BENEFIT CORPORATIONS: THE NEED FOR SOCIAL FOR-PROFIT ENTITY LEGISLATION IN NORTH DAKOTA

ABSTRACT

The benefit corporation is an emerging type of business entity that allows for-profit companies to consider social consequences in company decision-making processes. In April 2010, Maryland became the first state to pass benefit corporation legislation. Since then, thirty-one states, including Delaware, have passed similar legislation. Despite North Dakota's uniquely shareholder-friendly laws, the state legislature has yet to adopt benefit corporation legislation. Creating a business entity that modifies traditional notions about corporations would create some business and legal uncertainty; however, there may be a need for a business form that is unrestrained by the existing wealth maximization corporate model. Given the surge in capital investment and economic activity in North Dakota, the following note will explain why the state should consider benefit corporation legislation as a means to foster socially conscious business development.

I. INTRODUCTION

In June 2012, the Reputation Institute, a private global consulting firm headquartered in New York, conducted a research project inviting 47,000 consumers from across fifteen markets to participate in a study that ranked the world's one hundred most reputable companies.[1] The study showed that a person's willingness to buy, work for, and invest in companies is predominantly based on perceptions of the company over perceptions of the product.[2] In the wake of large corporate scandals like Enron[3] and WorldCom,[4] it should come as no surprise that consumers, employees, and investors make decisions based on a company's corporate social responsibility practices. Although theories of corporate social responsibility and social entrepreneurship are not novel, there is an upswing

1. Jacquelyn Smith, *The Companies with the Best CSR Reputations*, FORBES (Dec. 10, 2012), http://www forbes.com/sites/jacquelynsmith/2012/12/10/the-companies-with-the-best-csr-reputations/3/.

2. *Id.* (explaining that willingness to buy is sixty percent based on the perception of the corporation and only forty percent based on the perception of the product).

3. *See generally Enron: The Real Scandal*, THE ECONOMIST (Jan. 19. 2002), http://www.economist.com/node/940091 (detailing how Enron, the Texas-based energy-trading company, declared bankruptcy as a result of poor corporate governance and lack of corporate social responsibility).

4. *See generally The Great Telecoms Crash*, THE ECONOMIST (July 18, 2002), http://www.economist.com/node/1234886 (explaining how WorldCom, the long distance phone company now known as MCI, filed for bankruptcy due to corporate executives inflating company assets).

in demand for socially responsible products, employers, and investment opportunities as a result of continued public scandal.[5]

TOMS, a shoes company, is one among several notable social enterprises created in response to this demand. Founder Blake Mycoskie created TOMS in 2006 after being inspired by children in Argentina without shoes.[6] He created a for-profit corporation matching every pair of shoes purchased with a donated pair of new shoes for a child in need. Through a partnership with National Relief Charities, TOMS has donated shoes to children living in federal Indian reservations, including reservations in North Dakota.[7] The Body Shop, a subsidiary of L'Oreal, is another noteworthy example of a socially conscious corporation.[8] The Body Shop's core competencies include positive environmental practices, using trade products, defending human rights, and campaigning against animal testing.[9] Having recognized the difficulties faced by corporations pursuing social missions, The Body Shop has voluntarily implemented social auditing practices to increase their social accountability.[10] Other companies, like TOMS, have opted in favor of creating for-profit corporations with non-profit subsidiaries to circumvent the limitations of being a corporation with a social mission.[11] Others still have taken a different approach, rejecting for-profit corporations entirely in favor of not-for-profit entities. These companies argue that the traditional corporate purpose of shareholder wealth maximization embedded in the concept of a corporation is "wholly incompatible" with social and charitable missions.[12]

Most scholars find themselves ideologically somewhere in the middle. They acknowledge that the corporate form limits the ability of companies to achieve social missions, but applaud company-initiated programs like social audits and not-for-profit subsidiaries. Regardless of variations along the ideological spectrum, all socially conscious groups continue to lobby for the

5. Nate Holzapfel, *The Rise of Social Entrepreneurship*, THE HUFFINGTON POST (Dec. 12, 2014 11:00 AM), http://www huffingtonpost.com/nate-holzapfel/the-rise-of-social-entrep_b_6304280 html.

6. *One-For-One*, TOMS, http://www.toms.com/one-for-one-en.

7. Kelly Gibson, *TOMS Shoes Giving Partners*, NAT'L RELIEF CHARITIES BLOG (Feb. 12, 2012), http://blog.nrcprograms.org/toms-shoes-giving-partners/.

8. *Our Company*, THE BODY SHOP, http://www.thebodyshop.com/content/services/aboutus_company.aspx.

9. *Id*.

10. *Social and Environmental Reporting*, THE BODY SHOP, http://www.thebodyshop.com.au/about-us/social-and-environmental-reporting.aspx.

11. *One-for-One*, TOMS, http://www.toms.com.

12. Lisa M. Fairfax, *Doing Well While Doing Good: Reassessing the Scope of Directors' Fiduciary Obligations in For-Profit Corporations with Non-Shareholder Beneficiaries*, 59 WASH. & LEE L. REV. 409, 411 (2002).

creation of business forms that better facilitate social entrepreneurship. In thirty-one states,[13] legislators have responded to these requests by creating public benefit corporations: a new type of business entity that allows for-profit companies to prioritize social outcomes in decision-making.[14] North Dakota is a state that has yet to adopt public benefit corporation legislation.[15] Therefore, the purposes of this note are twofold: to determine how this new business entity differs from traditional corporate law and to debate whether adopting legislation creating such an entity is a viable means of promoting corporate social responsibility in North Dakota.

II. BACKGROUND

In debating the need for a new legal entity, it is important to understand the evolution and shortcomings of traditional corporate law. Two seemingly inconsistent conceptions exist regarding the purpose of the corporation.[16] The first concept postulates that the "primary purpose of the corporation is to maximize share value for shareholders."[17] The second recognizes that corporations do not operate in a vacuum, and, as a result, are responsible for considering the concerns of constituents such as employees, customers, creditors, and the community.[18] The former view is the more conventional of the two views and is known as the "shareholder primacy model."[19] The following section outlines the evolution of the model. It also explains that while constituency statutes were enacted to address some

13. *State by State Legislative Status*, BENEFIT CORP. INFO. CENTER, http://www.benefitcorp net/state-by-state-legislative-status (listing states that have enacted Benefit Corporation legislation: Arizona, Arkansas, California, Colorado, Connecticut, Delaware, Florida, Hawaii, Idaho, Illinois, Indiana, Louisiana, Maryland, Massachusetts, Minnesota, Montana, Nebraska, Nevada, New Hampshire, New Jersey, New York, Oregon, Pennsylvania, Rhode Island, South Carolina, Tennessee, Utah, Vermont, Virginia, Washington D.C., and West Virginia). States that have introduced Benefit Corporation Legislation include: Alaska, Kentucky, New Mexico, North Dakota, and Oklahoma. *Id.*

14. *What is a Benefit Corporation?,* BENEFIT CORP. INFO. CENTER, http://www.benefitcorp net.

15. *See State by State Legislative Status*, *supra* note 13. During the 64th Legislative Assembly of North Dakota, Representative Klemin introduced House Bill No. 1237, "A BILL for an Act to create and enact chapter 10-37 of the North Dakota Century Code, relating to North Dakota public benefit corporations." *See* H.B. 1237, 64th Legis. Assemb., 64th Reg. Sess. (N.D. 2015). On January 27th, 2015, the House of Representatives passed the bill with 87 yeas and 6 nays. On March 24th, 2015, the Senate failed to pass the bill after a second reading with 2 yeas and 44 nays. *North Dakota Bill Actions: HB 1237*, NORTH DAKOTA LEGISLATIVE BRANCH, http://www.legis nd.gov/assembly/64-2015/bill-actions/ba1237 html.

16. Fairfax, *supra* note 12, at 430.

17. Alicia E. Plerhoples, *Representing Social Enterprise*, 20 CLINICAL L. REV. 215, 216 (2013).

18. Fairfax, *supra* note 12, at 432.

19. *Id.* at 430.

of the model's shortcomings, these statutes have deficiencies of their own, perpetuating the need for additional legislation.

A. TRADITIONAL CORPORATE LAW

The concept behind the shareholder primacy model is routed in both legal and economic principals. Proponents argue that "shareholders are the property owners of the corporation and, therefore, are entitled to legal protection of their property—their invested capital."[20] Because directors hold shareholders' property in trust, they owe fiduciary duties of undivided loyalty, care, and fair dealing.[21] Other proponents of the shareholder primacy model base their theory on principals of contract law. They argue that a corporation is "essentially a web of contractual relations forming a 'nexus of contracts.'"[22] The relationship between a director and shareholder is contractual in nature and governed by principals of agency.[23] Implicit in the contract is an understanding that directors will perform their legal duty to promote shareholder interests, which is subordinate to other stakeholder concerns.[24] Because shareholders have "relatively little external influence over the corporation," some argue that it is appropriate for directors to protect shareholder interests above the interests of other constituent groups who have the ability to enter into and negotiate their own contracts.[25] The view is argued as not only "descriptively accurate," but also "normatively appropriate."[26]

Dodge v. Ford Motor Co.[27] is a foundational case supporting the shareholder wealth maximization model. In *Dodge,* shareholders brought suit after Henry Ford, founder and director of Ford Motor Company, refused to pay out shareholder dividends.[28] Instead of issuing dividends, Ford intended to use corporate revenues to make cars more affordable for the public.[29] The court refused to afford Henry Ford deference as a director of the corporation and ordered him to pay out shareholder dividends.[30] The court used Ford's statements regarding his altruistic intent to help his

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20. *Id.*
21. *Id.* at 430-31.
22. *Id.* at 431.
23. *Id.*
24. *Id.*
25. *Id.* at 432.
26. *Id.*
27. 170 N.W. 668 (Mich. 1919).
28. *Id.* at 670.
29. *Id.* at 671.
30. *Id.* at 684-85.

workers and general consumers as evidence of a violation of his fiduciary duties to stockholders.[31]

Revlon, Inc. v. MacAndrews Forbes Holdings is another landmark case supporting shareholder wealth maximization.[32] In *Revlon*, the defendants sought to enjoin an agreement entered into by Revlon's board of directors during a hostile takeover because it was not in the best interests of the shareholders.[33] The Delaware Supreme Court affirmed the lower court's decision to enjoin the agreement thereby establishing that a director's duty is to maximize shareholder value, without regard to other constituencies, when a takeover of a company is inevitable.[34]

B. CONSTITUENCY STATUTES

In direct response to *Revlon*, several states have adopted constituency statutes that permit directors to consider non-shareholder interests. In essence, directors are allowed to consider the interests of certain stakeholders such as employees, customers, suppliers, creditors, and the community when fulfilling their fiduciary duties.[35] These statues help modernize the business judgement rule[36] by explicitly protecting decisions that consider non-shareholder interests from derivative actions.[37] Directors are protected even when their decisions seem to counter the traditional priority of shareholder wealth maximization.[38] Some scholars argue that by adopting constituency statutes, the traditional shareholder maximization

31. *See, e.g., id*. at 671 ("My ambition, declared Mr. Ford, is to employ still more men; to spread the benefits of this industrial system to the greatest possible number, to help them build up their lives and their homes. To do this, we are putting the greatest share of our profits back into the business.") (internal quotation marks omitted).

32. 506 A.2d 173, 182 (Del. 1986).

33. *Id.* at 176.

34. *Id.* at 182.

35. Stephen M. Bainbridge, *Interpreting Nonshareholder Constituency Statutes*, 19 PEPP. L. REV. 971, 973-74 (1992).

36. *See* Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984) (explaining that the business judgment rule is a standard of judicial review employed by courts when they are asked to evaluate the business decisions made by corporate boards of directors. It is a rebuttable presumption that corporate business decisions are made by disinterested directors, acting "on an informed basis, and in the good faith belief that the decisions are in the best interests of the" corporation and its shareholders. Unless that presumption can be rebutted successfully by proving to the court that the directors violated their fiduciary duties and are therefore unable to claim the rule's protection, a court will dismiss any lawsuit challenging a board's business decision.).

37. BLACK'S LAW DICTIONARY 509 (9th ed. 2009) ("A suit by a beneficiary of a fiduciary to enforce a right belonging to the fiduciary; esp., a suit asserted by a shareholder on the corporation's behalf against a third party (usu. a corporate officer) because of the corporation's failure to take some action against the third party.").

38. Bainbridge, *supra* note 35, at 989.

model has been abandoned.[39] So far, thirty-one states have adopted some variation of these statutes with material differences among them.[40] In 2007, North Dakota enacted a constituency statute as a part of the North Dakota Business Corporation Act. The statute reads as follows:

> In discharging the duties of the position of director, a director may, in considering the best interests of the corporation, consider the interests of the corporation's employees, customers, suppliers, and creditors, the economy of the state and nation, community and societal considerations, and the long-term as well as the short-term interests of the corporation and its shareholders, including the possibility that these interests may be best served by the continued independence of the corporation.[41]

While North Dakota's constituency statute gives directors some protection in decision-making, it is not as encompassing as public benefit corporation legislation. First, the language in the statute merely permits, but does not mandate, the consideration of non-shareholder interests. It provides that a director "may"[42] consider non-shareholder interests and that those who do are not necessarily in breach of director standards of conduct. Unlike public benefit legislation, North Dakota's constituency statute does not require directors to consider non-shareholder interests nor does it include consequences for entities in breach of their social mandate and mission. Therefore, whether and to what degree non-shareholder interests should be considered is left to the discretion of directors. There is neither a legal requirement of directors to justify disregarding other stakeholders nor a need to justify only giving these interests a cursory review. Consequently, while the permissive language may protect directors, "it properly does not and should not vest rights, benefits, or even expectations in non-shareholders."[43]

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39. William T. Allen, *Our Schizophrenic Conception of the Business Corporation*, 14 CARDOZO L. REV. 261, 277 (1992) ("[W]hat arguably is eradicated is the command . . . that maximizing the financial interests of shareholders through lawful means over some period of time is the core duty of a corporate director."); *see also* Ronald M. Gree, *Shareholders as Stakeholders: Changing Metaphors of Corporate Governance*, 50 WASH. & LEE. L. REV. 1409, 1412-14 (1993) (arguing that the passing of constituency statutes demonstrates the erosion of the traditional shareholder-primacy view).

40. *See, e.g.*, MINN. STAT. § 302A.251(5) (2004); MO. REV. STAT. § 351.347 (2001); N.Y. BUS. CORP. LAW § 717(b) (McKinney 2003); N.D. CENT. CODE § 10-19.1-50(6) (2007); S.D. CODIFIED LAWS § 47-33-4(1) (2007); WIS. STAT. § 180.0827 (2002). *See also* John Tyler, *Negating the Legal Problem of Having "Two Masters": A Framework for L3C Fiduciary Duties and Accountability*, 35 VT. L. REV. 117, 131–38 (2010) (providing a detailed discussion of constituency statutes).

41. N.D. CENT. CODE § 10-19.1-50(6) (2013).

42. *Id.*

43. Tyler, *supra* note 40, at 134.

This permissive language is not unique to North Dakota. Connecticut is the only state that mandates the consideration of non-shareholder interests.[44] Furthermore, Connecticut's mandate only applies if a corporation is publicly traded and is undergoing a change of control.[45] Therefore, if North Dakota were to propose changes to its constituency statute's permissive language and mandate consideration of non-shareholder interests—as opposed to creating public benefit corporations—the state would be a pioneer. Yet, such an amendment would lack a successful model for guidance.

Even if the permissive language in North Dakota's constituency statute was successfully changed, the statute's limited applicability is still a compelling concern. Similar to other states, North Dakota's statute applies only to directors and does not include other key corporate participants such as agents and officers who are tasked with daily decision-making on behalf of the corporation. According to the statute's existing language, only directors are afforded protection for making decisions that consider non-stakeholder interests.

In contrast, benefit corporations provide more inclusive protection for other decision makers through agency theory. Agency is defined as the fiduciary relationship that arises when a principal assents to an agent acting on behalf of the principal and the agent accepts.[46] Once an agency relationship has been created, agents owe various fiduciary duties, including duties of loyalty, care, good faith, and fair dealing to the principal.[47] By including social or environmental concerns as the primary purpose of the corporation, public benefit corporations provide protection to agents by giving them implicit authority to make socially conscious decisions. Officers and agents of such corporations have the implied[48] and, in some

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44. CONN. GEN. STAT. § 33-756(d) (2008) ("[A] director of a corporation which has a class of voting stock registered pursuant to Section 12 of the Securities Exchange Act of 1934 . . . may consider, in determining what he reasonably believes to be in the best interests of the corporation, (1) the long-term as well as the short-term interests of the corporation, (2) the interests of the shareholders, long-term as well as short-term, including the possibility that those interests may be best served by the continued independence of the corporation, (3) the interests of the corporation's employees, customers, creditors and suppliers, and (4) community and societal considerations including those of any community in which any office or other facility of the corporation is located.").

45. *Id.*

46. RESTATEMENT (THIRD) OF AGENCY § 1.01 (2006).

47. *Id.* at § 8.01-08.

48. *Id.* at § 2.01 cmt. b ("Implied authority is often used to mean actual authority either (1) to do what is necessary, usual, and proper to accomplish or perform an agent's express responsibilities or (2) to act in a manner in which an agent believes the principal wishes the agent to act . . . .") (internal quotation marks omitted).

instances, the actual authority[49] to make decisions in furtherance of the corporation's social objectives. Consequently, adopting public benefit corporation legislation would provide more inclusive agent and employee protection for socially conscious decision-making as compared to North Dakota's existing constituency statute that only protects directors.

A third area of concern regarding constituency statutes is the narrow scope of non-shareholder interests protected. While North Dakota's list of protected shareholder interests is relatively comprehensive and includes employees, customers, suppliers, creditors, the economy, the community, and society, by specifically listing such interests the language inherently limits the non-shareholder interests protected by the statute.[50] In contrast, benefit corporation legislation provides corporations with more autonomy and freedom to create unique and innovative public benefits. By not listing, and therefore limiting, protected interests, public benefit corporation legislation provides a broader scope of protected non-shareholder interests. For example, benefit legislation provides protection for companies wanting to provide "low-income or underserved individuals or communities with beneficial products or services."[51] Under the legislation, corporations are specifically encouraged to provide beneficial products and services, perhaps at lower prices than the consumer is willing to pay. In contrast, directors who prioritize low-income individuals at the expense of shareholders could be held liable for a breach of fiduciary duties under *Ford*'s precedent and North Dakota's existing constituency statute.

Although North Dakota's constituency statue is facing the same criticisms as other state statutes, the drafters were successful in certain regards. While some constituency statutes apply exclusively to situations where corporations are undergoing a takeover or structural changes, North Dakota's statute provides broad applicability, including, but not limited to, merger and acquisition contexts.[52] North Dakota's constituency statute also has correctly included language that permits both long and short-term considerations, as opposed to permitting only short-term interests.[53] Despite these triumphs, however, when read as a whole, North Dakota's

49. *Id.* at § 2.01 ("An agent acts with actual authority when, at the time of taking action that has legal consequences for the principal, the agent reasonably believes, in accordance with the principal's manifestations to the agent, that the principal wishes the agent so to act.").

50. Tyler, *supra* note 40, at 134.

51. MODEL BENEFIT CORP. LEGISLATION § 102 (B Lab 2013).

52. Fairfax, *supra* note 12, at 474 (noting that one third of the states limit the statute to the takeover and structural changes contexts); N.D. CENT. CODE § 10-19.1-50(6) (2013) ("[*I*]*ncluding* the possibility that these interests may be best served by the continued independence of the corporation.") (emphasis added).

53. Fairfax, *supra* note 12, at 462 n.292.

statute "merely create[s] the potential for 'socially responsible directors' to afford *some* degree of consideration to the effects of decisions on non-shareholder interests, which is a far cry from being able to *prefer* non-shareholder interests over shareholder interests."[54] To conclude that North Dakota's statute overrules the traditional notion of shareholder wealth maximization as the first and foremost priority would be to misread the statute.[55]

Case law does not seem to supplement what the statute is lacking. In *Production Credit Association of Fargo v. Ista*, the North Dakota Supreme Court noted "an officer or director of a corporation owes a fiduciary duty to the corporation and its stockholders."[56] The court stated that "a director's first duty is to act in all things of trust wholly for the benefit of the corporation"[57] and continued by citing to the North Dakota Century Code section that states a director must act "in a manner the director reasonably believes to be in the best interests of the corporation."[58] While considering what is in the corporation's best interest, however, the court failed to clarify whether a director may prioritize non-shareholder over shareholder interests. Furthermore, the court derived its authority from an encyclopaedia that states "directors of a corporation are entrusted with the management of its business and property for the benefit of all the shareholders and occupy the position of trustees for the collective body of shareholders in respect to such business."[59] It is a director's duty to "administer corporate affairs for the common benefit of all the shareholders . . . ."[60] This language strongly supports the conclusion that any non-shareholder interests are subordinate interests.

As a result, public benefit corporation legislation is still necessary in North Dakota despite the existence of a constituency statute. The current statute "lack[s] enforcement mechanisms [and] standing provisions that hold directors accountable for inadequately considering non-shareholder interests."[61] The result is an expansion of the business judgment presumption as a defense mechanism used by directors, as opposed to a

54. Tyler, *supra* note 40, at 134 (emphasis added).
55. *Id.*
56. 451 N.W.2d 118, 121 (N.D. 1990).
57. *Id.* (quoting FLETCHER CYCLOPEDIA OF THE LAW OF CORPORATIONS § 838 (3d ed. 1986)).
58. *Id.* (citing N.D. CENT. CODE § 10-19.1-50 (1989)).
59. FLETCHER CYCLOPEDIA OF THE LAW OF CORPORATIONS § 838 (3d ed. 1986).
60. *Id.*
61. Tyler, *supra* note 40, at 135.

right vested in non-shareholders.[62] The statute also does not include any requirement that "directors favor or prioritize non-shareholder interests over those of shareholders."[63] The result is a statute that affords no general protection for directors "motivated by a desire to maximize benefits to non-shareholder interests when doing so has no legitimate benefit to shareholders."[64]

If a director prioritizes non-shareholder interests over shareholder interests and wealth maximization, a director may still be held accountable through several means. The director may still be subject to legal liability for breaches of fiduciary duties. Because shareholders elect directors,[65] the director may also be removed or passed-up for renewal at the end of his or her term. Director and manager compensation in traditional corporations are still linked to share price and other profitability measures. Therefore, if shareholder wealth maximization is not a director's primary agenda, directors may see their compensation suffer. Finally, directors must also be wary of competitors who take market share or pursue takeover strategies based on shareholder value as their objective.

III. ANALYSIS

In response to the shortcomings in constituency statutes and company struggles to fit within the confines of the traditional shareholder wealth maximization model, B Lab,[66] a non-profit organization has facilitated the creation of model benefit corporation legislation. William H. Clark, Jr., a renowned attorney from Drinker Biddle & Reath LLP, drafted the "model legislation."[67] Some of Clark's most notable work includes the draft and legislation strategy that lead to the enactment of the North Dakota Publicly Traded Corporations Act.[68] With Clark's help, North Dakota enacted the first state corporation law in the United States that addresses "all of the major issues of corporate governance that are of concern to institutional investors."[69] In the public benefit corporation arena, Clark has drafted

62. *Id.* (citing Kathleen Hale, *Corporate Law and Stakeholders: Moving Beyond Stakeholder Statutes*, 45 ARIZ. L. REV. 823, 825 (2003)).

63. *Id.*

64. *Id.* at 137.

65. *See* MODEL BUS. CORP. ACT § 8.03 (2007). *See also* DEL. CODE ANN. tit. 8, § 141k(d) (2014).

66. *Benefit Corp. Info. Center*, BENEFIT CORP. INFO. CENTER, http://benefitcorp.net/about-b-lab.

67. *William H. Clark, Jr.*, DRINKERBIDDLE, http://www.drinkerbiddle.com/people/attorneys/clark-william-h.

68. *Id.*

69. *Id.*

benefit statutes that have been enacted in seven states, including California and New York.[70] In light of the shortcomings in North Dakota's constituency statute, the following is a discussion about the model public benefit corporation legislation that could be adopted in North Dakota. The model legislation was initially created by Clark, but has "evolved based on comments from corporate attorneys in the states in which the legislation has been passed or introduced."[71]

A. MODEL LEGISLATION PROVISIONS

Under the model legislation, public benefit corporations are defined as "traditional corporations, incorporated under a state's general corporate law, that have elected to be subject to special provisions that impose stricter accountability and transparency requirements and explicitly alter some traditional corporate norms."[72] The model legislation only applies to corporations that elect to be subject to the regulation; therefore, benefit corporations are simultaneously subject to the state's corporate laws.

The legislation allows corporations to pursue both specific and general public benefits. Specific public benefits include providing low income housing, promoting economic opportunities for individuals and communities beyond job creation, protecting the environment, promoting the arts and science, funding companies with a purpose to benefit society, and improving human health.[73] Because specifically listing benefits inherently limits the ability of corporations to pursue different missions, the legislation differs from constituency statutes by simultaneously allowing the pursuit of general public benefits. General public benefits are defined as "material positive impact[s] on society and the environment, taken as a whole, assessed against a third-party standard, from the business and operations of a benefit corporation."[74] The concept of general public benefit requires directors and managers to consider the effects of their business actions on society and the environment "as a whole."[75]

General public benefits also help to prevent companies from naming a single benefit and then dismissing all other non-financial interests. For example, Company A, with a general public benefit purpose, could not list producing affordable widgets as a specific purpose and then dismiss all

70. *Id.*

71. *Interested in Passing Benefit Corp. Legislation?*, BENEFIT CORP. INFO. CENTER, http://benefitcorp net/interested-in-passing-legislation.

72. MODEL BENEFIT CORP. LEGISLATION § 101(c) (B Lab 2013).

73. *Id.* at § 102.

74. *Id.*

75. *Id.*

other stakeholder concerns, such as keeping Company A's neighboring wetland free of toxins produced by its manufacture of widgets. Under the public benefit legislation, Company A would be required to consider environmental impacts while pursuing its low-price widget business strategy.

The process of creating a public benefit corporation is similar to the existing process of incorporation. The company must choose a business name, obtain a registered agent, reserve the business name, and create an article or certificate of incorporation depending on the state of incorporation.[76] The only difference is that the articles or certificate of incorporation must state that the company is a benefit corporation.[77] Existing corporations may also elect to be a public corporation by either amending their articles of incorporation or by undergoing a fundamental transaction, like a merger or acquisition, with a benefit corporation.[78] Both amendments and fundamental transactions require a minimum status vote, typically a two-thirds supermajority of voting shareholders.[79]

A company may terminate its status as a public benefit corporation by amending its articles of incorporation to delete the benefit provision or by merging or acquiring a non-benefit corporation.[80] The legislation provides both flexibility and protection for the benefit corporation status by requiring the amendment to have the minimum status vote required to have established the public benefit corporation status.[81] Substantial sales of the corporation's assets will not automatically terminate the status of the corporation.[82] Rather, such sales will terminate the operation of the business—a similar effect to terminating benefit status.[83]

Enforcement mechanisms for public benefit corporations that have undertaken to maximize outcomes for stakeholders do not come from governmental oversight but rather from transparency and accountability provisions included in the model legislation. Public benefit corporations are required to "prepare an annual benefit report that assesses . . . performance in creating general public benefit against a third-party standard . . . . "[84] An independent entity develops the third-party standards

76. *How to Form a New Business Entity,* STATE OF DELAWARE, http://corp.delaware.gov/howtoform.shtml.

77. MODEL BENEFIT CORP. LEGISLATION § 103 (B Lab 2013).

78. *Id.* at § 104.

79. *Id.*

80. *Id.* at §105.

81. *Id.*

82. *Id.*

83. *Id.*

84. *Id.* at §102.

that assess company compliance in an attempt to provide a protection against potential abuse of the benefit corporation status.[85] The evaluation criteria is publicly available in an attempt provide transparency.[86] The third-party standard also provides consistency and impartiality by allowing the independent entity to develop a niche expertise in assessing corporate social performance.

Public benefit corporations differ from traditional corporations by requiring the provision of extensive financial statements and annual benefit reports. Although the Securities Exchange Commission already requires substantial financial disclosures, the annual benefit report is required because a corporation's success in creating general or specific public benefits is not always readily determinable from financial statements. The report is intended to reduce "greenwashing," a phenomenon of businesses trying to portray themselves as being more environmentally and socially responsible then they are in reality.[87] It provides both consumers and the general public a way of evaluating whether businesses are fulfilling their corporate social responsibility claims.

The annual benefit report also allows shareholders to hold directors accountable. Because shareholders are responsible for electing a corporation's board of directors, the report is a resource shareholders can use to decide whether directors should be retained or dismissed. More importantly, unlike the typical derivative action, the model legislation creates "benefit enforcement proceedings" whereby shareholders can bring suit for a corporation's failure to pursue or create the public benefits enumerated in the articles of incorporation.[88] Although in theory shareholders can bring derivative actions against directors for failing to pursue social missions, shareholders would have difficulty successfully arguing that a director breached a fiduciary duty by maximizing shareholder profits.

B. IMPLICATIONS

As exemplified above, the model legislation has several provisions that differ from traditional principles and theories of corporate law. Consequently, if enacted, the provisions would have both intended and unintended consequences. The following section outlines some of these

85. *Id.*
86. *Id.*
87. *Id.*
88. *Id.*

legal and business implications while highlighting meritorious critiques of the proposed legislation.

1. *Legal Implications*

Benefit corporations are particularly enticing for states without constituency statutes in liquidity scenarios. As a result of *Revlon*, directors' protection by the business judgment rule is narrowed, requiring directors to take the highest offer regardless of the decision's impact on non-financial stakeholder interests.[89] Although North Dakota has a constituency statute, the state may still reap the benefits of the model legislation. Due to the lack of case law in all circuits, North Dakota lawyers and the directors and officers they counsel are provided with little clarity about how a court would rule if, during liquidation, a director "made a decision based on broader considerations than just the highest offer."[90]

The legislation also affects director fiduciary duties. While the business judgment rule affords directors some degree of deference in considering non-financial interests, decision-making is still constrained to shareholder wealth maximization. As exemplified by *Ford,* directors must take care to frame a decision that considers non-financial interests to appear as a decision that increases share value. Whether discussing these decisions in board meetings with discoverable minutes or subsequently justifying these decisions in court, directors and officers must, at minimum, carefully select their language to characterize the decision as eventually beneficial to share price. While constituency statutes afford greater protection for directors, they do little for companies, employees, consumers, and shareholders who want to require, rather than just permit, directors to consider non-financial interests.

2. *Business Implications*

While legal constraints play an important role in director and officer decision-making, corporate culture can play an even larger role. Generally, "shareholder wealth maximization is usually accepted as the appropriate goal in American business circles."[91] This norm is deeply embedded within American corporate culture and tradition. Therefore, despite the existence of some business judgment protection and the permissive language of constituency statutes, directors, officers, and many lawyers believe their

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

90. *Legal FAQ's*, BENEFIT CORP. INFO. CENTER, http://benefitcorp net/attorneys/legal-faqs.

91. Mark J. Roe, *The Shareholder Wealth Maximization Norm and Industrial Organization*, 149 U. PA. L. REV. 2063, 2065 (2001).

actions are constrained to solely acting in furtherance of shareholder interests.[92] Of those directors who believe social responsibility is important, several believe that the social responsibility of business is solely to increase profits.[93] Although case law such as *Revlon* and constituency statutes aid in changing these beliefs, the lingering effects of the rigid wealth maximization mindset act as a cultural impediment to actual corporate social responsibility. Creating a new corporate form that requires directors and officers to consider stakeholder interests can help to remove this impediment.

Opponents of the legislation argue that a company choosing to incorporate as a public benefit corporation is an unviable and unsustainable business model.[94] Such pundits argue that being a public benefit corporation limits a company's ability to raise capital because investors are unlikely to invest in companies that are unwilling and unable to prioritize their interests.[95] In response, proponents of the legislation argue that the demand for socially responsible employers, products, and investment opportunities has indicated otherwise.[96] Given recent scandals in both the non-profit and for-profit sectors, some investors prefer to fund companies that focus on long-term sustainability and transparency. Investors view corporations with strong governance practices as sound investment opportunities and are willing to invest in these companies despite the fact that their short-term interests may be subordinate to sustainable decision-making. The United States Forum for Sustainable and Responsible Investment quantified this demand in its 2014 report on United States Sustainable, Responsible and Impact Investing Trends.[97] According to the Forum, "the total US-domiciled assets under management using [sustainable, responsible and impact investing] strategies expanded from \$3.74 trillion at the start of 2012 to \$6.57 trillion at the start of 2014, an increase of 76 percent."[98] Key drivers of this trend include the increasing incorporation of environmental, social, and governance factors in money managers' investment analysis and portfolio constructions.[99] In gathering

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92. *Id.*
93. *Id.*
94. Anna R. Kimbrell, *Benefit Corporation Legislation: An Opportunity for Kansas to Welcome Social Enterprises*, 62 U. KAN. L. REV. 549, 565 (2013).
95. *Id.*
96. *Id.*
97. *See Report on U.S. Sustainable, Responsible and Impact Investing Trends 2014*, THE FORUM FOR SUSTAINABLE AND RESPONSIBLE INVESTMENT (2014), http://www.ussif.org/Files/Publications/SIF_Trends_14.F.ES.pdf.
98. *Id.* at 12.
99. *Id.* at 15.

data for the report, eighty percent of these money managers cited client demand as their motivation for including these factors.

Proponents would also argue that the legislation has already been proven to be a viable business model.[100] Currently, there are 780 benefit corporations incorporated across the country.[101] Some of the more notable corporations include multinationals like Home Care Associates, Method Products, Patagonia, Plum, Greyston Bakery, and the Rasmussen Colleges.[102]

IV. RECOMMENDATION

There are several critiques of the model benefit corporation legislation and many are meritorious. Commentators have characterized such legislation as untested, ambiguous, and uncertain.[103] Pundits have also criticized this legislation for a "perceived lack of director accountability and enforcement mechanisms . . . ."[104] In states like Michigan and North Carolina, legislators and lobbies defeated this proposed legislation by "claim[ing] that benefit corporations create a false dichotomy between 'good' and 'bad' business."[105] Other critics argue that benefit corporations are "unnecessary and that current corporate law is adequate to accommodate mission-driven businesses . . . ."[106] These critics may have merit, just as the legislation may have value.

There is an ongoing debate as to the necessity and value of adopting public benefit corporation legislation. Lawyers, business people, and legislators across the country continue to weigh the pros and cons of the new corporate form. Others choose to wait and watch states that have adopted the legislation. Given the complexity of the issue, this note is not intended to provide a conclusive answer as to whether the corporate form is definitively right or wrong for North Dakota. Rather, it should serve as a mechanism for highlighting some of the existing gaps in North Dakota's corporate laws. Discussing public benefit corporation legislation is an interesting approach to resolving some of these short-comings.

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100. Kimbrell, *supra* note 95, at 565.

101. *Legislative Talking Points*, BENEFIT CORP. INFO. CENTER, http://benefitcorp net/legislators/legislative-talking-points.

102. *Id.*

103. Alicia E. Plerhoples, *Delaware Public Benefit Corporations 90 Days Out: Who's Opting In?*, 14 U.C. DAVIS. BUS. L.J. 247, 249 (2014).

104. *Id.*

105. *Id.*

106. Kimbrell, *supra* note 95, at 565.

V. CONCLUSION

In 2007, North Dakota "enacted the nation's most shareholder-friendly corporate governance law" in a battle against other states for companies seeking to incorporate.[107] Delaware is well established as the most popular state for incorporation and is subsequently North Dakota's largest competitor. Although Delaware, like North Dakota, prides itself on being a shareholder-friendly state, Delaware amended its corporate law to include public benefit corporations on August 1, 2013.[108] Delaware has recognized the gaps in existing corporate law and pursued the public benefit corporation as a possible solution. Delaware's approach is to attract companies by affording incorporators with increased flexibility. Delaware is a leader in corporate law. As a state that is undergoing increased economic expansion and is receiving increased investment, North Dakota should continue to dialogue about this new corporate form.

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107. Cari Tuna, *Shareholders Ponder North Dakota Law*, WALL ST. J. (Dec. 8, 2008), http://www.wsj.com/articles/SB122852051008284099.

108. *See* DEL. CODE ANN. tit. 8, § 361 (2013).

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