment opportunities and employment benefits and otherwise to contribute to the communities in which it does business”); 15 PA. CONS. STAT. ANN. § 1715(a)(1) (West, Westlaw through Regular Section Act 2013-11) (stating directors may consider “[t]he effects of any action upon any or all groups affected by such action, including shareholders, employees, suppliers, customers and creditors of the corporation, and upon communities in which offices or other establishments of the corporation are located”). In addition to these three states, some thirty other states have constituency statutes that protect directors who take into account non-shareholder concerns in their decision making. *See* ARIZ. REV. STAT. ANN. § 10-2702 (West, Westlaw through legislation effective June 20, 2013 of the First Regular Session of the Fifty-First Legislature); CONN. GEN. STAT. ANN. § 33-756(D) (West, Westlaw through Public Acts enrolled and approved by the Governor on or before June 25, 2013 and effective on or before July 1, 2013); FLA. STAT. ANN. § 607.0830(3) (West, Westlaw ch. 272 (End) of the 2013 1st Reg. Sess. of the Twenty-Third Legislature); GA. CODE ANN. § 14-2-202(B)(5) (West, Westlaw through end of the 2013 Regular Session); HAW. REV. STAT. § 414-221(A)-(B) (West, Westlaw through Act 140 of the 2013 Regular Session); IDAHO CODE ANN. § 30-1602 (West, Westlaw through (2013) Chs. 1-354 (End)); IND. CODE ANN. § 23-1-35-1(D) (West, Westlaw through 2013 legislation); IOWA CODE ANN. § 490.1108A (West, Westlaw through legislation from the 2013 Regular Session); KY. REV. STAT. ANN. § 271B.12-210(4) (West, Westlaw through the end of the 2012 Regular Session and the 2012 First Extraordinary Session); LA. REV. STAT. ANN. § 12:92(G) (West, Westlaw through the 2012 Regular Session); ME. REV. STAT. ANN. tit. 13-C, § 832 (West, Westlaw through emergency legislation through Chapter 367 and 369 through 427 of the 2013 First Regular Session of the 126th Legislature); MD. CODE ANN., CORPS. & ASS'NS § 2-104(B)(9) (West, Westlaw through all chapters of the 2013 Regular Session of

the General Assembly, effective through July 1, 2013); MASS. GEN. LAWS ANN. ch. 156B, § 65 (West, Westlaw through Chapter 35 of the 2013 1st Annual Session); MINN. STAT. ANN. § 302A.251(5) (West, Westlaw through laws of the 2013 Regular Session, Chapters 1 to 39; 41; 45; 54; 57; 58; 63, section 14; 66 to 68; 70, sections 1 to 6; 71; 73, sections 2, 4, 5; 74; 79; 80; and 116, Article 2, sections 8, 9, 11, 12, and Article 3, sections 10 to 12, 14 to 16, 22); MISS. CODE ANN. § 79-4-8.30 (West, Westlaw through general laws from the 2013 Regular Session); MO. ANN. STAT. § 351.347(1) (West, Westlaw through emergency legislation approved through July 1, 2013, of the 2013 First Regular Session of the 97th General Assembly); NEB. REV. STAT. ANN. § 21-2432(2) (West, Westlaw through 102d Legislature Second Regular Session (2012)); NEV. REV. STAT. ANN. § 78.138(4) (West, Westlaw through the 2011 76th Regular Session of the Nevada Legislature, and technical corrections received from the Legislative Counsel Bureau (2012)); N.J. STAT. ANN. § 14A:6-1(2) (West, Westlaw through L. 2013, c. 84 and J.R. No. 9); N.M. STAT. ANN. § 53-11-35(D) (West, Westlaw through Ch. 228 (end) of the First Regular Session of the 51st Legislature (2013)); N.D. CENT. CODE ANN. § 10-19.1-50(6) (West, Westlaw through 2011 Regular and Special Sessions of the 62d Legislative Assembly); OHIO REV. CODE ANN. § 1701.59(E) (West, Westlaw through 2013 Files 24 and 26 to 38 of the 130th GA (2013-2014)); OR. REV. STAT. ANN. § 60.357 (West, Westlaw through emergency legislation through Ch. 622 of the 2013 Reg. Sess.); R.I. GEN. LAWS ANN. § 7-5.2-8 (West, Westlaw through amendments through chapter 66 of the 2013 Regular Session); S.D. CODIFIED LAWS § 47-33-4 (West, Westlaw through 2013 Regular Session and Supreme Court Rule 13-08); TENN. CODE ANN. § 48-103-204 (West, Westlaw through 2013 First Reg. Sess., eff. through June 30, 2013 and Ch. 390, eff. July 1, 2013); VT. STAT. ANN. tit. 11A, § 8.30 (West, Westlaw through law No. 53 of the First Session of the 2013-2014 Vermont General Assembly (2013)); VA. CODE ANN. § 13.1-727.1 (West, Westlaw through End of the 2013 Reg. Sess. and the End of the 2013 Sp. Sess. I); WIS. STAT. ANN. § 180.0827 (West, Westlaw through 2013 Wisconsin Act 19, published 6/28/2013); WYO. STAT. ANN. § 17-16-830(E) (West, Westlaw through 2013 General Session).

[FN4]. The amendment would consist of the addition of a “constituency statute.” In the White Paper, the authors suggest a reason why benefit corporation legislation is needed even in those states with a constituency statute:

Even in states with constituency statutes, the creation of a new corporate entity provides additional legal clarity that the fiduciary duty of directors of a benefit corporation includes consideration of stakeholder interests and that shareholders have the right to enforce that standard of consideration.

WHITE PAPER, *supra* note 2, at 6. This statement is true enough, but if the problem is a narrow one of clarifying the fiduciary duties of directors, a new statute is hardly needed.

[FN5]. Hawaii has decided to call its version of a benefit corporation a “sustainable business corporation.” HAW. REV. STAT. § 420D-2 (West, Westlaw through Act 140 of the 2013 Regular Session).

[FN6]. The Model Legislation is attached as Appendix A to the White Paper, *supra* note 2.

[FN7]. The states that adopted or rejected the Model Legislation are set out in *infra* notes 15 and 16, respectively. It is noteworthy, as developed below, that no state has adopted the Model Legislation without change and the Model Legislation itself has been modified from time to time.

[FN8]. *E.g.*, REVISED MODEL NONPROFIT CORP. ACT § 13.0 (1987). The Act is *available at* <http://goo.gl/2cVLHt>.

[FN9]. SOCIAL INV. FORUM FOUND., REPORT ON SOCIALLY RESPONSIBLE INVESTING TRENDS IN THE UNITED STATES 10 (2010), available at [http://www.ussif.org/files/Publications/10\\_Trends\\_Exec\\_Summary.pdf](http://www.ussif.org/files/Publications/10_Trends_Exec_Summary.pdf).

[FN10]. See generally HOPE CONSULTING, STRATEGIES FOR SOCIAL CHANGE, MONEY FOR GOOD REPORT (2010), available at [http://www.hopeconsulting.us/wordpress/wp-content/uploads/2013/03/MFGI-Full\\_July-2010.pdf](http://www.hopeconsulting.us/wordpress/wp-content/uploads/2013/03/MFGI-Full_July-2010.pdf).

[FN11]. Leo E. Strine, Jr., Our Continuing Struggle with the Idea that For-Profit Corporations *Seek Profit*, 47 WAKE FOREST L. REV. 135, 150 (2012). Of course, with the growing number of states adopting and considering the Model Legislation, the “fictional land” to which Chancellor Stine refers is rapidly becoming non-fiction.

[FN12]. See authorities cited in *supra* note 2.

[FN13]. E.g., J. William Callison, *Putting New Sheets on a Procrustean Bed: How Benefit Corporations Address Fiduciary Duties, The Dangers Created, and Suggestions for Change*, 2 AM. U. BUS. L. REV. 85 (2012); Christopher Lacovara, *Strange Creatures: A Hybrid Approach to Fiduciary Duty in Benefit Corporations*, 2011 COLUM. BUS. L. REV. 815; Alissa Mickels, *Beyond Corporate Social Responsibility: Reconciling the Ideals of a For-Benefit Corporation with Director Fiduciary Duties in the U.S. and Europe*, 32 HASTINGS INT'L & COMP. L. REV. 271 (2009); Steven Munch, *Improving the Benefit Corporation: How Traditional Governance Mechanisms Can Enhance the Innovative New Business Form*, 7 NW. J.L. & SOC. POL'Y 170 (2012); J. Haskell Murray, *Choose Your Own Master: Social Enterprise, Certifications and Benefit Corporation Statutes*, 2 AM. U. BUS. L. REV. 1 (2012); Ashley Schoenjahn, *New Faces of Corporate Social Responsibility: Will New Entity Forms Allow Businesses to Do Good?*, 37 J. CORP. L. 453, 455-59 (2012).

[FN14]. Some states have opted for both a benefit corporation act and a more flexible form of socially responsible corporation. See, e.g., California Flexibility Act, 2011 Cal. Legis. Serv. ch. 740 (S.B. 201) (West) (filed with the Secretary of State Oct. 9, 2011), discussed in Christen Clarke, *California's Flexible Purpose Corporation: A Step Forward, A Step Back, or No Step at All*, 5 BUS., ENTREPRENEURSHIP & L. 301 (2012).

[FN15]. See California, Assemb. B. 361, 2011-2012 Reg. Sess. (Cal. 2011); Colorado, H.B. 13-1138, 69th Gen. Assemb., 1st Reg. Sess. (Colo. 2013); Delaware, S.B. 47, 147th Gen. Assemb., Reg. Sess. (Del. 2013); Hawaii, S.B. 298, 26th Leg., 2011 Reg. Sess. (Haw. 2011); Illinois, S.B. 2897, 98th Gen. Assemb., 2012 Sess. (Ill. 2012); Louisiana, H.B. 1178, 38th Reg. Sess. (La. 2012); Maryland, H.B. 1178, 427th Gen. Assemb. (Md. 2010); Massachusetts, H.B. 4352, 187th Leg., 2011-2012 Sess. (Mass. 2012); New Jersey, S.B. 2170, 214th Leg., Reg. Sess. (N.J. 2010); New York, S.B. S00079, 2011-2012 Reg. Sess. (N.Y. 2011); Pennsylvania, H.B. 1616, 196th Gen. Assemb., 2011-2012 Sess. (Pa. 2012); South Carolina, H.B. 4766, 119th Gen. Assemb., 2d Sess. (S.C. 2012); Vermont, S.B. 263, 2009-2010 Leg. Sess. (Vt. 2010); Virginia, H.B. 2358, 2011 Reg. Sess. (Va. 2011); Washington, H.B. 2239, 2012 Reg. Sess. (Wash. 2012).

The state of Washington adopted legislation patterned after the Model Legislation and the California flexible purpose corporation act, see *supra* note 14. Entities formed under the Washington law are called “special purpose

corporations.”

[FN16]. Alabama, S.B. 569, 2012 Reg. Sess. (Ala. 2012); Connecticut, S.B. 5490, Gen. Assemb., Feb. 2012 Sess. (Conn. 2012); Florida, H.B. 757, 114th Reg. Sess. (Fla. 2012); District of Columbia, L.B. 19-0584, 19th Period (D.C. 2011); Michigan, S.B. 359, 96th Leg., 2011 Reg. Sess. (Mich. 2011); Minnesota, H.F. 2499, 87th Legis. Sess., 2d Reg. Sess. (Minn. 2012); North Carolina, S.B. 26, 2011 Gen. Assemb., 2012 Reg. Sess. (N.C. 2011); Pennsylvania, S.B. 433, 195th Gen. Assemb., 2011-2012 Sess. (Pa. 2011); Wisconsin, A.B. 742, 100th Legis., 2011-2012 Reg. Sess. (Wis. 2012).

[FN17]. The legislation was introduced in the 2011 session as Senate Bill 11-005, in the 2012 session as Senate Bill 12-182, and in a special session held in 2012 as Senate Bill S-003. As to the history of the Colorado legislation, see Herrick K. Lidstone, Jr., *Benefit Corporations: New Breed or Old Wine in New Skins?*, L. WK. COLO., May 28, 2012, at 16.

[FN18]. This information is provided on the B Lab website:

Jay Coen Gilbert, Bart Houlahan, and Andrew Kassoy [the “Co-Founders”] share passion for creating a better world through business and have been friends for over 20 years. Prior to B Lab, Jay and Bart were Co-Founder and President, respectively, of AND 1, a \$250 million basketball footwear and apparel business. Andrew has spent his entire career as a private equity investor; most recently as a Partner at MSD Real Estate Capital, a \$1 billion real estate fund controlled by MSD Capital, the investment vehicle for the assets of Michael Dell and the Michael and Susan Dell Foundation.

*Our Team*, B LAB, <http://www.bcorporation.net/what-are-b-corps/the-non-profit-behind-b-corps/ourteam> (last visited Aug. 10, 2013). The website also contains additional information about each of these founders.

[FN19]. *The Non-Profit Behind B Corps*, B LAB, <http://www.bcorporation.net/what-are-b-corps/the-nonprofitbehind-b-corps> (last visited Aug. 10, 2013).

[FN20]. *How to Become a B Corp*, B LAB, <http://www.bcorporation.net/become-a-b-corp/how-to-become-a-b-corp> (last visited Aug. 10, 2013). The certification process is not limited to corporations; limited liability companies may also be certified and the B Lab website lists a number that have.

[FN21]. *Id.*

[FN22]. *Id.*

[FN23]. *Id.* It appears that an entity (corporation or limited liability company) may obtain the B Lab certification even if, in the case of a corporation, it does not incorporate under the state's benefit corporation statute, at least if such a statute is unavailable when certification from B Lab is sought. This is an inference from the fact that several Colorado corporations have received B Lab certification notwithstanding the fact that Colorado had not adopted benefit corporation legislation. Moreover, anecdotal evidence suggests that B Lab does not, in fact, take any action if a certified corporation fails to adopt benefit corporation status.

[FN24]. *Find a B Corp*, B LAB, <http://www.bcorporation.net/community/find-a-b-corp> (last visited Aug. 10, 2013).

[FN25]. *Id.*

[FN26]. There is evidence that at least some consumers attach value to products produced by sustainable businesses. *See, e.g., A Look at Sustainability in the USA*, NAT'L MARKETING INST., <http://nmi-solutions.com/index.php/research-reports/us-sustainability-report> (last visited Sept. 1, 2013).

[FN27]. The Hawaii statute uses the term “sustainable business corporation” in lieu of benefit corporation. HAW. REV. STAT. § 420D-2 (West, Westlaw through Act 140 of the 2013 Regular Session).

[FN28]. MODEL BENEFIT CORP. LEGIS. § 201 (B Lab 2013), *available at* [http://benefitcorp.net/storage/documents/Model\\_Benefit\\_Corporation\\_Legislation.pdf](http://benefitcorp.net/storage/documents/Model_Benefit_Corporation_Legislation.pdf). This definition has been modified in a number of jurisdictions. Vermont's law provides, for instance, that a general public benefit means “a material impact on society and the environment, as measured by a third-party standard, through activities that promote some combination of specific public benefits.” VT. STAT. ANN. tit. 11A, § 21.03(a)(4) (West, Westlaw through Law No. 53 of the First Session of the 2013-2014 Vermont General Assembly (2013), except for Law Nos. 29, 50 and 51, and laws and sections of laws effective July 1, 2013, and later).

[FN29]. MODEL BENEFIT CORP. LEGIS. § 102(a). This definition has not been uniformly adopted. The New Jersey legislation, for instance, defines “general public benefit” as “a material positive impact on society and the environment by the operations of a benefit corporation through activities that promote some combination of specific public benefits.” N.J. STAT. ANN. 14A:18-1 (West, Westlaw through Laws effective through L. 2013, c. 84 and J.R. No. 9). Similarly, Maryland law omits the phrase, “taken as a whole.” MD. CODE ANN., CORPS. & ASS'NS § 5-6C-01(c) (West, Westlaw through all chapters of the 2013 Regular Session of the General Assembly, effective through July 1, 2013).

[FN30]. MODEL BENEFIT CORP. LEGIS. § 201(b).

[FN31]. *Id.* § 102(a).

[FN32]. I am indebted to the members of my committee for pointing this out. *See supra* \* footnote.

[FN33]. In addition to legislation providing for the formation of a benefit corporation, California has adopted legislation allowing the formation of a “flexible purpose corporation,” which may have as its purpose what are, essentially, specific public benefits. A California flexible purpose corporation does not have to include among its purposes a general public benefit. CAL. CORP. CODE § 2602 (West, Westlaw through Ch. 30 of the 2013 Reg. Sess.). *See generally* Christen Clarke, *California's Flexible Purpose Corporation: A Step Forward, A Step Back, or No Step at All*, 5 BUS., ENTREPRENEURSHIP & L. 301 (2012).

[FN34]. MODEL BENEFIT CORP. LEGIS. § 401(a). The Vermont act requires that the report be submitted to the shareholders for their approval or rejection. VT. STAT. ANN. tit. 11A, § 21.14(c) (West, Westlaw through Law No. 53 of the First Session of the 2013-2014 Vermont General Assembly (2013), except for Law Nos. 29, 50 and 51, and laws and sections of laws effective July 1, 2013, and later). Vermont law does not indicate what consequences, if any, flow from a rejection by shareholders. The New Jersey law provides that a benefit corporation may lose its status as such, subject to reinstatement, if it fails to file such a report for two years. N.J. STAT. ANN. 14A:18-11(d)(2) (West, Westlaw through Laws effective through L. 2013, c. 84 and J.R. No. 9).

[FN35]. MODEL BENEFIT CORP. LEGIS. § 102(a). While the Model Legislation includes factors by which to judge that independence, not all benefit corporation legislation has retained that provision. *See, e.g.*, N.J. STAT. ANN. 14A:18-1 (West, Westlaw through Laws effective through L. 2013, c. 84 and J.R. No. 9).

[FN36]. MODEL BENEFIT CORP. LEGIS. § 102(a). Legislation in several states severely edited the criteria that delineate comprehensive, credible, and transparent. *See, e.g.*, HAW. REV. STAT. § 420D-12 (West, Westlaw through Act 140 of the 2013 Regular Session); MD. CODE ANN., CORPS. & ASS'NS § 5-6C-01(e) (West, Westlaw through all chapters of the 2013 Regular Session of the General Assembly, effective through July 1, 2013); N.J. STAT. ANN. 14A:18-1.

[FN37]. Unlike the Model Legislation, the Vermont statute, for instance, does not specify what constitutes independence. VT. STAT. ANN. tit. 11A, § 21.03(a)(8) (West, Westlaw through Law No. 53 of the First Session of the 2013-2014 Vermont General Assembly (2013), except for Law Nos. 29, 50 and 51, and laws and sections of laws effective July 1, 2013, and later). Several acts contain a much stripped-down provision on the requirements for a third-party standard. *See* N.Y. BUS. CORP. § 1702 (McKinney, Westlaw through L. 2013, chapters 1 to 57 and 60 to 110); VA. CODE ANN. § 13.1-782 (West, Westlaw through through the end of the 2013 Reg. Sess. and the end of the 2013 Sp. Sess. I). The Maryland law omits most of the disclosures required under the Model Legislation.

[FN38]. *E.g.*, CAL. CORP. CODE § 14630(a)(2) (West, Westlaw through Ch. 70 of 2013 Reg. Sess.).

[FN39]. Interestingly, I have not run across any limitation on the use of the word “benefit” in the name of a corporation that is not organized as a benefit corporation and, indeed, many non-benefit corporations do include the word in their name. For instance, companies that administer employee benefits may have the word “benefit” in their name. *See, e.g.*, Three Rivers Benefit Corporation, an Iowa corporation founded in 1975, with a web address of <http://www.threeriversbenefit.com/>.

[FN40]. The European Union currently encourages companies to disclose voluntarily their performance on corporate social responsibility issues. *See* Ruben Zandvliet, *Corporate Social Responsibility Reporting in the European Union: Toward a More Univocal Framework*, 18 COLUM. J. EUR. L. 38 (2011).

[FN41]. *See, e.g.*, Michael C. Jensen & William H. Meckling, *Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure*, 3 J. FIN. ECON. 305 (1976) (discussing bonding mechanisms).

[FN42]. *See supra* note 20 and accompanying text. Apparently, B Lab does not audit benefit corporations seeking

certification at the time certification is sought.

[FN43]. See generally *Guide to Green Symbols*, EASY WAYS TO GO GREEN (Apr. 27, 2008), <http://www.easywaystogogreen.com/green-guides/guide-to-green-symbols/>.

[FN44]. *Our Corporate Culture*, BIG BAD WOOF, [http:// www.bbwoofinc.com/business\\_phlosophy.php](http://www.bbwoofinc.com/business_phlosophy.php) (last visited Aug. 10, 2013).

[FN45]. *Id.*

[FN46]. *B Consumer Report*, BB WOLF INC. (June 21, 2011), [http:// thebigbadwoof.com/files/My%20B%20Report2011.pdf](http://thebigbadwoof.com/files/My%20B%20Report2011.pdf). The composite score appears to be the sum of points earned in the following categories: accountability, employees, consumers, community, and environment. However, the report does not indicate the scale, maximum number of points, etc.

[FN47]. These recommendations appeared on the B Lab website in 2012, but are now not available for public viewing.

[FN48]. Briana Cummings, *Benefit Corporations: How to Enforce a Mandate to Promote the Public Interest*, 112 COLUM. L. REV. 578, 612 (2012).

[FN49]. See, e.g., Jay M. Feinman, *Liability of Accountants for Negligent Auditing: Doctrine, Policy and Ideology*, 31 FLA. ST. U. L. REV. 17 (2003) (describing the law in every jurisdiction regarding the liability of accountants).

[FN50]. See, e.g., *Abu Dhabi Commercial Bank v. Morgan Stanley & Co.*, 651 F. Supp. 2d 155 (S.D.N.Y. 2009) (certain claims against credit rating agency survived motion to dismiss); Nan S. Ellis et al., *Is Imposing Liability on Credit Rating Agencies a Good Idea? Credit Rating Agency Reform in the Aftermath of the Global Financial Crisis*, 17 STAN. J. BUS. & FIN. 175 (2012) (arguing for increased civil liability for credit rating agencies); Stephen Harper, *Credit Rating Agencies Deserve Credit for the 2007-2008 Financial Crisis: An Analysis of CRA Liability Following the Enactment of the Dodd-Frank Act*, 68 WASH. & LEE L. REV. 1925 (2011) (arguing that increased liability is likely).

[FN51]. MODEL BENEFIT CORP. LEGIS. § 303(c) (B Lab 2013).

[FN52]. *Id.* § 301(c).

[FN53]. *Id.* § 305(a)(2).

[FN54]. The city of San Francisco, California give preferences to benefit corporation in the awarding of city contracts. See S.F., CAL., ADMIN. CODE, ch. 14C (2012) (in calculating low bidder on city contracts, bids by benefit corporations are “discounted” by 4 percent).

[FN55]. The Maryland act does not include a provision on enforcement. *See* MD. CODE ANN., CORPS. & ASS'NS § 5-6C-01 to 08 (West, Westlaw through all chapters of the 2013 Regular Session of the General Assembly, effective through July 1, 2013).

[FN56]. MODEL BENEFIT CORP. LEGIS. § 305(b). The Virginia act does not include the provision that an action may be brought by a “5% owner of an entity of which the benefit corporation is a subsidiary”; the Vermont act increases the percentage ownership requirement to 10 percent and allows the benefit corporation to specify in its articles other persons who may bring a benefit enforcement proceeding. VT. STAT. ANN. tit. 11A, § 21.13(b) (West, Westlaw through Law No. 53 of the First Session of the 2013-2014 Vermont General Assembly (2013), except for Law Nos. 29, 50 and 51, and laws and sections of laws effective July 1, 2013, and later).

[FN57]. MODEL BENEFIT CORP. LEGIS. § 305(a)(1).

[FN58]. *Id.* §§ 305(a)(2) (benefit corporation), 303(c)(2) (officer), 302(e) (director).

[FN59]. *Id.* § 305(b)(2)(iv).

[FN60]. *Id.*

[FN61]. Specific performance of contracts is routinely denied because of the difficulty that a court faces in enforcing its decree. *See* CALAMARI AND PERILLO ON CONTRACTS 557 (6th ed. 2009). A similar difficulty would arise were a court to order a corporation to take certain actions to achieve its general or specific public benefit, especially since the necessary actions are not easily identified and, in any case, are likely beyond the competence of a court to supervise.

[FN62]. *See, e.g.*, MODEL BUS. CORP. ACT ANN. § 8.08 (2011).

[FN63]. *E.g.*, N.Y. NOT-FOR-PROFIT CORP. LAW § 112 (McKinney, Westlaw through L. 2013, chapters 1 to 57 and 60 to 110) (New York not-for-profit corporation law authorizing the attorney general of the state to bring suit to remedy certain improper actions by the entity and its officers and directors, among other things).

[FN64]. *In re* First Baptist Church of Spring Mill, 22 A.3d 1091, 1093 (Pa. Commw. Ct. 2011) (state attorney general challenged proposed distributions by nonprofit corporation in its dissolution); Commonwealth ex rel. Corbett v. Citizens Alliance for Better Neighborhoods, Inc., 983 A.2d 1274, 1277 (Pa. Commw. Ct. 2009) (“it is the well-settled law of the Commonwealth that the Attorney General is responsible for the public supervision of charities through his *parens patriae* powers”).

[FN65]. Steven Munch, *Improving the Benefit Corporation: How Traditional Governance Mechanisms Can Enhance the Innovative New Business Form*, 7 NW. J.L. & SOC. POL'Y 170, 190 (2012).

[FN66]. *E.g.*, DEL. CODE ANN. tit. 8, § 102(b)(7) (2011); MODEL BUS. CORP. ACT ANN. § 2.02(b)(4) (2011).

[FN67]. *See, e.g.*, Thomas W. Joo, *Contract, Property, and the Role of Metaphor in Corporations Law*, 35 U.C. DAVIS L. REV. 779, 780 (2002) (“The ‘nexus of contracts’ or ‘contractarian’ model, a metaphor that attempts to understand corporations in terms of ‘contracts,’ currently dominates corporation law scholarship.”).

[FN68]. *See generally* CALAMARI AND PERILLO ON CONTRACTS 577-600 (6th ed. 2009).

[FN69]. *See supra* note 66.

[FN70]. Anecdotally, some insurance companies have been unwilling to provide director and officer liability insurance for benefit corporations.

[FN71]. California and Maryland omitted the requirement that the benefit corporation have a benefit director.

[FN72]. Independence is defined in section 102(a) as:

Having no material relationship with a benefit corporation or a subsidiary of the benefit corporation.  
Serving as benefit director or benefit officer does not make a person not independent.

A material relationship between a person and a benefit corporation or any of its subsidiaries will be conclusively presumed to exist if any of the following apply:

(1) The person is, or has been within the last three years, an employee other than a benefit officer of the benefit corporation or a subsidiary of the benefit corporation.

(2) An immediate family member of the person is, or has been within the last three years, an executive officer other than a benefit officer of the benefit corporation or its subsidiary.

(3) There is beneficial or record ownership of 5% or more of the outstanding shares of the benefit corporation by:

(i) the person; or

(ii) an association:

(A) of which the person is a director, an officer or a manager; or

(B) in which the person owns beneficially or of record 5% or more of the outstanding equity interests.

MODEL BENEFIT CORP. LEGIS. § 102(a) (B Lab 2013). The California benefit corporation legislation does not include a definition of “independent.”

[FN73]. *Id.* § 302(c). The benefit director is also required to opine on “whether the directors and officers complied with sections 301(a) and 303(a),” which are sections that require the consideration of other corporate stakeholders when making corporate decisions. *Id.* Several states, including California, Maryland, New York, and Virginia, have declined to mandate that a benefit corporation have a benefit director.

[FN74]. A majority of the directors of publicly held corporations are typically independent, but the board of directors of a closely held corporation typically consists of the shareholders and/or key employees of the corporation.

[FN75]. MODEL BENEFIT CORP. LEGIS. § 302(a).

[FN76]. *See, e.g.*, Phillip W. Lear, *Representations, Warranties, Covenants, Conditions, and Indemnities: Stitching Them Together in the Purchase Agreement*, 37 ROCKY MTN. MIN. L. INST. 3-1 (1991). The phrase might also refer to an opinion regarding financial statements, viz., that the financial statements fully present, in all material respects, the financial position of a particular company. *See, e.g.*, STEPHEN E. ROTH, PRIMER ON THE REGULATION OF VARIABLE ANNUITY AND VARIABLE LIFE INSURANCE PRODUCTS UNDER THE FEDERAL SECURITIES LAWS (A.L.I.-A.B.A. Continuing Legal Educ., Oct. 31-Nov. 2, 2012), *available at* Westlaw SU001 ALI-ABA 1.

[FN77]. MODEL BENEFIT CORP. LEGIS. § 301(a). The New Jersey benefit corporation legislation wisely omits the word “inaction,” N.J. STAT. ANN. 14A:18-6 (West, Westlaw through Laws effective through L. 2013, c. 84 and J.R. No. 9), as does the Illinois act. ILL. COMP. STAT. ANN. 40/4.01(a) (West, Westlaw through P.A. 98-108, with the exception of P.A. 98-104, of the 2013 Reg. Sess.). What, after all, is inaction? Does it arise only after consideration of a proposed course of action or policy? Or does inaction occur even in the absence of an agenda item? The Hawaii law requires the board of directors to consider the effects of any action (not inaction) on the shareholder and the accomplishment of the corporation's general and specific public benefits. The board may (not must) consider the effect of its actions on the other listed constituencies. HAW. REV. STAT. § 420D-6(a) (West, Westlaw through Act 140 of the 2013 Regular Session).

[FN78]. MODEL BENEFIT CORP. LEGIS. § 301(a). The section provides the directors “need not give priority to a particular interest or factor referred to in paragraph (1) or (2) over any other interest or factor unless the benefit corporation has stated in its articles of incorporation its intention to give priority to certain interests or factors related to its accomplishment of its general public benefit purpose or of a specific public benefit purpose identified in its articles.” *Id.* § 301(a)(2), (3).

[FN79]. Under the Model Legislation, existing corporations may convert to a benefit corporation provided that shareholders holding at least two-thirds of each class or series of outstanding shares consent. Conversion occurs by amending the corporation's article of incorporation. MODEL BENEFIT CORP. LEGIS. § 104(a).

[FN80]. *See* FTC v. Retail Credit Co., 515 F.2d 988, 996 (D.C. Cir. 1975) (“[t]hat the specific should prevail over the general is not merely a technical canon of statutory construction, but also, to borrow Justice Holmes' phrase, an axiom of experience” (citation omitted)).

[FN81]. Cass R. Sunstein & Edna Ullmann-Margalit, *Second-Order Decisions*, ETHICS, Oct. 1999, at 5, 7.

[FN82]. *Id.* at 10.

[FN83]. *See* Grimes v. Donald, 673 A.2d 1207, 1213 (Del. 1996). Successful claims by shareholders alleging abdication typically involve formal abdication by the board of directors. *See* Chapin v. Benwood Found., Inc., 402 A.2d 1205 (Del. Ch. 1979) (trustees agreed to appoint particular person to future vacancy on board); Abercrombie v. Davies, 123 A.2d 893 (Del. Ch. 1956) (directors agreed to vote unanimously or submit to outside arbitrator), *rev'd on other grounds*, 130 A.2d 338 (Del. 1957).

[FN84]. Mary Frances Luce, John W. Payne & James R. Bettman, *Emotional Trade-Off Difficulty and Choice*, 36 J. MARKETING RES. 143, 144 (1999). In the context of consumer preferences, the authors wrote: “Given a set of attributes with roughly equal important weights, our research suggests that a product positioned as better on a more emotionally difficult attribute to trade off will gain greater choice share.” *Id.* at 157.

[FN85]. Melanie C. Green, Penny S. Visser & Philip E. Tetlock, *Coping with Accountability Cross-Pressures: Low-Effort Evasive Tactics and High-Effort Quests for Complex Compromises*, 26 PERS. & SOC. PSYCHOL. BULL. 1380 (2000), available at [http://psychology.uchicago.edu/people/faculty/visser/Green,Visser,Tetlock\(2000\).pdf](http://psychology.uchicago.edu/people/faculty/visser/Green,Visser,Tetlock(2000).pdf) (drawing on Philip E. Tetlock & Richard Boettger, *Accountability Amplifies the Status Quo Effect When Change Creates Victims*, 7 J. BEHAV. DECISION MAKING 1 (1994)).

[FN86]. DANIEL KAHNEMAN, *THINKING, FAST AND SLOW* 269-72 (2011).

[FN87]. *Id.* at 304; see generally Raquel Fernandez & Dani Rodrik, *Resistance to Reform: Status Quo Bias in the Presence of Individual-Specific Uncertainty*, 81 AM. ECON. REV. 1146 (1991) (arguing that there is a bias against efficiency enhancing reform when individual winners and losers cannot be identified ex-ante).

[FN88]. KAHNEMAN, *supra* note 86, at 304-05.

[FN89]. Amos Tversky & Eldar Shafir, *Choice Under Conflict: The Dynamics of Deferred Decision*, 3 PSYCHOL. SCI. 358 (1992).

[FN90]. Sheena S. Iyengar & Mark R. Lepper, *When Choice Is Demotivating: Can One Desire Too Much of a Good Thing?*, 79 J. PERSONALITY & SOC. PSYCHOL. 995 (2000).

[FN91]. On the negative effects of too many consumer choices, see generally BARRY SCHWARTZ, *THE PARADOX OF CHOICE: WHY MORE IS LESS* (2004). In the preface, for instance, Professor Schwartz writes: “[A]s the number of choices keeps growing, negative aspects of having a multitude of options begins to appear. As the number of choices grows further, the negatives escalate until we become overloaded. At this point, choice no longer liberates, but debilitates. It might even be said to tyrannize.” *Id.* at 2. The book is devoted to proving this assertion, in part by citing various experiments and data and is consistent with the studies cited in this article.

[FN92]. D. Redelmeier & E. Shafir, *Medical Decision Making in Situations that Offer Multiple Alternates*, 273 J. AM. MED. ASS'N 302 (1995).

[FN93]. John R. Hauser & Birger Wernerfelt, *An Evaluation Cost Model of Consideration Sets*, 16 J. CONSUMER RES. 393, 404-05 (1990); see also Natalie Ram, *Tiered Consent and Tyranny of Choice*, 48 JURIMETRICS J. 253, 271 (2008) (discussing the phenomenon). In addition, social choice theory suggests that if there are multiple decision makers with inconsistent preferences, there may be no voting system to aggregate such preferences into a single choice. KENNETH J. ARROW, *SOCIAL CHOICE AND INDIVIDUAL VALUES* (2d ed. 1963); Amartya Sen,

*Internal Consistency of Choice*, 61 *ECONOMETRICA* 495 (1993). While this is theoretically a problem in any board decision, it is particularly acute in decisions by benefit corporation directors because a director's ability to persuade his co-directors that a particular choice will satisfy their duty to maximize shareholder value becomes irrelevant.

[FN94]. The author participated on a committee that negotiated with proponents of benefit corporation legislation in Colorado. The legislation was based on the Model Legislation and its proponents were unwilling to agree to amendments that provided the sorts of flexibility suggested here.

[FN95]. *E.g.*, J. Haskell Murray, *Choose Your Own Master: Social Enterprise, Certifications and Benefit Corporation Statutes*, 2 *AM. U. BUS. L. REV.* 1 (2012).

[FN96]. A benefit corporation could, of course, provide in its bylaws for a benefit director.

[FN97]. *See* Robert R. Keatinge et al., *The Limited Liability Company: A Study of the Emerging Entity*, 47 *BUS. LAW.* 378 (1992).

[FN98]. *See* J. William Callison, *L3Cs: Useless Gadgets?*, *BUS. L. TODAY*, Nov./Dec. 2009, at 55.

[FN99]. *See* Robert W. Hamilton, *Registered Limited Liability Partnerships: Present at the Birth (Nearly)*, 66 *U. COLO. L. REV.* 1065 (1995).

[FN100]. *See* J. DENNIS HYNES & MARK J. LOEWENSTEIN, *AGENCY, PARTNERSHIP AND THE LLC: THE LAW OF UNINCORPORATED BUSINESS ENTERPRISES* 783-84 (8th ed. 2010).

[FN101]. There is some evidence that some consumers base their purchasing decisions on their perception of a company's social responsibility. *See Benefits of Becoming a Sustainable Business*, *ECOEFFICIENCY.COM*, [http://www.eco-efficiency.com/benefits\\_becoming\\_sustainable\\_business.html](http://www.eco-efficiency.com/benefits_becoming_sustainable_business.html) (last visited Aug. 10, 2013); *CONE COMM'NS, RESEARCH REPORT: CONE CAUSE EVOLUTION & ENVIRONMENTAL SURVEY 8* (2007), available at <http://goo.gl/IW0G3A>.

[FN102]. Michael Porter & Mark Kramer, *Creating Shared Value: How to Reinvent Capitalism--and Unleash a Wave of Innovation and Growth*, *HARV. BUS. REV.*, Jan.-Feb. 2011, at 62.

[FN103]. *Id.*

[FN104]. JOHN MACKKEY & RAY SISODIA, *CONSCIOUS CAPITALISM* (2013).

[FN105]. LYNN STOUT, *THE SHAREHOLDER VALUE MYTH: HOW PUTTING SHAREHOLDERS FIRST HARMS INVESTORS, CORPORATIONS, AND THE PUBLIC* (2012).

[FN106]. The concern that American corporations are overly focused on the short term is hardly a new idea. *See, e.g.*,

Michael T. Jacobs, *SHORT-TERM AMERICA: THE CAUSES AND CURES OF OUR BUSINESS MYOPIA* (1991), discussed in Mark J. Loewenstein, *Making America Competitive*, 18 DEL. J. CORP. L. 453 (1993). More recent articles include Lynne L. Dallas, *Short-Termism, the Financial Crisis, and Corporate Governance*, 37 J. CORP. L. 265 (2012); Emeka Duruigbo, *Tackling Shareholder Short-Termism and Managerial Myopia*, 100 KY. L.J. 531 (2012); ASPEN INST., *OVERCOMING SHORT-TERMISM: A CALL FOR A MORE RESPONSIBLE APPROACH TO INVESTMENT AND BUSINESS MANAGEMENT* (2009), available at <http://www.aspeninstitute.org/publications/overcoming-short-termism-call-more-responsible-approach-investmentbusinessmanagement>. This report was signed by a number of prominent business leaders, including Berkshire Hathaway CEO Warren Buffett, Vanguard Group founder John Bogle, and retired IBM CEO Louis Gerstner, Jr., among others.

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