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The Value of Corporate Purpose:

A Guide for CEOs and Entrepreneurs



About Us

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About KKS Advisors

KKS Advisors is a leading advisory firm specializing in strategy and research, formed with the vision to reshape markets. Our goal is to enable clients to create long-term value through the integrated management of economic, environmental, social and governance factors. KKS works with companies, investors, NGOs and policy-makers to drive systemic change, across a range of service offerings including - strategy, corporate governance and reporting, sustainable investing, sustainable development and branding. KKS provides thought leadership by regularly publishing research that inspires decision makers to drive market transformation. Learn more about our work and impact at *www.kksadvisors.com*

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About Generation Foundation

The Generation Foundation ("the Foundation") was established alongside Generation Investment Management LLP ("Generation IM") to strengthen the case for Sustainable Capitalism. Our strategy in pursuit of this vision is to mobilize asset owners, asset managers, companies and other key participants in the global economy around the business case for Sustainable Capitalism. All of the activities of the Foundation, a not-for-profit entity, are funded by a distribution of Generation IM's annual profitability. Learn more at *www.genfound.org*

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Methodology

Our methodological approach combines qualitative and quantitative research to inform our discussion and conclusions.

Throughout the report, we draw upon primary research obtained from panel discussions during a conference at Harvard Business School in November 2016. The panel participants were principally CEOs and C-Suite executives, the majority from Certified B Corporations ("B Corps") and Benefit Corporations based in the U.S. Other participants included experts in corporate law and corporate governance. The audience included academics and practitioners shaping the landscape of purpose-driven companies.

Each panel explored a different issue, such as why a company chooses to become a B Corp, how a business is managed differently as a purpose-driven company, and the choice to adopt alternative corporate forms. Discussions were held under Chatham House rules to foster openness from participants.

Part three of the report, which discusses the importance of law and culture, is based on statistical analysis of data collected across 32 countries. Sources included:

- **B Corps** - Information on the number and location of B Corps from the website of B Lab.
- **Law** - To identify the level of shareholder primacy across the countries under study, we analysed and coded legal documents from the Sustainable Development Taskforce of the American Bar Association, which provide a standardised list of questions and answers from lawyers on the legal frameworks which underpin the fiduciary duties of directors.
- **Culture** - We gathered information on the cultural dimensions of the sample countries using information from Geert Hofstede's dimensions of national culture.

We performed regression analysis on the data collected to understand the relationship between dependent variables (i.e. number of B Corps or existence of Benefit legislation) and used our data to model the economic effects of applying the cultural and legal characteristics of one country (the US) on another country (the UK).

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Executive Summary

Many companies are now seeking a way to signal their purpose; their reason for being beyond profits. In doing so, some companies have chosen to become certified B Corps or adopt alternative legal forms, such as the Public Benefit Corporation. But why do companies choose to signal their commitment to society and what are the potential mechanisms to do so?

Our research suggests that the answer lies in understanding the nexus of purpose, authenticity, trust and value. Purpose could drive customer, employee and investor choices as long as that purpose is authentic. If the company's purpose is authentic and this is understood by stakeholders, they trust the company and could make choices accordingly. This creates value for the company and a competitive advantage in the marketplace.

Since purpose has value, but this value depends critically on authenticity, then the critical question is - how do companies signal their authenticity? We find that organizations adopt different ways to do so. Some companies choose to signal the authenticity of their purpose by adopting integrated guidance and reporting, ceasing quarterly earnings guidance, and aligning incentive structures with long-term societal impact. Other companies choose to become B Corps and use the measurement and certification mechanism provided by B Lab to signal the authenticity of their purpose. Some companies choose to adopt alternative legal forms that require directors to consider the company's purpose in each decision they make. No one solution fits all. Business leaders should carefully weigh the benefits (i.e. credibility of the signal) and the costs (i.e. uncertainty introduced by the signal) in choosing how to signal the organizational purpose.

The report then goes on to explain the rise of B Corps around the world. We conclude that this is related to a measure of short-termism and the extent to which the law is interpreted in a country to require shareholder value maximization. Specifically, we find more B Corps in countries with a higher short-term orientation and an interpretation of the law that puts shareholders first. Many business leaders, as a result, decide to certify their corporations as B corps to protect the purpose of the business from short-term pressures and an interpretation of the law that might be too restrictive for the company's mission.

Report Roadmap



Purpose

The nexus of purpose, authenticity, trust and value

Authenticity

Trust in purpose creates value

Signals

C Corporations

The B Corp certifications

Alternative corporate forms

Is it Law or Culture that matters?

Key findings from statistical analysis

Purpose

The nexus of purpose, authenticity, trust and value

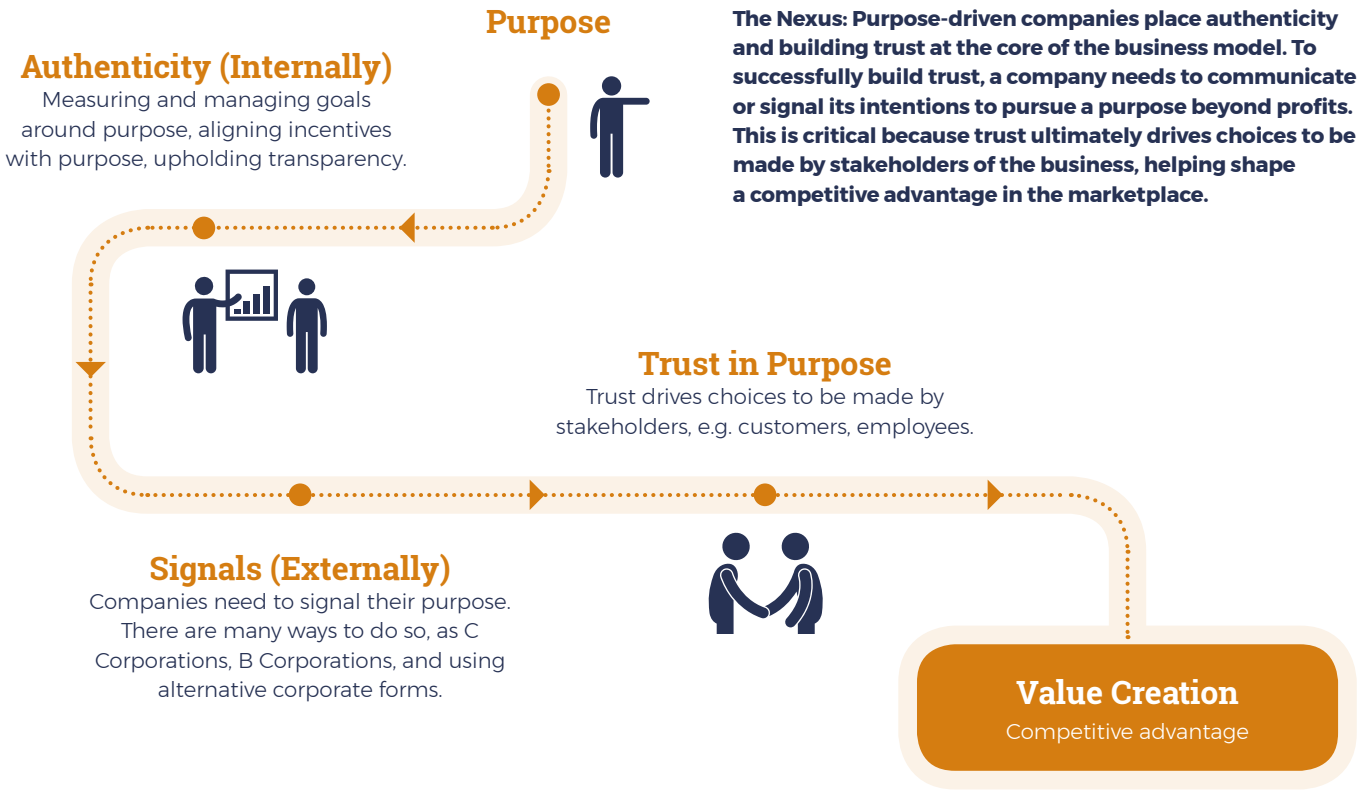
Many companies are now putting social purpose at their core. They are using the power of business to create a positive impact on communities and the environment and at the same time generate financial value. Purpose defines a reason for the existence of the business, which goes beyond simply making a profit. Pursuing purpose is not a corporate afterthought or a new marketing campaign which will be soon forgotten. Purpose places social and environmental considerations at the centre of making strategic business decisions which underpin long-term profitability. It is what keeps employees engaged. It is what customers are loyal to. It is what investors invest in. From this point onwards, we refer to companies which strategically derive their financial value from purpose as *purpose-driven companies*.

Purpose can potentially drive customer, employee and investor choices in the marketplace and act as a key driver for innovation that creates a competitive advantage. Brazilian cosmetics company Natura, for example, saw the need for a new valuation model which would allow investment decisions to evaluate the multiple dimensions of the company's ability to create value.[1] As nothing existed in the market, the finance team developed a new framework. This helped management make the decision to switch from synthetic alcohol to using organic alcohol as a key raw material. The analysis framework showed that organic alcohol was almost a third more expensive in terms of the acquisition cost, but had a lower total cost when environmental and social externalities were included. Joey Bergstein, General Manager and CMO at Seventh Generation, a company that produces green household and personal care products, told us:

"Our purpose is a key source of innovation, we channel it to drive new solutions in the market."

– Joey Bergstein, General Manager and CMO, Seventh Generation

Bergstein explained how this approach helped to solve a dangerous problem that perplexed the laundry industry. Liquid laundry detergent pods were causing sometimes fatal poisoning incidents in children, and it was unclear how the liquid ingredients could be made safe. Going against the industry norm of petroleum based products, the team started work on a plant-based solution. After months of work, two individually non-toxic liquid ingredients had been developed, but there were still no guarantees that they would not react to produce toxic results. Despite the commercial implications, the team set aside their progress and started again. Months later, they arrived at an industry-leading solution of non-toxic pods consisting of powder rather than liquid. This example demonstrates how a company may channel a strong commitment to purpose to deliver innovative solutions to the market.



The Nexus: Purpose-driven companies place authenticity and building trust at the core of the business model. To successfully build trust, a company needs to communicate or signal its intentions to pursue a purpose beyond profits. This is critical because trust ultimately drives choices to be made by stakeholders of the business, helping shape a competitive advantage in the marketplace.

For purpose-driven companies to generate competitive advantage, authenticity is essential. Authenticity can be defined as a genuine commitment to pursuing purpose-related objectives. Purpose-driven companies create authenticity by establishing clear goals to be achieved and ensuring that the conditions are in place to translate values into actions. Purpose-driven companies maintain authenticity and integrity by defining what they do, and just as important, what they don't do. For example,

Kirsten Tobey, Co-Founder and Chief Impact Officer of Revolution Foods explained how their pricing system always takes a "baseline" of quality - a minimum standard that all products will always meet.

This includes a promise that products will never contain any artificial colours, flavours, or sweeteners. Buyers can always expect this from the business.

This principle of discipline is shared by the management of Seventh Generation, which like Revolution Foods, obtains a third-party certification that scores the business on its environmental and social performance. From management's viewpoint, Joey Bergstein suggests that: "It keeps us grounded in our purpose, ensuring that our continual efforts are bearing fruit," as the scores serve as an objective assessment of performance on aspects relating to purpose. By tracking the scores and benchmarking against competitors, management can easily identify where improvements can be made to push the business further and enhance competitiveness. Another company ensures to "do the work internally", so that externally, the more information that is provided to stakeholders, the better the position the business will be in.

Authenticity is supported by transparency around business practices. CEOs told us "I invite transparency", "we pride ourselves on transparency" and reiterated that what matters is "transparency, authenticity, and knowing who's behind products".

They strive to open up the business to outsiders and keep stakeholders informed about the social and environmental issues that relate to their strategy and operations.

Increasingly, multinational companies are committing to, and developing new business capabilities around, transparency. For instance, multinational clothing company Patagonia launched their 'Footprint Chronicles', which aim to create supply chain transparency.[2] Similarly, Kering Group, which develops fashion houses such as Gucci and sports brands such as Puma, has invested in creating the Environmental Profit and Loss statement,[3] a tool which allows companies to express their environmental impacts in monetary terms alongside conventional financial accounts. These examples fit into a global trend towards greater transparency through increased disclosure of business-relevant non-financial information.[4]

When asked why their company strives to pursue broader social purposes in addition to profits, one CEO immediately answered "trust is a key element". Indeed, trust emerged as a recurring theme amongst CEOs of purpose-driven companies. This is because trust in purpose, that is built through authenticity, positively influences choices made by stakeholders, necessary for competitive advantage and strategic positioning. For example:



Customers' purchasing decisions are influenced by their trust in purpose

Trust in purpose drives customer preferences in the marketplace and boosts loyalty. According to Joey Bergstein of Seventh Generation, people who understand the purpose of the business are twice as loyal. In fact, the company realised that public advocacy work had a much higher return on investment than the traditional marketing mix when a one page, one time ad had more impact for the business than couponing. Their focus is now on educating customers to create more awareness on the environmental issues that the business exists to solve. Many CEOs noted that customers who recognize the broader purpose of the company are captivated by this aspect of the business and act based on trust. When customers understand *why* the business exists, which relates to the broader purpose that it serves, they make choices and build preferences around purpose. According to management at one company, brand trust is driven by the company having both what customers look for, and also not having what they don't want. The CEO of a seafood company explained how increasing awareness on the environmental issues which affect the industry incites a positive reaction from customers, observing that "people are as hungry for the stories as they are for the fish".



Employees choose to work hard because they believe in the purpose

Companies that demonstrate a commitment to a purpose beyond making profit are better positioned to attract and retain the best human capital. Research[5] on Millennials, for example, identifies a generation of workers that believe purpose is an important foundation for business success, and who seek to align work with personal values. When evaluating job opportunities, Millennials rank a sense of meaning from their work higher than other factors such as being able to travel internationally or even working for a leading company that people admire. Many CEOs underlined the importance of ensuring that employees understand not just how to do their work but also *why* their work is valuable, as a driver of employee satisfaction and engagement. Strong leadership helps communicate the 'why' by reiterating the importance of purpose, both for business and society. When employees believe that everyone in the organisation is working towards an important purpose, this builds an emotional connection and induces a strong work ethic, often even across different parts of the business. This 'unification' towards the achievement of common goals, was described by Chris Mann, CEO of organic beverage company Guayaki as creating a state of "congruency across all parts of the business."

Multiple CEOs revealed the use of internal social media streams to enhance communications amongst all employees. In particular, they encourage the visualization of results, with team members sharing images of recent activities and achievements. When everyone can visualize outcomes, employees can relate their individual tasks and contributions to a shared sense of purpose that aligns with larger goals. Chris Mann of Guayaki recognizes that when employees experience the purpose, they develop a personal connection and become more engaged with their work. For this reason, employees are often sent to spend time with the communities in the rainforests where inputs are sourced from, which motivates employees to serve the "people on both ends" of the business through a model of market-driven restoration. Kirsten Tobey of Revolution Foods, a company which serves 2 million meals a week to students across the US, highlighted the importance of hiring from the communities which the company serves. The human experience approach is especially important at the point of interface between the business and the community. The employees dishing up the food at lunchtime realize they could be nourishing a relative or a neighbour, a thought which builds a strong personal connection to the outcomes of work activities.

Which employees have the most significant effect in driving performance?

Recent research demonstrates that organisations with both a strong corporate purpose and high management clarity around where the organization is headed display increased financial performance, and this relationship is largely driven by middle management rather than top management.[6]

Signals

To create trust, companies need to signal their purpose

We find that there are multiple ways for a company communicate purpose to stakeholders. The first is to operate as a traditional corporate entity while aligning the core business strategy with purpose. A C Corp, the most common form of corporation in the US, would fall under this category. The second is to achieve a third-party certification of performance on metrics related to broader social and environmental objectives. For example, becoming a 'B Corp' - a certified B Corporation, requires meeting minimum standards on four aspects of the business - governance, workers, community, and the environment. The third signal is to adopt a corporate form which is designed specifically to embed purpose in a for-profit legal entity. For instance, a company may choose to incorporate as a Benefit Corporation. Recent developments in corporate law make this third type of signal an increasingly viable option for companies in many jurisdictions.

The three main mechanisms to signal purpose are summarized in the diagram below. The diagram reveals an encouraging conclusion for business leaders – that *all* companies can achieve purpose. While the strength and credibility of the signal may increase as a company moves further up the signalling diagram (from signal 1 to 3), this does not imply that there is one best approach for all companies. A variety of signals also bring a variety of opportunities and levels of risk for the company and its management. Our research suggests that increasing the strength and credibility of the signal may further enhance authenticity and create greater trust in purpose, but may also bring greater uncertainty and risk, such as a lack of investor knowledge about non-traditional legal forms for corporations. Moreover, while the strength and credibility of the signal is highest with alternative corporate forms (at the top of the diagram), the reality is that the majority of companies today signal purpose through traditional corporate forms (at the bottom of the diagram).

The point of importance is not the choice of signal but rather the choice to signal. Companies must communicate the value which is derived from purpose to build trust and generate a competitive advantage.

All companies can achieve purpose.



Overview

Firstly, traditional for-profit entities such as C Corporations, the most common type of corporation in the US, can build trust by demonstrating that the core business strategy is aligned with purpose. Signals help to communicate that financial value and social value are deeply interrelated. In the section below, the methods for a company to signal purpose are outlined:

1

Signal by ceasing quarterly earnings guidance

By ending the default practice of quarterly earnings guidance, which should not be confused with quarterly earnings reporting, management can signal a focus on long-term strategy in which financial value is derived from purpose. Regular earnings guidance refers to the default practice of disclosing predictions of a company's earnings for future quarters or the next fiscal year. In the first report by the Generation Foundation and KKS Advisors, entitled *Earnings Guidance – Part of the Future or the Past?*, we discuss how regular earnings guidance infuses short-term thinking in corporate management and provide an action framework for CEOs who wish to cease earnings guidance. Our research suggests that the actual costs of issuing regular earnings guidance far outweigh the perceived benefits and can impede a company's competitiveness by emphasizing short-term actions at the expense of the longer term. Ending quarterly guidance is one step towards closing the gap between valuing purpose and living purpose as a part of the long-term business strategy.

2

Signal by adopting the Integrated Guidance framework

The Integrated Guidance framework is a communications strategy which aims to support long-term investors by providing them with relevant and meaningful information. Adopting this framework can help purpose-driven companies to effectively communicate their long-term strategic vision to providers of capital. The framework, presented in our second report entitled *Implementing Integrated Guidance*, details the key steps in this communication strategy, which involves understanding the type of information that investors require by identifying leading indicators of future financial performance, planning the 'path to value' by quantifying key indicators, and finally communicating integrated guidance through a transparent dialogue with investors around the strategic direction of the firm.

3

Signal with Integrated Reporting

Corporate reporting is an important tool for signalling the purpose of a company in manner that is relevant to investors. Integrated Reporting is the emerging practice of presenting investor-relevant financial and non-financial information together in one corporate report. An integrated report considers the 6 forms of capital (financial, manufactured, intellectual, human, social and relationship, and natural) which an organization's business model may draw upon, and gives a comprehensive explanation of how the organization creates value over time.[7] Past research has shown that companies committing to Integrated Reporting attract more long-term investors thereby insulating themselves from short-term pressures.[8]

4

Signal by aligning incentives with purpose

Compensation schemes based solely on meeting financial targets can disproportionately incentivize short-term actions and reward behaviour which may be detrimental to a company's purpose and its profitability in the long-term. Management should align incentives inside the organization to establish short and long-term strategic goals and integrate both financial and non-financial indicators of success. Performance metrics should recognize the multiple dimensions of performance for a purpose-driven firm. As the text on the following page describes, this is consistent with corporate law that gives directors duties, under most cases, scope to consider a wide set of constituents when making decisions and not only shareholders.

Are company directors bound to maximize shareholder value at all times?

The concept of shareholder wealth maximization currently dominates capital markets. At its core, this ideology rests upon the belief that managerial decision making must only consider the impacts of business decisions in a single dimension – whether the outcome will increase shareholder profits, thereby placing all other stakeholders as a secondary concern. The question is whether company directors are bound to maximize shareholder value at all times as part of their fiduciary duties. Simply put, is there a legal obligation to place the interests of shareholders above all others?

The argument that for-profit corporations must put shareholders first arises from agency theory. As managers act as agents running the business on behalf of shareholders, there are a comprehensive set of rules which govern their behaviour. A commonly cited case which suggests a strict interpretation of fiduciary duty is that of Dodge v. Ford (1919), when the Michigan courts held that "A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end".[9] Moreover, key figures have argued not just that directors have to maximize shareholder wealth, but that they should. In other words, they theorise that shareholder wealth maximization benefits society. Case and point is Milton Friedman's notorious statement that "There is one and only one social responsibility of business — to use its resources and engage in activities designed to increase its profits".[10] However, there is an increasing realization that maximizing shareholder wealth does not always benefit society, but rather it is often at the expense of society and the environment. Multiple high-profile corporate scandals of unethical business conduct and the 2008 financial crisis have hit home that business as usual simply cannot continue.

Business must be a central part of the solution to the extraordinary challenges which face society today, among which are climate change, water scarcity, poverty and social inequality.

While the case of Dodge v Ford would seem to suggest that US law hugely narrows the scope of directors' decisions, the reality is that this case is somewhat of an anomaly. Moreover, the case hinges on the fact that Ford openly accepted having placed his altruism over his duty to shareholders; had he instead argued that his actions were intended to improve long-term profits of shareholders (e.g. paying employees more in order to reduce turnover and boost productivity), he may well have escaped liability.[11] Indeed, US law provides much greater latitude than this case would suggest.[12] To determine liability, courts will generally apply the business judgement rule, which requires a director to be informed and to act in good faith and in honest belief that the action was taken in the best interests of the company when making business decisions. Some go even further, to argue that shareholder wealth maximization has no foundations in US corporate law. Stout notably states:

"As far as the law is concerned, maximizing shareholder value is not a requirement; it is just one possible corporate objective out of many",

– Lynn Stout

and dismisses shareholder wealth maximization as a managerial choice rather than a legal obligation.[13]

In change of control situations, Delaware and other state laws outline the only duty of directors as to accept the highest bidder,[14] regardless of the implication, based on duties which were established in the landmark case Revlon Inc. v. MacAndrews & Forbes Holding, Inc.[15] In the day-to-day, the law may permit directors to consider the long-term and stakeholder interests, but for the most part it does not require them to do so. In this regard, UK company law stands out for its stance on enlightened shareholder value. A director of a UK company must have regard to the long-term consequences of their decisions, the interests of employees, the need to foster relationships with other stakeholders such as suppliers, and the impact of operations on the community and the environment.[16]

Overview

To signal purpose in an even stronger and more credible way, companies can undergo certification. This signals that a company genuinely pursues a goal beyond shareholder wealth maximization, as demonstrated by an external evaluation. Certification represents an additional level of scrutiny over purpose as it requires actively measuring impacts through metrics of environmental and social performance. Moreover, to achieve certification, companies are required to reach a minimum standard set by an objective third-party rather than internally by management. This external evaluation of a company's progress against social and environmental goals enhances the authenticity of its commitments and builds trust with stakeholders. Our analysis in this section will focus on the B Corp certification, perhaps the best-known certification, and one which has received significant media attention in recent years.

Certified B Corporations, also known as 'B Corps', are verified by a third-party organization called B Lab to have met "rigorous standards of social and environmental performance, accountability, and transparency" throughout the entire company.[17] This marks a contrast to other certification marks which evaluate specific 'parts' of a business or its products (e.g. Fairtrade).

The B certification aims to provide a credible signal of purpose by scoring companies on four dimensions of impact – governance, workers, community, and environment.

The principal requirement of certification is that a company meets a predefined minimum score when it undergoes the B Impact Assessment. The assessment aims to set a benchmark of performance and indicates that certified companies are leading the way in terms of engaging in good business practices in relation to the four core areas being assessed.

The certifying body, B Lab, is a non-profit organization that also advocates for Benefit Corporation legislation, which provides a specific legal form for incorporating as a profit-with-purpose business. It is worth noting that this is distinct to the certification and thus we discuss Benefit Corporations separately in the next section of this report. However, a degree of crossover between the two terms means that they are often confused - a company can be a B Corp, a Benefit Corporation, or both. The key takeaway is that while B Corps are required to modify their legal documents to include a requirement to consider a broad range of stakeholders to the extent possible in their jurisdiction, Benefit Corporations transform to an entirely different legal entity. In some states, the strictness of the law on traditional corporate forms means that company articles cannot be modified to include a consideration of other stakeholders, and therefore the company may be required to become a Benefit Corporation within a certain time period after achieving certification.

By quantifying a company's social and environmental performance, management can develop the tools to know when its efforts are successful. The company can authenticate its progress and, in doing so, provide the motivation to continue improving, as well as the clarity to know what areas to focus on.

Translating promises of purpose into data, metrics, and scores allows us to verify that claims are true and to draw comparisons against a common standard. This comparability was an added advantage for Ben & Jerry's, who have been reviewing their environmental and social performance independently for decades. According to Rob Michalak of Ben & Jerry's, the assessment pushed the company to look into specific areas such as HR and Supply Chain, to find out how the company could engage in, or beat, best practices.[18] For Etsy, the assessment revealed that employees were highly motivated to work together to raise the score; acting as a "quantifiable way to look at responsible decision making", the assessment provides a framework for decision-making and goal-setting.[19]

What is a B Corp?

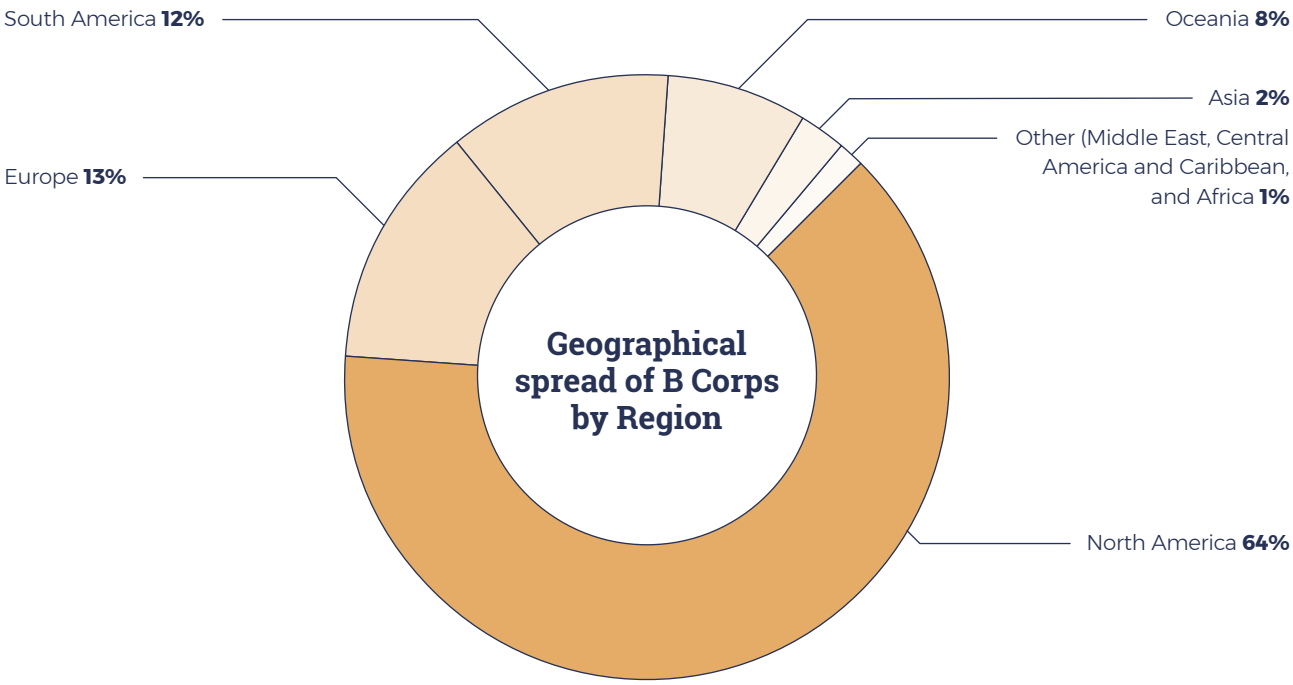
Issue	Certified B Corporations
Accountability	Directors required to consider impacts on all stakeholders to the extent possible within the corporate law of the jurisdiction of incorporation.
Transparency	Upon certification and recertification, the company must make its impact report publicly available.
Performance	Required to submit a completed B Impact assessment for review and achieve a minimum score of 80 points out of 200. Recertification is required every 2 years.
Availability	Global - Available to all businesses regardless of corporate structure, state, or country of incorporation.
Cost	Certification fees range from $500 to $50,000/year, based on revenues.
Role of B Lab	Certification body.

Source: Adapted from *https://www.bcorporation.net/what-are-b-corps/certified-b-corps-and-benefit-corporations* and "Term Sheets" for Certified B Corporations.

Geographical spread of B Corps by region[20]

The first generation of B Corps earned the certification in 2007. Since then, the number of certified companies has been growing rapidly. There are currently over 2,000 companies[21] which are Certified B Corporations, including many high-profile examples such as Patagonia, Seventh Generation, Plum Organics, Rubicon, and New Resource Bank. The certification of several big brands has sparked heightened interest and substantial media attention, and suggests that the B Certification is a valued tool for today's leaders in responsible business.

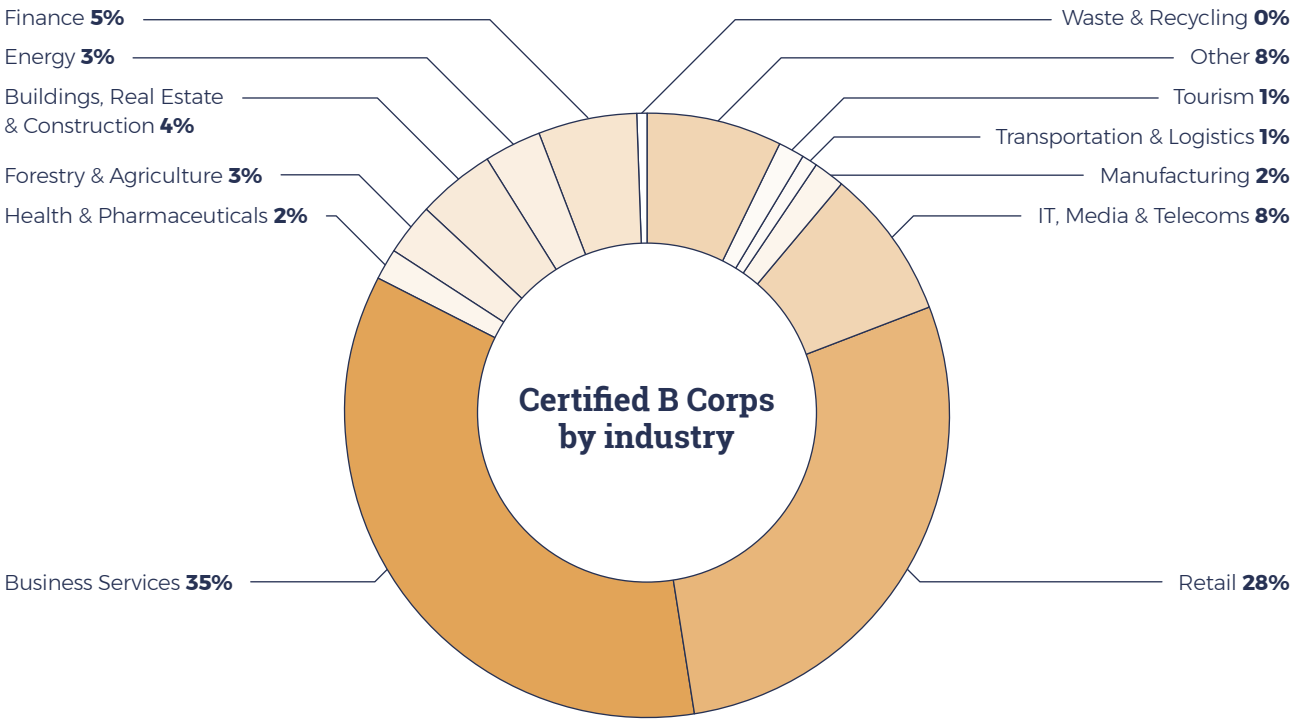
Over recent years, the geographical spread of B Corps has also expanded significantly. B Corps are no longer confined to the US, but are increasingly a global phenomenon. Regional hubs have been set up by B Lab to manage growth in Canada, South America, Australia and New Zealand, Europe and the UK. B Corps are now appearing in greater numbers around the world. Our research shows that Europe has the largest grouping of certified B Corps outside the US (13% of all B Corps), followed by South America (12%). The number of B Corps outside the US is only expected to rise further as the regional hubs consolidate their positions in the various national contexts.



Certified B Corps by industry [22]

Certified B Corps also operate in a range of industries. 35% of B Corps provide Business Services, under which Management & Financial Consulting and Marketing & Communication Services are the largest groupings. Retail accounts for 28% of B Corps, under which the majority is composed by Food & Beverage (36%), Home & Personal Care (21%) and Apparel, Footwear & Accessories (12%).

The fact that B Corps span both Business-to-business (B2B) and Business-to-consumer (B2C) companies suggests that the certification offers something which is valuable for many types of companies, and reinforces the claim that the B Corp certification goes beyond a marketing exercise to signal a credible commitment to purpose.



Overview

Lastly, to signal a legal commitment to purpose, companies can adopt an alternative corporate form, such as the Benefit Corporation structure. Using the law to embed purpose in a corporation is the strongest and most credible signal of purpose that management may use. It assigns legal importance to purpose, confirming that purpose goes beyond mere rhetoric and is embedded structurally in the business.

Corporate form refers to the separate legal entity that exists when a corporation is created. The question is, are alternative corporate forms necessary to facilitate purpose-driven business? New corporate forms build upon existing forms and go further to address the limitations that the latter often present. While the business judgement rule may provide considerable flexibility for company directors to consider stakeholders beyond shareholders, it certainly does not protect them in all scenarios, especially under circumstances where the ownership of the company changes. Moreover, corporate law generally permits but does not require directors to consider and act on a broader range of stakeholder concerns when making decisions, leading at times to passive or reactionary managerial behaviour to social and environmental issues. Even managers that would like to consider more than the financial dimension of a business lack sufficient protection if they do so. There is greater risk of liability for directors who deviate from the status quo of shareholder primacy, evident in the advice given by lawyers to businesses and in rulings made in courts of law. The risk of liability is a disincentive for proactive behaviour. Yet, by creating corporate forms which are specifically designed to serve purposes beyond profits, it may be possible to effectuate more immediate and tangible change than would otherwise occur. Corporate lawyer Susan Mac Cormac told us:

"Corporate form has the power to effect change. We need new corporate forms to require corporations to identify and actively pursue goals related to their purpose in society."

– Susan Mac Cormac, Corporate Lawyer

Decades of evolution in corporate forms

While the concept of creating legal forms appropriate for purpose driven companies may seem entirely new, the idea has in fact been around for some time. In the late 1970s, America's leading corporate lawyers came together to review corporate governance,[42] and more than a decade later published the American Law Institute's 'Principles of Corporate Governance: Analysis and Recommendations' in which the authors discuss the limitations of corporate forms with respect to social issues and provide recommendations for improving corporate form in this regard. For decades, corporations have been employing certain mechanisms to protect their social and environmental goals. For instance, corporations may set up a separate non-profit entity which can license back a product or service to the main company. Another option is the use of corporate constituency statutes. These statutes, which were created in the context of a wave of takeovers in the 80's, can permit or require directors to consider the interests of non-shareholder constituents in their decisions.[43] However, constituency statutes carry significant risks and cannot be relied on alone for protection.[44]

Corporate form is undergoing a transformation. What are the available options?
Next, we consider some of the new legal entities which have emerged to combine profits with purpose.

Low-Profit Limited Liability Company

The first innovation to emerge in the US was the Low-Profit Limited Liability Company (L3C), written into Vermont law in 2008, and subsequently adopted by several other states including Wyoming, Michigan and Utah.[23] The L3C is a variation of the limited liability company, with a key difference being that the primary purpose of a L3C must be charitable or educational. While the L3C is a for-profit entity, it must have no "significant purpose" of producing income or appreciating property although these are allowed.[24] It is therefore an alternative corporate form for companies which seek to prioritize social purpose over profit seeking. The L3C was designed to facilitate program related investments (PRIs) from private foundations which could be leveraged to attract traditional debt and equity financing.[25] Their main advantage was envisioned to be their enhanced ability to receive capital from both non-profit and for-profit investors through various stages of investment with different corresponding levels of risk and return. However, the American Bar Association criticized L3C legislation for promising what it cannot deliver in terms of facilitating PRIs, and opposed the legislation on a number of grounds.[26] One major concern is the lack of mechanisms to prevent a L3C from abandoning its social purpose, as failing to satisfy the requirements of being an L3C means that a company shall revert to operating as a limited liability company.[27] Although the extent to which L3C legislation offers solutions to the problems which it set out to resolve is questionable, it has provided inspiration for further legislative innovations.

Social Purpose Corporation

In 2012, a new corporate form became effective in California, known as the Flexible Purpose Corporation. This corporate form was designed with the goal of creating a viable and well-used alternative which would be capable of attracting mainstream capital and being used by both small companies as well as publicly-listed multinationals.[28] Later renamed as the Social Purpose Corporation (SPC), this corporate form has also become available in Florida, Washington, and Texas.[29] SPCs differ from traditional for-profit entities in a number of important ways. Notably, the company's articles of incorporation must state one or more social or environmental purposes.[30] The 'special purpose' may be considered alongside shareholder value when determining the company's and shareholders' best interests. A key advantage of the Social Purpose Corporation is that it provides additional protection (or 'safe harbor') for managers to consider environmental and social issues both in everyday decisions and change of control situations. Moreover, the Social Purpose Corporation also strengthens the ability of corporate purpose to endure in the long-term, as amendments to the defined purpose must be voted on and approved by at least two-thirds of each class of outstanding shares, as is the case with plans to convert to another corporate form. Transparency is also upheld through a requirement for management and directors to specify objectives for measuring the impact of efforts relating to the company's special purpose, and to include an analysis of these in annual reports, together with financial statements.[31]

Public Benefit Corporation

In many states, the model legislation has undergone a number of revisions before being passed into law. Delaware, which continues to be the most favoured state for incorporation,[36] has its own version, known as the (Delaware) Public Benefit Corporation (PBC). This is considered by many legal experts to be the best model currently available.[37] A Delaware Public Benefit Corporation is a for-profit corporation that is intended to produce one or more public benefits and to operate in a responsible and sustainable manner.[38] 'Public benefit' is defined as "a positive effect (or reduction of negative effects) on one or more categories of persons, entities, communities, or interests".[39] In contrast with the model legislation, the Delaware approach requires directors to 'balance' interests rather than 'consider' a list of stakeholders and issues.[40]

Benefit Corporation

Another corporate form to have emerged in recent years is the Benefit Corporation. Benefit Corporation legislation is currently available in 30 US states plus the District of Columbia, as well as in Italy and Puerto Rico.[32] Well known Benefit Corporations include companies such as Patagonia, Method, Kickstarter, and Plum Organics (owned by Campbell Soup Company). The first Benefit Corporation legislation was passed in Maryland in 2010, which adopted the model legislation as drawn up by B Lab (the organisation which also provides the B Certification). B Lab advocates for companies to adopt the legislation, but has no role in oversight as corporate law is a matter of state or jurisdictional law. The new corporate form has taken a variety of names in different states, including the Benefit Corporation and the Public Benefit Corporation. More importantly, the legislation itself varies significantly depending on the state.

Under the model legislation, a Benefit Corporation is a for-profit corporation which must have the purpose of creating "general public benefit" and which may also identify one or more specific public benefit purposes.[33] General public benefit is defined[34] as a "material positive impact on society and the environment, taken as a whole, as assessed against a third-party standard, from the business and operations of a benefit corporation". According to the model, in discharging their duties directors "shall" consider the effects of any action or inaction upon a list of factors, which includes shareholders, employees, subsidiaries, suppliers, customers, community and societal factors, the local and global environment, short and long-term interests, and accomplishing the general public benefit purpose as well as any specific public benefit purpose.[35]

Is corporate form the solution?

While traditional corporate form can and does continue to serve companies which pursue societal or environmental purposes in addition to profits, there are limitations. New corporate forms seek to lower the risk of liability for directors, create mechanisms for embedding purpose legally, and offer standards for increased transparency. Corporate form offers a tangible solution to the challenges of short-term pressures, effectively allowing directors to "choose their own master".[41]

This solution, however, does not come free of risks. As a recent innovation in corporate law, the new forms have not been tested extensively in courts. Case law is lacking, and there is uncertainty as to the weighting which will be given to duties relating to shareholders compared to other stakeholders, especially in cases where a for-profit entity, as new corporate forms are for-profit, ceases to be profitable.

Moreover, there is a lack of investor and public knowledge about what new corporate forms entail, why they are needed, and what to call them.

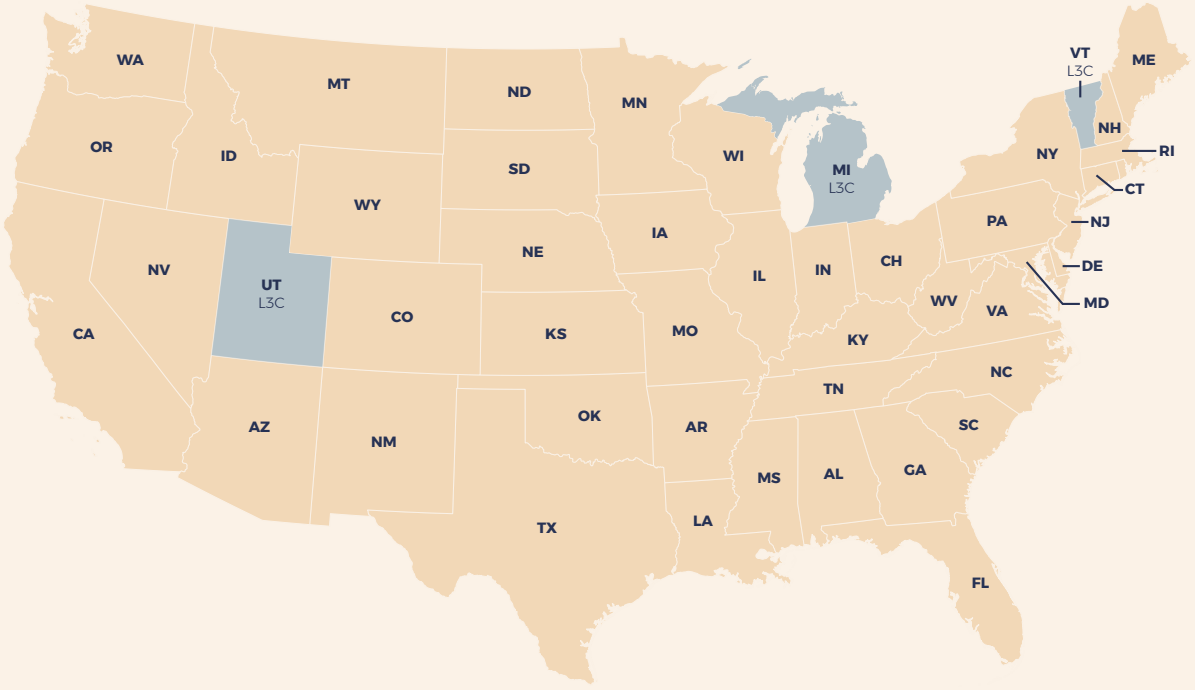
Moreover, there is a lack of investor and public knowledge about what new corporate forms entail, why they are needed, and what to call them, given that many different variations exist. For instance, Thomas Matzzie, CEO of CleanChoice Energy, explained how management had to abandon the Benefit Corporation structure in order to secure funding from a perplexed financial institution.

While new corporate forms have been designed to receive mainstream capital and increasingly receive financing from this source, traditionally they received financing by impact investors. We see promising developments that suggest access to financing broadening for companies with the Public Benefit Corporation structure, such as the IPO of Laureate Education and venture financing of AltSchool in excess of $130 million. Whether new corporate forms are able to attract sufficient capital from mainstream investors and enter public markets on a large scale will be the true test of their success.

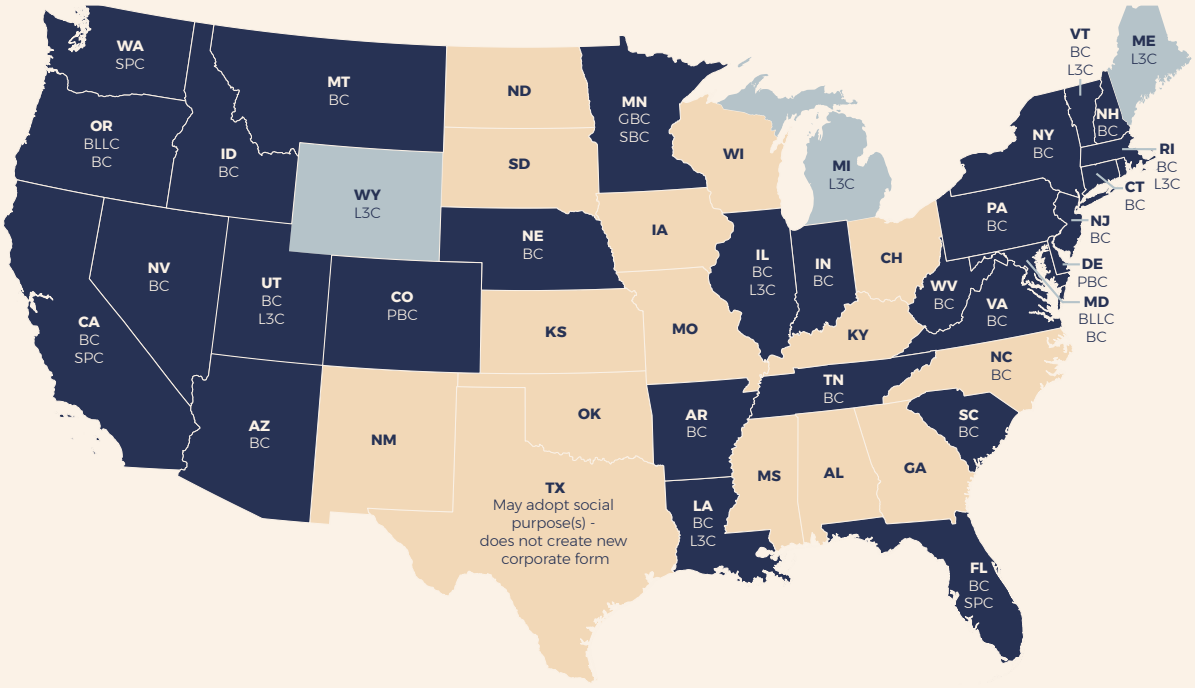
United States: An overview of corporate forms available for purpose-driven business

- No specific corporate form
- Only L3C available
- Specific corporate form available

The outlook in 2009:



The outlook in 2016:



Note: Benefit Corporation (BC) available in Washington D.C. Sustainable Business Corporation (SBC) designation available in Hawaii

Comparison of corporate forms

	Benefit Corporation (Model Legislation)	California Social Purpose Corporation (SPC)	Delaware Public Benefit Corporation (PBC)
Corporate purpose 	A model Benefit Corporation must have the purpose of creating "general public benefit", defined as a "material positive impact on society and the environment, taken as a whole, as assessed against a third-party standard, from the business and operations of a benefit corporation". • May also identify one or more specific public benefit purposes.	A SPC must set forth a "special purpose" in the articles of incorporation. The articles must state one or more social or environmental purposes, defined as engaging in one or more of the following: • Charitable or public purpose activities. • Promoting positive effects, or minimizing adverse effects, of the social purpose corporation's activities upon any of the following - (i) The social purpose corporation's employees, suppliers, customers, and creditors. (ii) The community and society. (iii) The environment.	A Delaware PBC is intended to produce one or more public benefits and to operate in a responsible and sustainable manner. 'Public benefit' defined as "a positive effect (or reduction of negative effects) on one or more categories of persons, entities, communities, or interests (other than shareholders in their capacities as shareholders) including, but not limited to, effects of an artistic, charitable, cultural, economic, educational, environmental, literary, medical, religious, scientific or technological nature."
Directors duties 	Directors shall consider the effects of any action or inaction upon a list including: • Shareholders, employees, subsidiaries, suppliers, customers, community and societal factors, the local and global environment, short and long-term interests, and • Accomplishing the general public benefit purpose as well as any specific public benefit purpose.	A director shall perform their duties in good faith, in a manner they believe to be in the best interests of the social purpose corporation and its shareholders. In discharging his or her duties, a director shall consider and give weight to factors, as the director deems relevant, including: • The overall prospects of the social purpose corporation, • The best interests of the social purpose corporation and its shareholders, • The purposes of the social purpose corporation as set forth in its articles.	The board of directors shall act in a manner that balances the pecuniary interests of shareholders, the best interests of those materially affected by the corporation's conduct, and the specific public benefit or public benefits identified in its certificate of incorporation. • Decisions will satisfy fiduciary duties to shareholders and the corporation if they are both informed and disinterested and not such that no person of ordinary, sound judgment would approve.
Transparency requirements 	• Must prepare an annual benefit report that assesses its performance in creating general public benefit against a third-party standard.	• The annual report sent to shareholders must contain a 'special purpose management discussion and analysis' concerning the stated purpose(s), which must be made publicly available. • A special purpose current report to be sent to shareholders, and to be made publicly available. • Where best practices emerge, reporting should be in accordance with the best practices used.	• Must provide shareholders with a statement every 2 years as to the corporation's promotion of the public benefit or public benefits identified in the certificate of incorporation and of the best interests of those materially affected by the corporation's conduct. • No requirement to make reports publicly available.

Globally: What alternative corporate forms are available in 2016?

Country	Corporate Form	Details
Italy 	Società Benefit	In 2015, Italy became the first country outside the USA to allow companies to register as Benefit Corporations.[45] They are for-profit companies which pursue "one or more purposes of common benefit and act in a responsibly, sustainable and transparent manner".[46]
Puerto Rico 	Corporación de Beneficio Social	In 2015, Puerto Rico passed its version of Benefit Corporation legislation. The main objective of such an entity is the creation of a social benefit, and not profit. However, if a profit is generated, it may be distributed among the owners.[47]
United Kingdom 	Community Interest Company (CIC)	First established in 2005, CICs are limited companies which operate to provide a benefit to the community. The purpose of CIC is primarily one of community benefit rather than private profit. Returns to investors must be balanced and reasonable.[48]
Canada 	Community Contribution Company (C3) in British Columbia Community Interest Company (CIC) in Nova Scotia	Introduced in 2013, most of a C3's profits must go towards the C3's community purposes (or be transferred to a qualified entity, such as a charity).[49] CICs use business practices to advance social, community or environmental goals, combining entrepreneurship with a social purpose (e.g. community-owned wind farms or businesses that invest their profits into charitable organizations).[50]

Globally: Beyond 2016

The following countries are reported to be moving forward with creating Benefit Corporation legislation - Australia, Argentina, Chile, Colombia and Canada. In addition, a recommendation has been made to the UK Government to explore the introduction of "benefit company" status in English law.[51] In France, a new corporate from has been proposed, called the Extended Purpose Corporation, or Société à Objet social Etendu (SOSE).[52]

Is it law or culture that matters?

In the previous section, we outlined various pathways to signal corporate purpose. Across these signals, law and culture are two central themes. While culture relates to the informal rules which influence behaviour (such as societal norms and codes of conduct), law addresses the formal rules which govern the behaviour of individuals and institutions. The question arises as to whether it is law or culture which is most important for driving change in the current corporate paradigm. Our analysis reveals that both are important to understanding the existence of certified B Corps around the world.

The statistical analysis is presented in the Appendix. Here we describe the primary results from the analysis.

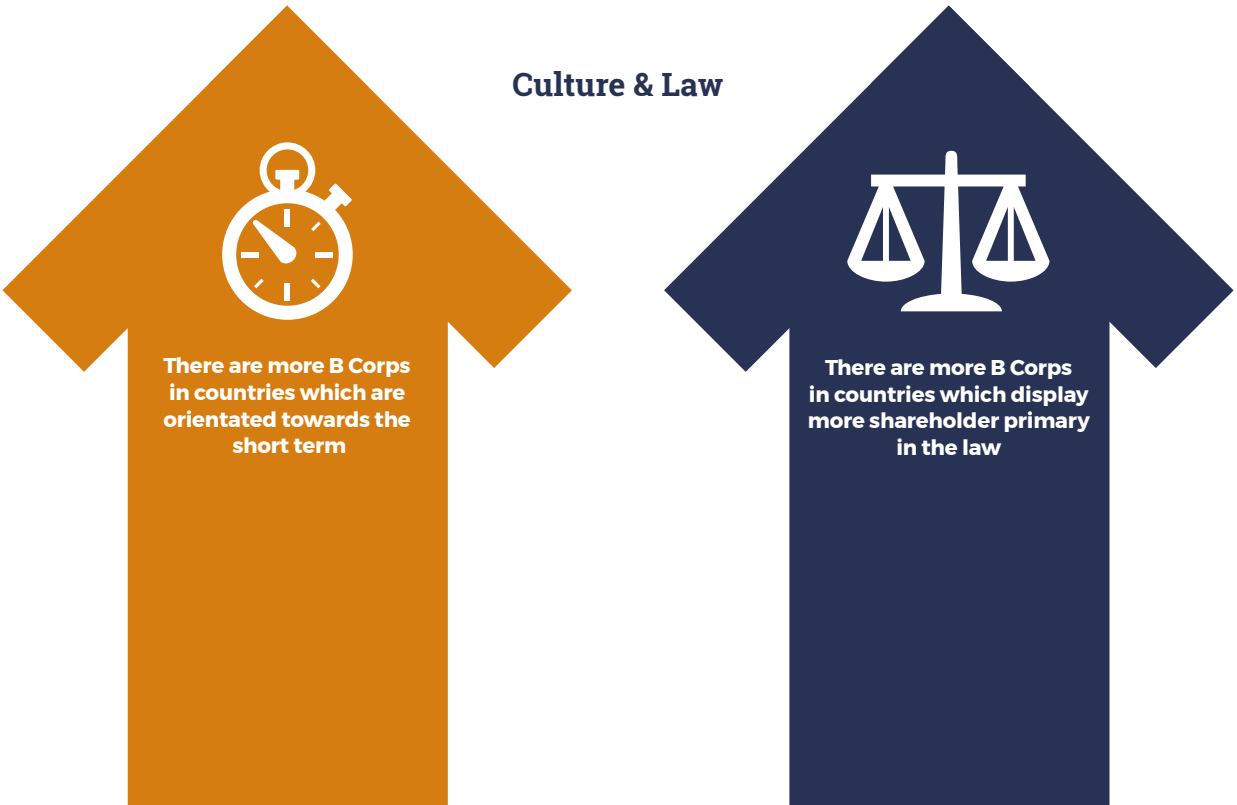
Firstly, our research shows that there are more B Corps in countries which are culturally more orientated towards the short term. Secondly, we discover that there are more B Corps in countries with a higher degree of shareholder primacy present in the law.

Countries with a higher degree of shareholder primacy are more heavily disposed towards shareholders, and more inclined to overlook other stakeholders, such as employees, customers, suppliers and local communities, in legal discussions. The level of shareholder primacy in a country is affected by factors such as whether the law requires directors to consider non-shareholders and whether it is explicit in stating duties towards non-shareholders.

Our findings are evidence of the tangible economic effects of a short-term culture and shareholder primacy in the law. These effects can be further demonstrated by considering two countries which display contrasting characteristics. If one country were to adopt the cultural and legal characteristics of the other, what would the economic effects be in terms of the number of B Corps present? We modelled for this scenario using the United States and United Kingdom. At one extreme, the US demonstrates an extremely high level of shareholder primacy, combined with a short-term culture that drives individuals towards seeking quick results in the work place. At the other extreme, the UK has a low level of shareholder primacy (exemplified by its use of the legal doctrine called 'enlightened shareholder value'), combined with no dominant cultural preference towards the short or long term.

If the UK were to have the same level of shareholder primacy as the US, the expected effect would be a 96% rise in the number of B Corps in the UK. If we additionally model for the UK to display the same level of short term orientation as the US, the expected number of B Corps present in the country rises further.

Our model means that the UK adopting the legal and cultural characteristics of the US would result in a 159% increase in the number of B Corps present.



Our findings provide the first evidence of the specific legal and cultural factors which influence the presence of B Corps around the world. Our analysis indicates that businesses are responding to certain legal and cultural challenges which are present in current economic models, namely the norm of shareholder primacy and strong cultures infused with short-term thinking. In this context, signals of corporate purpose, such as those identified in the previous section of this report, offer a useful means of articulating the important role of business in pro-actively addressing social and environmental issues, against a legal and cultural backdrop which works to prolong the status quo. New corporate forms are the strongest signal that something is amiss in corporate law and business culture, and highlight that this 'something' is significant enough to initiate a widespread reaction.

Empowering business leaders to pursue social and environmental purposes in addition to profits in the future must consider the importance of both legal and cultural dimensions of business.

On one hand, the informal rules of culture can be powerful in shaping behaviour, but without suitable protection from the law, directors will continue to see a greater risk from acting on greater purposes. On the other hand, the law may greatly enhance the protections for directors to pursue corporate purpose alongside profits, but without cultural change, business will not avail of these mechanisms and corporate purpose will not become mainstream.

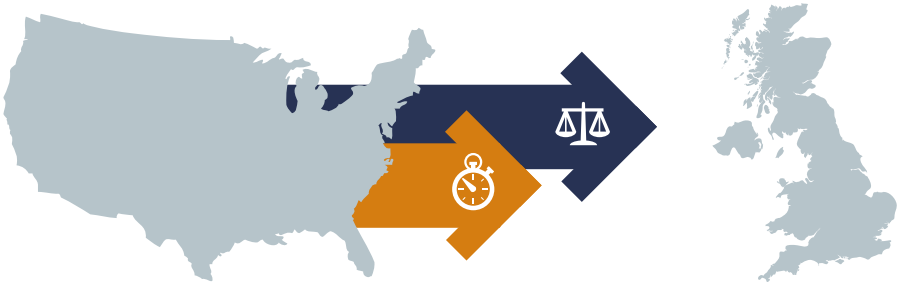
Law and culture both play an important role in driving change.

A model of the economic effects expected if the cultural and legal characteristics of the US are applied to the UK.



96%

Increase in B Corps
If the UK had the shareholder primacy level of the US



159%

Increase in B Corps
If the UK had both the shareholder primacy level & short-termism of the US

Appendix

Appendix

Summary Statistics and Correlations								
Variable	**N**	**Average**	**Standard Deviation**	**% B Corps**	**# B Corps**	**Shareholder Primacy Law**	**Short Termism**	**# of Firms**
% B Corps	32	5.8%	10.3%	1.000				
# B Corps	32	48	160	0.603	1.000			
Shareholder Primacy Law	32	0.516	0.237	0.525	0.259	1.000		
Short Termism	32	0.521	0.208	0.494	0.354	0.193	1.000	
# of Firms	32	1,080	1,496	-0.230	0.320	-0.158	-0.218	1.000
GDP-per-capita	32	30,421	25,364	-0.025	0.390	0.011	-0.070	0.031

% B Corps is the ratio of number of B Corps in a country over total number of companies publicly listed. # B Corps is the number of B Corps in a country. Shareholder Primacy Law is a variable that takes the value of zero if corporate law in a country explicitly requires in the fiduciary duties of the board directors stakeholders other than shareholders, 0.5 if corporate law in a country explicitly requires in the fiduciary duties of the board directors stakeholders other than shareholders but it specifies a duty to society in the incorporation stage or other duties relevant to the interests of stakeholders, or one otherwise (source: *http://www.americanbar.org/groups/leadership/office_of_the_president/sustainable_development_task_force.html*). Short-termism is 100 minus a measure of long-term orientation over a 100 (source: Geert Hofstede, Culture's Consequences: Comparing Values, Behaviors, Institutions, and Organizations Across Nations. Second Edition, Thousand Oaks CA: Sage Publications, 2001). # of Firms is the number of publicly listed firms in a country.

Relation between B Corps, short-termism and shareholder primacy in the law					
Dependent Variable		**% B Corps**		**# B Corps**	
Parameter		**Estimate**	**Pr > |t|**	**Estimate**	**Pr > |t|**
Intercept		-0.1444	0.1276	-10.9579	<.0001
Shareholder Primacy Law	+	0.1937	0.0176	1.7975	0.0681
Short Termism	+	0.2012	0.0120	3.6697	0.0009
GDP-per-capita		-0.0002	0.9855	0.6663	0.0010
# of Firms				0.5860	0.0002
N		32		32	
Adjusted R-squared		38%		44%	

This table presents the results of a multivariate ordinary least squares model for 32 countries. Dependent variable is % B Corps or # B Corps. All variables are specific in Table 1.

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