The Future or Fancy? An Empirical Study of Public Benefit Corporations

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Abstract

The public benefit corporation ("PBC") is one of the most hyped developments in corporate law, due to the PBC's unique social purpose. Unlike the traditional corporation, directors of PBCs are required under their fiduciary duties to consider the impact of their decisions on a range of stakeholders and communities. This new form is hailed by many as a framework for a reformed capitalism. Critics, on the other hand, have assailed PBCs as unworkable—at best allowing corporations to "greenwash," providing a thin disguise for ordinary corporate profit-seeking behavior. What has been lacking in this debate is evidence about whether and how the new form is being adopted. We fill this gap with an empirical study of early-stage investment in PBCs. Early-stage investment, consisting of venture capital and similar funds, presents an interesting test case for PBC funding, because these investors have profit-maximizing incentives and fiduciary duties of their own. Using our novel dataset, we can discern whether for-profit investment is occurring in PBCs, and if so, whether it is different in kind from ordinary early stage investment. We find that PBCs are receiving investment at significant rates, and that funding is coming from typical sources of venture capital—including traditional, profit-seeking VC firms. We also find that VC firms are investing in more consumer-facing industries, as well as investing smaller amounts than traditional investments at the same stage, raising concerns about greenwashing. While the ultimate arc of the PBC remains uncertain, our results show that it is gaining acceptance as an investment that can earn an acceptable rate of return—though, as we argue, the PBC status itself may be a secondary factor in VCs' decisions. We use these results to develop a theory of future PBC development, which asserts that in the medium term, investment in PBCs is likely to remain siloed in smaller, newly formed firms. We conclude that widespread adoption of the form will take time, as network effects build and experience with the form becomes embedded within the entrepreneurial and legal ecosystem. The PBC is not a failure. But it is in its infancy, and any full embrace will take a significant period of time.

Keywords: Public Benefit Corporations, Venture Capital, For-Profit Investment

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Abstract

The public benefit corporation ("PBC") is one of the most hyped developments in corporate law, due to the PBC's unique social purpose. Unlike the traditional corporation, directors of PBCs are required under their fiduciary duties to consider the impact of their decisions on a range of stakeholders and communities. This new form is hailed by many as a framework for a reformed capitalism. Critics, on the other hand, have assailed PBCs as unworkable—at best allowing corporations to "greenwash," providing a thin disguise for ordinary corporate profit-seeking behavior.

What has been lacking in this debate is evidence about whether and how the new form is being adopted. We fill this gap with an empirical study of early-stage investment in PBCs. Early-stage investment, consisting of venture capital and similar funds, presents an interesting test case for PBC funding, because these investors have profit-maximizing incentives and fiduciary duties of their own. Using our novel dataset, we can

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discern whether for-profit investment is occurring in PBCs, and if so, whether it is different in kind from ordinary early stage investment.

We find that PBCs are receiving investment at significant rates, and that funding is coming from typical sources of venture capital—including traditional, profit-seeking VC firms. We also find that VC firms are investing in more consumer-facing industries, as well as investing smaller amounts than traditional investments at the same stage, raising concerns about greenwashing. While the ultimate arc of the PBC remains uncertain, our results show that it is gaining acceptance as an investment that can earn an acceptable rate of return—though, as we argue, the PBC status itself may be a secondary factor in VCs' decisions.

We use these results to develop a theory of future PBC development, which asserts that in the medium term, investment in PBCs is likely to remain siloed in smaller, newly formed firms. We conclude that widespread adoption of the form will take time, as network effects build and experience with the form becomes embedded within the entrepreneurial and legal ecosystem. The PBC is not a failure. But it is in its infancy, and any full embrace will take a significant period of time.

INTRODUCTION

The public benefit corporation ("PBC") is one of the hottest developments in corporate law.[1] The *sine qua non* of this new form is that directors are required under their fiduciary obligations to consider a social purpose in addition to the traditional profit-seeking duty. The

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[1] A close cousin to the PBC is the benefit corporation ("BC"). The two forms do have some different characteristics, but they share the core shift from the traditional corporation that matters most for our purposes: the requirement that the board consider other prosocial values in addition to profit-seeking when setting corporate strategy. Our data sample consists entirely of PBCs, but we suspect the pattern of VC investment in BCs will turn out to be similar.

PBC has thus been described as different from the traditional corporation, which in some measure must be devoted solely to a for-profit motive.[2] The PBC has been hailed as the "new corporate form": one that permits a corporation to both "do well" and "do good", earning money while also serving a social purpose.

While there has been significant hype and theoretical consideration of this new form, to date there has been little empirical study.[3] Critics of the PBC argue that it will be used for "purpose washing," merely donning the garb of social good for public relations purposes, while actually pursuing a purely for-profit motive.[4] Other critics argue that the current corporate form already has enough latitude to serve multiple purposes.[5] Advocates counter that the PBC will do nothing

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[2] The seminal case on this point is *Dodge v. Ford Motor Co.*, 204 Mich. 459, 170 N.W. 668 (1919), which held that "[a] business corporation is organized and carried on primarily for the profit of the stockholders." *Id.* at 507. While this case is often cited as the principle that corporations are for profit, whether this is the actual law in other states is still subject to debate and an open question. *See* Lynn A. Stout, *Why We Should Stop Teaching* Dodge v. Ford, Sept. 18, 2007, Law-Econ Research Paper No. 07-11. UCLA School of Law. SSRN 1013744. There are those however who argue that this is a decided question and the corporation's goal is indeed to seek profit. *See* Leo E. Strine, Jr., *Our Continuing Struggle with the Idea That For-Profit Corporations Seek Profit*, 47 WAKE FOREST L. REV. 135, 136 (2012) (arguing that we should "recogniz[e] that for-profit corporations will seek profit for their stockholders using all legal means available.")

[3] *See, e.g.,* Ellen Berrey*, Social Enterprise Law in Action: Organizational Characteristics of U.S. Benefit Corporations*, 20 TENN. J. BUS. L. 21 (2018).

[4] *See* Caleb Diehl, *Benefit Company Label Marred by Confusion and Lax Reporting Practices*, OREGON BUSINESS (Sep. 20, 2018), https://www.oregonbusiness.com/article/energy-environment/item/18511-benefit-company-label-marred-by-confusion-and-lax-reporting-practices; Kennan El Khatib, *The Harms of the Benefit Corporation*, 65 AM. U. L. REV. 151, 182 n.172 (2015); Dan Pontefract, *Stop Confusing CSR With Purpose*, FORBES (Nov. 18, 2017), https://www.forbes.com/sites/danpontefract/2017/11/18/stop-confusing-csr-with-purpose/.

[5] *See* Joan MacLeod Heminway, *Let's Not Give Up on Traditional For-Profit Corporations for Sustainable Social Enterprise*, 86 UMKC L. REV. 779, 800-01 (2018) (asserting that "[u]nder existing corporate law doctrine, theory, and policy, sustainable social enterprises have been, are being, and may be properly and

less than transform U.S. capital markets, arguing that the profit maximization norm has contributed to a litany of preventable social ills, from global warming to income inequality, and from declining job stability to political corruption.[6] By incorporating values other than profit-seeking into a company's "DNA," proponents assert, the law can tame capitalism's worst excesses while retaining its many virtues.[7]

But these are theories. Not only is there no empirical study of any of these arguments, we lack even more fundamental metrics of PBC

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profitably formed, and may continue to exist, as [conventional corporations]--even with the relatively new introduction of benefit corporations and other social enterprise forms of entity"); Peter Molk, *Do We Need Specialized Business Forms for Social Enterprise?*, in THE CAMBRIDGE HANDBOOK OF SOCIAL ENTERPRISE LAW 241, 244 (Benjamin Means & Joseph W. Yockey eds., 2018) ("[M]any firms that have now converted to one of the new social enterprise forms first operated for many years as corporations. And they were able to do so because corporate law has long allowed corporations the flexibility to consider other constituents beyond investors."); El Khatib, *supra* note 3, at 188; Mark A. Underberg, *Benefit Corporations vs. "Regular" Corporations: A Harmful Dichotomy*, HARV. L. SCH. F. ON CORP. GOVERNANCE & FIN. REG. (May 13, 2012), https://corpgov.law.harvard.edu/2012/05/13/benefit-corporations-vs-regular-corporations-a-harmful-dichotomy/.

[6] *See* Jay Coen Gilbert, *Maximising Shareholder Profits Still Rules the Day for US Businesses*, THE GUARDIAN (Aug. 13, 2013), https://www.theguardian.com/sustainable-business/maximising-shareholder-profits-rules-us-businesses; Steven Pearlstein, *How the Cult of Shareholder Value Wrecked American Business*, WASHINGTON POST (Sep. 9, 2013), https://www.washingtonpost.com/news/wonk/wp/2013/09/09/how-the-cult-of-shareholder-value-wrecked-american-business/; Tess Riley, *Just 100 Companies Responsible for 71% of Global Emissions, Study Says*, THE GUARDIAN (Jul. 10, 2017), https://www.theguardian.com/sustainable-business/2017/jul/10/100-fossil-fuel-companies-investors-responsible-71-global-emissions-cdp-study-climate-change.

[7] Gilbert, *supra* note 5; Jack Rodolico, *Benefit Corporations Look Beyond the Profit Motive*, NPR (June 18, 2014), https://www.npr.org/2014/06/18/316349988/benefit-corporations-look-beyond-the-profit-motive; Ariel Schwartz, *A Q&A With B Lab's Andrew Kassoy About Benefit Corporations, B Corp Certification, and Everything In Between*, FAST COMPANY (March 11, 2014), https://www.fastcompany.com/3027420/a-qa-with-b-labs-andrew-kassoy-about-benefit-corporations-b-corp-certification-and-everythin.

foundation and formation.[8] Are PBCs being funded? If so, by whom—and to what degree? We aim to close this gap by conducting an empirical study of early-stage investment in PBCs. Our strategy is to examine the universe of PBC formations and the types of investment they receive. We do so through early-stage investment, which consists of the usual range of angel investors, accelerators and incubators, venture capital funds, and private equity. Together, these present an interesting test case for PBC funding, because the investors themselves often have profit-maximizing incentives and fiduciary duties. By examining early-stage investment we can discern whether for-profit investment is occurring in PBCs, and if so, whether it is different in kind from traditional VC investment. This allows us to assess the development of PBCs, and the potential for future large-scale investment and utilization of the forms by mainstream companies. This study of early-stage investment also provides some evidence on how PBCs are being used: do they appear to serve wider purposes, or are they simply purpose-washing devices?

We collate a dataset of all Delaware-registered PBCs that received investment between 2013 and 2019. This comprises a small but not trivial number of companies (n = 295). We then examine the type and scope of early-stage investment in these companies. We find that early-stage investment in PBCs is indeed significant (over $2.5 billion), and includes well-known companies such as Allbirds, Lemonade, and Numi Tea.[9] Moreover, we find that PBCs are being funded over a wide range of mostly consumer-focused industries (banking, food, education, technology, and more), by traditional, for-profit venture capital investment firms.[10] Our evidence suggests that PBC round sizes are slightly smaller than their purely profit-seeking

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[8] The only comprehensive study that we are aware of is by Professor Ellen Berrey, who found that between 2010 and 2018, 7,704 BCs and PBCs were formed. Berrey, *supra* note 3, at 1.
[9] *See infra,* note 109 and associated text.
[10] *See infra,* note 110-112 and associated text.

peers, but that on average investment occurs at similar stages to traditional startups.[11]

Our results confirm that PBCs are being utilized as for-profit investment vehicles at a steady rate. PBCs are attracting investment, despite their split focus. We find that consumer-focused PBCs receive higher average investments that their non-consumer peers. At first blush, this supports the purpose-washing hypothesis, but we also consider alternative possible explanations.

We conclude by drawing some new theories on the future of investment in PBCs. We theorize that PBCs still have significant hurdles to widespread adoption. One of the primary drawbacks to widespread use of PBCs is the lack of case law on the scope of fiduciary duties and certainty of board action under the new statute.[12] The investment patterns and flows that we find show that this has not deterred investment, but also that the PBC has not garnered unmitigated support from the VC community.

We argue that, based on our results, PBC status remains a secondary driver of early-stage investment and, by proxy, more widespread for-profit investment. VCs and other investors appear willing to tolerate the PBC's wider purpose, but want to ensure some for-profit motive, and they focus on consumer-facing companies where PBC status is more likely to buttress a profit purpose. We suspect that the consequence of this is that the widespread use of the PBC remains some way off, but that there is groundwork being laid for more significant adoption. This will only come once there is a greater network of companies and lawyers familiar with the form and willing

[11] *See infra*, note 113 and associated text.

[12] *See* Roxanne Thorelli, *Providing Clarity for Standard of Conduct for Directors Within Benefit Corporations: Requiring Priority of a Specific Public Benefit*, 101 MINN. L. REV. 1749, 1751-52 (2017).

to have their companies opt in to the PBC framework.[13] Until then, PBCs are likely to be the purview of small and start-up businesses and, when utilized by for-profit companies, we suspect the social purpose will remain secondary to their for-profit motive.

Part I examines the use and scope of PBCs and provides a theoretical framework for investors' willingness to participate in these relatively new forms. Part II describes the data that we use to evaluate our theoretical framework and sets out our findings. Part III builds on our empirical analysis to offer a theory for the future development and growth of PBCs. Ultimately, we draw a mixed view of PBCs, one that sees them neither as the form of the future nor as a mere fancy. Instead, this is an emerging corporate form that is very early in its lifecycle, awaiting more significant networks to develop to support its growth. If these networks develop, PBCs may attract much wider usage than is currently the case.

I. WHY MIGHT VENTURE CAPITALISTS INVEST IN PBCS?

A. Introduction

The PBC form serves as the latest salvo in the long-raging debate about the corporation's proper purpose. The shareholder primacy approach—rooted in Jensen and Meckling's view of the corporation as a "nexus of contracts"—holds that boards of directors should run corporations primarily for the benefit of the shareholders, with all corporate actions ultimately aimed at maximizing profits.[14] Adherents

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[13] *See* Mark A. Lemley & David McGowan, *Legal Implications of Network Economic Effects*, 86 CALIF. L. REV. 479, 562 (1998); Mohsen Manesh, *Legal Asymmetry and the End of Corporate Law*, 34 DEL. J. CORP. L. 465, 509 (2009).

[14] *See* Michael C. Jensen & William H. Meckling, *The Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure*, 3 J. FIN. ECON. 305 (1976) ("[W]e believe the emphasis which Alchian-Demsetz place on joint input production is too narrow and therefore misleading. Contractual relations are the

have raised many arguments in favor of this position, including that shareholders are the most vulnerable participants in the corporate enterprise, that shareholders are the owners of the corporation, and that shareholders are the residual claimants of the corporation.[15] They may acknowledge that corporations run purely for profit will have incentives that run contrary to broader societal interests, but rely on regulation outside of corporate governance to moderate corporate behavior.[16]

The opposing, managerialist view stems from Ronald Coase's definition of the boundaries of the firm as the space where transactions occur by fiat, rather than by voluntary market exchanges, which arguably implies that the firm is an entity separate from its constituent parts and may have separate interests and concerns.[17] Advocates argue

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essence of the firm, not only with employees but with suppliers, customers, creditors, etc.");

[15] *See, e.g.,* Stephen M. Bainbridge, *Director Primacy: The Means and Ends of Corporate Governance*, NW. U. L. REV. 547, 588 at n. 199 (vulnerable); FRANK EASTERBROOK & DANIEL FISCHEL, THE ECONOMIC STRUCTURE OF CORPORATE LAW (1991) (residual claimants); Milton Friedman, *The Social Responsibility of Business Is to Increase Its Profits*, N.Y. TIMES MAG. (Sept. 13, 1970), at 32-33, 122-26 (owners).

[16] *See* Leo E. Strine, Jr. & Nicholas Walter, *Conservative Collision Course?: The Tension Between Conservative Corporate Law Theory and Citizens United*, 100 CORNELL L. REV. 335, 339 ("Conservative corporate theory acknowledges that corporations have a rational incentive to try to externalize the costs of their conduct to society (e.g., by taking environmental shortcuts), while internalizing the resulting excess profits reaped from those shortcuts. The answer of conservative corporate theory is that the duty of corporate managers to pursue profit is checked by their duty to do so within the "rules of the game"—the laws and regulations enacted by legislators, who represent not corporations but society as a whole").

[17] *See* Ronald H. Coase, *The Nature of the Firm*, 4 ECONOMICA 386 (1937) ("Outside the firm, price movements direct production, which is coordinated through a series of exchange transactions on the market. Within a firm, these market transactions are eliminated and in place of the complicated market structure with exchange transactions is substituted the entrepreneur-coordinator, who directors production."). *See also* Melvin A. Eisenberg, *The Conception that the Corporation is a Nexus of Contracts, and the Dual Nature of the Firm*, 24 J. CORP. L. 819 (1998)

that corporations thrive best when each group that contributes to its success – investors, employees, and communities – possess ample incentive to make firm-specific investments. Corporate law provides wide latitude to boards of directors to manage corporations as they see fit in order to empower them to balance the needs of different input providers and encourage each of these providers to make relationship-specific investments.[18]

Some commentators have also argued that corporations are inherently focused on the short term, leading them to impose negative externalities on government welfare programs, the environment, customers, employees, and even future shareholders. This focus stems from current shareholders' – and therefore current managers' – preference to avoid costs that can be externalized to others, and to delay costs to the future when the current participants may no longer be connected to the corporation.[19] This camp may also doubt the

("Coase characterized the boundaries of the firm as the range of exchanges over which the market system was superseded and resource allocation was accomplished instead by authority and direction.").

[18] *See* Margaret M. Blair and Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 VA. L. REV. 247, 253 ("The team production model . . . suggests that the legal requirement that public corporations be managed under the supervision of a board of directors has evolved not to reduce agency costs--indeed, such a requirement may exacerbate them--but to encourage the firm-specific investment essential to certain forms of team production. In other words, boards exist not to protect shareholders per se, but to protect the enterprise-specific investments of all the members of the corporate 'team,' including shareholders, managers, rank and file employees, and possibly other groups, such as creditors.").

[19] *See* Kent Greenfield, *The Puzzle of Short-Termism*, 46 WAKE FOREST L. REV. 627, 627-28 (2011) ("A company might refuse to provide health benefits to its employees, leaving Medicare or Medicaid to pick up the tab. The company might save on production costs by skirting environmental laws, thereby forcing communities, neighbors, or employees to suffer risks of harm that do not need to be accounted for on the company's financial statements. Alternatively, the company could sell shoddy products to one-time purchasers, produce goods in sweatshops, or underfund employees' pension funds. . . . Current shareholders may prioritize present returns over future returns, and current shareholders may not expect to be future shareholders at all. This means that corporate managers have incentives not only to externalize costs to current and future stakeholders whose interests they can ignore

government's ability to regulate corporations effectively, in part because of corporations' ability to dominate the political system through lobbying and campaign contributions.[20]

These opposing schools of thought have long disputed the normative point of what the obligation of corporate boards in managing traditional corporations ought to be. But most corporate scholars now agree that descriptively, Delaware law commands boards to pursue profit maximization for shareholders' benefit.[21]

Corporate reformers launched an innovative end-run around this debate about a decade ago. They pushed for a new form of legal business entity that would resemble the corporation in all relevant

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but also to future shareholders as well. This means that corporations will, by their very natures, be fixated on the short term.") (internal notes omitted).

[20] *See* LAWRENCE LESSIG, REPUBLIC, LOST: HOW MONEY CORRUPTS POLITICS – AND A PLAN TO STOP IT 81-84 (2011) (explaining the Great Recession in large part as a result of a campaign by finance firms to deregulate derivatives through campaign contributions); Russ Feingold, *The Money Crisis: How Citizens United Undermines Our Elections and the Supreme Court,* 64 STAN. L. REV. ONLINE 145, 149 (2012) ("[Because of the Supreme Court's *Citizens United* decision,] instead of small-dollar, online donors, the most prominent actors in the 2012 election cycle are unnamed corporations and a small group of influential--primarily conservative--billionaires."); Matthew D. Hill, G. Wayne Kelly, G. Brandon Lockhart & Robert A. Van Ness, *Determinants and Effects of Corporate Lobbying*, 42 FIN. MGMT. ASS'N INT'L 931, 954 (2013) ("[M]any firms use multiple channels of potential political influence to influence regulatory and policy outcomes. Our results also suggest that firms with greater potential payoffs from favorable policy and regulations are those that lobby more actively.");

[21] *See* Stephen M. Bainbridge, *In Defense of the Shareholder Wealth Maximization Norm: A Reply to Professor Green*, 50 WASH. & LEE L. REV. 1423, 1424–25 (1993) ("At least in Delaware, the shareholder wealth maximization norm . . . remains a more accurate description of the state of the law than any of its competitors."); Leo E. Strine, Jr., *Our Continuing Struggle with the Idea That For-Profit Corporations Seek Profit*, 47 WAKE FOREST L. REV. 135, 151 (2012) ("Directors for a for-profit Delaware corporation cannot deploy a rights plan to defend a business strategy that openly eschews stockholder wealth maximization—at least not consistently with the directors' fiduciary duty under Delaware law.") (citing *eBay Domestic Holdings, Inc. v. Newmark*, 16 A.3d 1 (Del. Ch. 2010)).

respects except that it would pursue social good as well as profit. Boards of these new entities would have to balance the pursuit of profit against the interests of other corporate constituencies such as employees, communities, and the environment and against the provision of social good.[22] This new form's requirements actually exceed the managerialists' classical goals, since these entities are required not only to consider other constituencies who might thereby be induced to make firm-specific investments but also to take into account the role of corporate activity in promoting benefits to those entirely outside the corporate framework.[23]

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[22] *See* Rae André, *Assessing the Accountability of the Benefit Corporation: Will This New Gray Sector Organization Enhance Corporate Social Responsibility?,* 110 J. BUS. ETHICS 133, 134 (2012) ("They function as corporations have always functioned (having private ownership and entering into business to make a profit for their shareholders), yet at the same time they are empowered by law to compromise private profit-making in order to pursue a more publicly-oriented CSR mission. This new type of corporation has a mission to do well (e.g., to make a profit) by doing good (e.g. by enhancing CSR), and in the process allows itself to be significantly influenced by stakeholders other than shareholders."); Michael B. Dorff, *Why Benefit Corporations?*, 42 DEL. J. CORP. L. 77 (2017).

[23] *See* Del. Gen. Corp. L. §365(a) ("The board of directors shall manage or direct the business and affairs of the public benefit corporation in a manner that balances the pecuniary interests of the stockholders, the best interests of those materially affected by the corporation's conduct, and the specific public benefit or public benefits identified in its certificate of incorporation."). BCs are subject to similar requirements. *See* Model Act §301(a) ("In discharging the duties of their respective positions and in considering the best interests of the benefit corporation, the board of directors, committees of the board, and individual directors of a benefit corporation: (1) shall consider the effects of any action or inaction upon: (i) the shareholders of the benefit corporation; (ii) the employees and the work force of the benefit corporation, its subsidiaries, and its suppliers; (iii) the interests of customers as beneficiaries of the general public benefit or a specific public benefit purpose of the benefit corporation; (iv) community and societal factors, including those of each community in which offices or facilities of the benefit corporation, its subsidiaries, or its suppliers are located; (v) the local and global environment; (vi) the short-term and long-term interests of the benefit corporation, including benefits that may accrue to the benefit corporation from its long-term plans and the possibility that these interests may be best served by the continued independence of the benefit

It is somewhat ironic, then, given that the PBC form was designed to implement the managerialists' view, that to test the utility of the form we have to take the shareholders' perspective. We need to know whether the creators of the new form went too far in shifting the corporate purpose so that now a key constituent – the shareholders – will refuse to participate. In particular, our concern is with a subset of the shareholders – outside investors.[24]

Outside investors are critical to the success of most high-growth, start-up enterprises, the type that have the potential to earn billions in revenue and employ thousands of people.[25] These businesses typically achieve high growth rates in their early stages by sacrificing profitability for growth, spending much more than they earn to develop new products and services and market to potential customers.[26] Without an inflow of capital to finance these early losses, these

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corporation; and (vii) the ability of the benefit corporation to accomplish its general public benefit purpose and any specific benefit purpose . . . .").

[24] One of us has written elsewhere about the interests of a different subset of shareholders, the founders/entrepreneurs. *See* Michael B. Dorff, *Why Public Benefit Corporations?*, 42 DEL. J. CORP. L. 77 (2017).

[25] *See* David H. Hsu, *Venture Capitalist and Cooperative Start-up Commercialization Strategy*, 52 MGMT. SCI. 204, 217 (2006) (empirical study found that VC-backed firms were more likely to engage in strategic alliances and technology licensing arrangements than comparable firms that did not receive VC backing).

[26] *See* Alison Coleman, *Profitability Versus Growth: A Balancing Act For Startups*, FORBES (Mar. 4 2018), https://www.forbes.com/sites/alisoncoleman/2018/03/04/profitability-versus-growth-a-balancing-act-for-startups/ (quoting entrepreneurs explaining the need to reinvest profits into the business); Xin En Lee, *No Profit? No Problem. Investors Keep Snapping Up Loss-Making Companies*, CNBC (Aug. 29, 2018), https://www.cnbc.com/2018/08/29/no-profits-no-problem-the-economy-has-a-growing-appetite-for-unprofitable-companies.html (investors are comfortable with tech companies losing money in order to achieve faster growth); Spencer Soper and Mark Bergen, *Amazon Has a Plan to Become Profitable. It's Called Advertising*, BLOOMBERG (Jan. 18, 2008), https://www.bloomberg.com/news/articles/2018-01-18/amazon-has-a-plan-tobecome-profitable-it-s-called-advertising (Amazon has sacrificed profits for growth for two decades).

businesses will typically fail before they achieve consistent profitability. There are exceptions. Some company founders have already achieved great wealth from prior successful start-ups and can self-finance.[27] Some businesses do not require huge investments of capital up front and are therefore profitable almost from the outset and capable of funding themselves organically out of profits.[28] But both these exceptions are relatively rare. Most companies with ambitions to

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[27] For example, Amazon founder Jeff Bezos has said that he has been selling $1 billion of Amazon stock per year to finance his space company Blue Origin. *See* Nicholas St. Fleur, *Jeff Bezos Says He is Selling $1 Billion a Year in Amazon Stock to Finance Race to Space*, N.Y. TIMES (Apr. 5 2017), https://www.nytimes.com/2017/04/05/science/blue-origin-rocket-jeff-bezos-amazon-stock.html. Even enormously successful entrepreneurs may require outside funding for subsequent ventures. For example, Elon Musk, who earned on the order of $150 million when he and his co-founders sold PayPal to eBay, required substantial outside funding for his ventures Tesla and SpaceX. *See* Owen Thomas, *Tesla's Elon Musk: "I Ran Out of Cash"*, VENTURE BEAT (May 27, 2010) https://venturebeat.com/2010/05/27/elon-musk-personal-finances/ (Musk realized some $160 million when PayPal was sold); Alex Knapp, *SpaceX is Raising a $500 Million Funding Round at a $25 Billion Valuation*, FORBES (Apr. 12, 2018); *Tesla Funding Rounds*, CRUNCHBASE, https://www.crunchbase.com/organization/tesla-motors/funding_rounds/funding_rounds_list#section-funding-rounds (last viewed Jun. 26, 2019) (Tesla raised $17.8 billion over 33 funding rounds).

[28] For example, Nick Woodman, the founder of GoPro, started the company in 2004 with $250,000 from family, friends and selling bead and shell belts from his van. Over a decade later, GoPro earned about $1.15 billion in revenue in 2018. *See* Lizette Chapman, *How Family Ties Helped Nick Woodman Make GoPro Click*, WALL STREET J. (Jun. 20 2013), https://blogs.wsj.com/venturecapital/2013/06/20/how-family-ties-helped-nick-woodman-make-gopro-click/; Greg Jarboe, *GoPro: One of the Biggest Youtube Success Stories Ever*, TUBULAR INSIGHTS (Jun. 9, 2014), https://tubularinsights.com/gopro-youtube-success/; Press Release, GoPro, GoPro Announces Fourth Quarter and Full Year 2018 Results (Feb. 6, 2019), https://investor.gopro.com/press-releases/press-release-details/2019/GoPro-Announces-Fourth-Quarter-and-Full-Year-2018-Results/default.aspx.
Cards Against Humanity, was crowdfunded on Kickstarter with $15,570 in 2011. After the series of unconventional marketing tactics the company earned over $12 million three years later. *See* Cards Against Humanity Kickstarter Page, https://www.kickstarter.com/projects/maxtemkin/cards-against-humanity (last visited Jun. 3, 2019); Christine Largorio-Chafkin, *The Humans Behind Cards Against Humanity,* INC. (Jan. 6, 2014), https://www.inc.com/christine-lagorio/humans-behind-cards-against-humanity.html.

grow quickly must secure substantial outside investment to have any chance at success. The fate of the PBC form therefore depends to a great degree on investors' willingness to furnish capital to companies that have adopted one of these new forms.

We present here the first in-depth theoretical analysis of why investors might or might not choose to fund these enterprises. In doing so, we must discuss two groups of investors separately: traditional, for-profit investors, whose goal is to maximize the return on their investment, and prosocial investors, who are willing to sacrifice some degree of financial return for investments that will produce social good.

Looming in the background of this debate is a concern that the PBC status is simply a propaganda tool. Some have argued that traditional corporations already have the ability to engage in the actions that those who support PBCs desire,[29] and that the PBC form is likely to result in "purpose washing" without the accountability of a traditional company.[30] We take no position here on the wider debate. Instead, the purpose of this article is focused on whether the PBC is attracting for-profit investment, and what it means for the future of this form.

B. For-Profit Investors

It is believed that for-profit investors generally search purely for the highest returns possible for any given level of risk. They are theoretically indifferent as to whether the target companies also produce externalities (positive or negative)—or at least they invest as if they were indifferent.

If this theoretical construct is true, such investors would seem likely to avoid investing in PBCs. The core function of this new form of business organization is to ensure that companies organized this way

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[29] *See supra*, note 4.
[30] *See supra*, note 3.

will pursue not only profit, but also social good. While many businesses provide economic value to society — by providing valuable goods and services, as well as jobs and a tax base — PBCs must provide something more. The Delaware statute requires PBCs to operate "in a responsible and sustainable manner" and to be "managed in a manner that balances the stockholders' pecuniary interests, the best interests of those materially affected by the corporation's conduct, and the public benefit or public benefits identified in its certificate of incorporation."[31]

The identification of a public benefit may not always worry investors unduly. Indeed, many of the "public benefits" are already provided by traditional corporations as part of their profit-seeking business model. The Delaware statute defines a public benefit as "a positive effect (or reduction of negative effects) on 1 or more categories of persons, entities, communities or interests (other than stockholders in their capacities as stockholders) including, but not limited to, effects of an artistic, charitable, cultural, economic, educational, environmental, literary, medical, religious, scientific or technological nature."[32]

The business model of pharmaceutical companies, for example, is to sell therapeutic substances. Their primary motive for doing so is to earn a profit, but they are clearly providing a medical benefit within the definition of the statute. Their profit motive for doing so should not disqualify them, since PBCs are profit-seeking entities. Similarly, a pharmaceutical company might well donate some money to charity, as most major corporations do for marketing purposes, and might also engage in educational efforts (if only to educate physicians on the value of their products). The specific public benefit then, might not distinguish a PBC from a traditional corporation very effectively, and

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[31] *See* Del. Gen. Corp. L. §362(a).
[32] Del. Gen. Corp. L. §362(b).

may not present a concern to profit-seeking investors, at least in the general case.

But PBCs are also required to balance the interests of stockholders against those of others materially affected by the corporation's conduct.[33] This requirement may sometimes require PBCs to sacrifice profit in order to accommodate other corporate constituencies. While the Delaware courts have yet to interpret the PBC statute, they might be influenced in reading the "those materially affected by the corporation's conduct" rule by the parallel provision in the Model Act, which governs the analogous business organization, the benefit corporation ("BC"), in many other states.[34]

The Model Act requires BCs to provide a "general public benefit,"[35] which that statute defines in relevant part as a "material positive impact on society and the environment."[36] The Model Act mandates

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[33] Del. Gen. Corp. L. §§ 362(a) ("A "public benefit corporation" is a for-profit corporation organized under and subject to the requirements of this chapter that is intended to produce a public benefit or public benefits and to operate in a responsible and sustainable manner. To that end, a public benefit corporation shall be managed in a manner that balances the stockholders' pecuniary interests, the best interests of those materially affected by the corporation's conduct, and the public benefit or public benefits identified in its certificate of incorporation."); 365(a) ("The board of directors shall manage or direct the business and affairs of the public benefit corporation in a manner that balances the pecuniary interests of the stockholders, the best interests of those materially affected by the corporation's conduct, and the specific public benefit or public benefits identified in its certificate of incorporation.").

[34] The Model Act can be found here: https://benefitcorp.net/sites/default/files/Model%20benefit%20corp%20legislation%20_4_17_17.pdf.

[35] *See* Model Act §201 ("A benefit corporation shall have a purpose of creating a general public benefit.").

[36] Model Act, §102. The full definition is, "A material positive impact on society and the environment, taken as a whole, from the business and operations of a benefit corporation assessed taking into account the impacts of the benefit corporation as reported against a third-party standard." BCs may also choose to adopt a specific public benefit, which is fairly broadly defined, but they are not required to do so. *See*

that BC boards, in making any decision on behalf of the BC, consider the effects of the decision on the shareholders; the employees of the BC; the employees of the BC's subsidiaries and suppliers; customers who gain from the provision of the general public benefit or any specific public benefit the BC has adopted; the community and societal factors; the environment, both locally and globally; the short-term and long-term interests of the BC; and the ability of the BC to accomplish its general public benefit purpose and any specific public benefit purpose.[37] Officers with relevant authority must also consider these factors in making decisions on behalf of a BC.[38]

The factors that boards and officers must consider under the Model Act could all conceivably be covered by the Delaware statute's "those materially affected by the corporation's conduct" rule, assuming the Delaware courts give a broad construction to that phrase.[39] But the Delaware courts might also limit that phrase by excluding some of the broader categories listed in the Model Act, such as the global environment.

The broader the reading Delaware courts ultimately give to this requirement, the more one might expect profit-seeking investors to shy away from PBCs. Nevertheless, there are three reasons why for-profit

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Model Act §201(b) ("The articles of incorporation of a benefit corporation may identify one or more specific public benefits that it is the purpose of the benefit corporation to create . . . .").

[37] *See* Model Act §301(a)(1).

[38] *See* Model Act §303(a)

[39] *See* Del. Gen. Corp. L. §362(a). As of this writing, there are no reported Delaware cases interpreting the PBC statute, but noted Delaware corporate law expert Rick Alexander interprets the phrase broadly as including environmental concerns. *See* FREDERICK H. ALEXANDER, BENEFIT CORPORATION LAW AND GOVERNANCE: PURSUING PROFIT WITH PURPOSE 89 (2018) ("Although some have expressed concern that the PBC statute does not explicitly address the environment, this phrase clearly picks up any environmental issue that has an effect on people (since such people would be materially affected by degradation or improvement in their environment).").

investors might prove willing to invest in PBCs: (1) PBCs may earn greater profits despite investing resources in generating social good; (2) PBCs may engage in purpose washing rather than actually investing resources in generating social good; and (3) the company's business model may be sufficiently promising, in an environment which high-growth-potential businesses are relatively scarce, to offset any disadvantage incurred by the PBC legal form. We explore each of these reasons in the next subsections.

1. PBCs May Earn Greater Profits

First, investors might believe that PBCs will earn greater profits precisely because of their prosocial status. While counterintuitive, there are three rationales that might support this theory. One is that the balancing requirement might promote managerial behavior that is profit-maximizing, especially over the longer term. Managers of traditional corporations might also engage in such behavior, but they may feel pressure to generate immediate profits, which might inhibit them from bearing short-run costs that ultimately redound to the company's benefit. Conversely, the mandatory focus on other corporate constituencies in the PBC statute might shelter managers from this pressure and encourage them to make choices that ultimately are profit-maximizing.

The second is that the companies' status as a prosocial organization may garner goodwill from important constituencies, which the companies can translate into greater profits. Customers, employees, communities, suppliers, and prosocial investors may all grant favored treatment to PBCs because of their legal status, resulting in higher profits despite the associated costs of generating meaningful social good. We discuss both possibilities below.

The third reason PBCs may earn greater profits is less appetizing: PBCs may engage in purpose washing. By choosing the PBC as their legal form, companies may send a signal that they are behaving better than traditional corporations do, thereby securing favorable treatment from important constituencies in the ways just described. By posing as a prosocial corporation and gaining the associated benefits, but not bearing the costs of actually behaving in a prosocial manner, PBCs may earn greater profits.

a. Promote Long-Term, Profit-Maximizing Behavior

One way that PBCs might encourage long-run profit-maximizing behavior is by requiring boards and managers to focus on the well-being of the company's employees. Under Delaware law, boards must consider the impact of business decisions on those materially affected by the company's conduct, which would generally include employees.[40] Under the Model Act, boards are specifically required to consider the impact of their decisions on the company's employees.[41]

A substantial management literature argues that investing in employee well-being results in better long-term profitability outcomes.[42] For example, Jeffrey Pfeffer argues that there are seven employee-relations tactics that can improve profitability.[43] Of these, the most efficacious is

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[40] *See* Del. Gen. Corp. L. §362(a).

[41] *See* Model Act §301(a)(1).

[42] *See, e.g.,* Brian Becker & Mark Huselid, *High Performance Work Systems and Firm Performance*, 16 RESEARCH IN PERS. AND HUMAN RIGHTS MGMT 53, 54 (1998) ("[B]oth the theoretical and empirical work in this area is broadly consistent with the conclusion that there is a strong relationship between the quality of a firm's [human resource management] system and its subsequent financial performance."); Alex Edmans, Lucius Li, and Chendi Zhang, *Employee Satisfaction, Labor Market Flexibility, and Stock Returns Around the World* (Feb. 21, 2017), available at https://ssrn.com/abstract=2461003 (Employee satisfaction is associated with superior long-run returns and future profitability); Olubunmi Faleye & Emery A. Trahan, *Is What's Best for Employees Best for Shareholders?*, (May 2006), available at https://ssrn.com/abstract=888180 (devoting resources to employee welfare results in greater financial success).

[43] *See* JEFFREY PFEFFER, THE HUMAN EQUATION: BUILDING PROFITS BY PUTTING PEOPLE FIRST 64-98 (1998). Pfeffer marshals substantial evidence that this tendency is short-sighted and ultimately counterproductive. By preserving their freedom of

to provide employees with job security because job security tends to encourage employees to identify with their employer and therefore make more firm-specific investments.[44] Most large companies avoid granting job security to their employees in order to preserve the flexibility to downsize in the event of a need to reduce costs because of a decline in sales or other setback.[45]

Traditional corporations could grant employees job security, but Pfeffer identifies a number of factors which impede their ability to do so. These include a reluctance to defy conventional management wisdom; pressure on managers to achieve the short-term goals set by their superiors; focus on short-term costs rather than on returns on investments; lauding toughness as the core managerial virtue; managerial training's emphasis on finance rather than management skills; and shareholder primacy combined with the capital market's emphasis on short-term returns.[46]

Managers at PBCs may experience these pressures as well, but the enabling statutes set up countervailing forces. The requirement to

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action, companies erode employees' sense of security and belonging, reducing their willingness to make firm-specific investments and damaging morale. Providing employees with job security, in contrast, imbues a sense of belonging and communicates to employees that they are valuable and trusted. Employees then become more likely to identify with the firm and its success, inspiring them to work harder and develop skills and gain knowledge that will improve their performance and, by extension, that of the firm.

[44] *See id.* at 176-82. The other six factors are careful hiring, decentralized management, high compensation related to organizational performance, training, non-hierarchical workplace culture, and extensive financial transparency.

[45] *See* Sarah Gardner, *Wall Street Does Not Value Having Employees and That's Changing Everything About the US Workplace*, BUS. INSIDER (Jun. 25, 2016), https://www.businessinsider.com/companies-dont-like-having-full-time-employees-2016-6/ ("Job stability hasn't defined the American workplace for decades. Just ask anyone who has been escorted out by security in a mass layoff or whose factory moved offshore. In a global marketplace constantly upended by technology, companies are under unrelenting pressure to cut costs and maximize profits.").

[46] *See* PFEFFER, *supra* note 42, at 132.

consider the needs of employees and balance those needs against the demand for profits may encourage PBC managers to think more deeply about the merits of pro-employee policies such as granting some measure of job security.

We are not suggesting that all companies should grant tenure to all employees, nor are we even contending that greater employee job security will necessarily lead to greater profits. Scholars such as Pfeffer who argue for the utility of job security may be correct in their assertions, or they may not. Job security and other pro-employee policies may or may not produce greater profits.[47] We merely point out that investors in PBCs may believe – in line with many management theorists – that pro-employee policies will bolster profits in the long-run and may also believe that managers at PBCs will be more likely to adopt these policies because of their statutory obligation to weigh employee welfare when making business decisions. Investors that embrace these beliefs may be willing to invest in PBCs under the theory that businesses organized with these forms will be more profitable.

A second reason investors might believe that PBCs will encourage more profitable decisions over the long run is that these entities may focus more strongly on their customers' welfare. Customers are also a corporate constituency that PBCs are required to prioritize—they are

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[47] Some management scholars are skeptical of the connection between pro-employee policies and long-term profits. *See, e.g.,* Dr. John Sullivan, *A Dozen Good Reasons You Should be Cautious About Employee Happiness*, TLNT (Jan. 20, 2016) https://www.tlnt.com/a-dozen-good-reasons-you-should-be-cautious-about-employee-happiness/; Dr. John Sullivan, *More Reasons Why the Employee Happiness Doesn't Drive Productivity*, TLNT (Jan. 21, 2016) https://www.tlnt.com/more-reasons-why-the-employee-happiness-doesnt-drive-productivity/.

certainly among those "materially affected" by the corporation's conduct, so PBC boards must take their interests into account.[48]

There is good reason to suppose that a focus on customer welfare might boost corporate profits.[49] Happy customers recommend the product to their social circles and may become repeat customers; unhappy customers post negative reviews on social media and discourage their friends from buying. Of course, traditional corporations might well be expected to focus on customers as well, without the further prompting of the PBC statute, but there are ample examples of traditional companies that have lost sight of this principle, often with disastrous results for both the corporation and its customers.[50]

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[48] *See* Del. Gen. Corp. L. §§ 362(a). BCs must also do so, at least to the extent that customers are beneficiaries of the general public benefit or a specific public benefit of the BC, which should often be the case. *See* Model Act § 301(a)(1)(iii).

[49] *See* Amy Gallo, *The Value of Keeping the Right Customers*, HARVARD BUS. REV. (Oct. 29, 2014), https://hbr.org/2014/10/the-value-of-keeping-the-right-customers (citing Fred Reichheld, *Prescription for Cutting Costs*, BAIN & COMPANY, http://www2.bain.com/Images/BB_Prescription_cutting_costs.pdf).

[50] Some prominent examples include: Guidant's sale of a defectively-designed defibrillator even after discovering the defect; A.H. Robins' sale of the Dalkin Shield after discovering that it was causing severe infections and even deaths in users; Firestone's knowing sale of defective tires, causing scores of deaths; and Ford Motor's marketing the Pinto while knowing of a dangerous defect that could set the car on fire in a rear-end collision. *See See* Ashley M. Heher, *Guidant Recalls Heart Devices, Associated Press,* WASHINGTON POST (June 18, 2005), http://www.washingtonpost.com/wp-dyn/content/article/2005/06/17/AR2005061700680.html; *See* Robin Marantz Henig, *The Dalkon Shield Disaster*, WASHINGTON POST (Nov. 17, 1985), https://www.washingtonpost.com/archive/entertainment/books/1985/11/17/the-dalkon-shield-disaster/6c58f354-fa50-46e5-877a-10d96e1de610/; Ricardo Alonso-Zaldivar and Robert L. Jackson, *Firestone CEO Apologizes for Tire Failures*, L.A. TIMES (Sep. 7, 2000), https://www.latimes.com/archives/la-xpm-2000-sep-07-mn-16935-story.html; and Ben Wojdyla, *The Top Automotive Engineering Failures: The Ford Pinto Fuel Tanks*, POPULAR MECHANICS (May 20, 2011), https://www.popularmechanics.com/cars/a6700/top-automotive-engineering-failures-ford-pinto-fuel-tanks/.

A third, related reason investors might believe PBCs promote profit-maximizing behavior better than do traditional corporations, is that these entities might prove less likely to violate the law. Violating the law may often benefit a corporation, at least for a time. A business may reduce its costs by, for example, neglecting to provide safe working conditions in violation of the Occupational Safety and Health Act.[51] When this violation is eventually detected, however, the company may face severe financial penalties.[52] Similarly, a company may boost sales and profits by lying about the quality of its products, in violation of the federal truth-in-advertising statutory requirement.[53] If the company's falsehood is detected, however, the Federal Trade Commission and the state attorneys general in states with affected consumers may impose penalties, and the company may be liable for common law fraud.[54] Investors might rationally prefer that companies obey the law to reduce the risk of the penalties the companies may suffer if the government detects and punishes a violation.

All companies are equally subject to the law, whether organized as a traditional corporation or as a PBC. But PBC boards must consider all those affected by corporate activity when making decisions.[55] PBCs are therefore under a particular duty to avoid violating laws which

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[51] *See* 29 U.S.C.A. 15 *et seq.*

[52] *See* 29 U.S.C.A. §666(a) (providing for civil penalties of up to $70,000 for each willful or repeated violation).

[53] *See,* 15 U.S.C.A. §52(a) ("It shall be unlawful for any person, partnership, or corporation to disseminate, or cause to be disseminated, any false advertisement – (1) By United States mails, or in or having an effect on commerce, by any means, for the purpose of inducing, or which is likely to induce, directly or indirectly the purchase of food, drugs, devices, services, or cosmetics; or (2) By any means, for the purpose of inducing, or which is likely to induce, directly or indirectly, the purchase in or having an effect upon commerce, of food, drugs, devices, services, or cosmetics.").

[54] *See* 15 U.S.C.A. § 54 (imposition of penalties by the FTC for false advertising); Cal. Bus. & Prof. Code § 17500 (imposing penalties for false advertising); New York Gen. Bus. L. §§ 350, 350-d (banning false advertising and providing for civil penalties).

[55] *See* Del. Gen. Corp. L. §§ 362(a).

would materially and deleteriously impact others such as employees (in the case of OSHA) and consumers (in the case of truth-in-advertising statutes).[56] They too, then, are under a particular duty to avoid violating laws that might harm others.

These requirements for PBCs may foster a corporate culture of compliance, rather than one that sees legal restrictions as an impediment to the core value of profit maximization, especially when the legal rule in question is designed to protect health or safety. While this issue has yet to be studied empirically, PBCs may therefore be less likely to violate the law willfully, making them a lower risk investment than traditional corporations. Investors who believe this to be true may be willing to invest despite the countervailing risk that a PBC will sometimes sacrifice profit for other social interests.

Fourth and finally, investors might think PBCs will be more profitable than traditional corporations because they may have less exposure to future environmental regulation. PBCs' duty to consider all those materially affected by corporate actions should be read to require them to consider the impact on the environment, just as BCs are expressly required to weigh the impact of their actions on the local and global environment before making any corporate decision.[57] These requirements may inspire PBC boards to reach beyond legal requirements that govern their interactions with the environment. Instead of barebones compliance, PBCs may structure their business models to minimize their environmental impact or even strive to repair the damage done by others. For example, Thread International PBC,

[56] Similarly, BC boards must consider the impact of the company's actions on the general good and on society. *See* Model Act § 301(a)(1).
[57] *See* Del. Gen. Corp. L. §§ 362(a); Model Act §301(a)(1)(v).

Inc. gathers used plastic bottles from Haiti and transforms them into cloth that it sells to apparel companies.[58]

Traditional companies must obey environmental laws, but they may have less incentive to go beyond mere compliance. Environmental laws may become more stringent over time, if the damage from climate change mounts and voters put pressure on regulators to ameliorate the damage caused by rising temperatures. Unlike environmentally focused PBCs, companies that only meet the standards of existing regulations will bear increasing compliance costs in the future.[59] Investors who believe this may perceive that PBCs present lower environmental compliance risks than traditional corporations, thus offsetting to some degree the risk that PBC boards will sacrifice profit for the benefit of other corporate constituencies.

We emphasize that all four of these strategies to increase long-term profits – treating employees well, focusing on customers' welfare, complying with legal regulations, and adopting strong environmental policies – are available to traditional corporations as well as to PBCs. But there are reasons investors may believe that PBCs may pursue some or all of these strategies more consistently or aggressively than traditional corporations. Investors who hold these beliefs may be

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[58] *See* Adele Peters, *Timberland's New Line is Made From Trash Collected From the Streets in Haiti*, FASTCOMPANY (Mar. 10, 2017), https://www.fastcompany.com/3068876/timberlands-new-line-is-made-from-trash-collected-from-the-streets-in-haiti.

[59] In contrast, companies like Thread whose environmentalism is baked into their business model are likely to thrive in a stricter regulatory environment. Their environmentalism will provide a strategic advantage as they compete with traditional suppliers. Even PBCs whose business models are less directly connected to environmentalism will likely adopt policies that exceed current regulatory requirements, putting them far ahead of their conventional competitors as regulations tighten. For example, Allbirds, Inc., a PBC, not only manufactures its shoes out of wool, a renewable material, but it also packages its shoes with 90% post-consumer recycled cardboard.

willing to invest in PBCs despite the attendant risk that PBCs may sometimes sacrifice profit in favor of pursuing other values.

b. Garner Goodwill that Translates to Profits

In the last section, we discussed the possibility that investors might believe that PBCs could be more profitable than traditional corporations because the statutory requirements may encourage managerial behavior that is profit-maximizing over the long term. In this section, we advance the possibility that, by adopting the PBC form of business organization, companies may gain material advantage due to the perception by various corporate constituencies that the companies are conferring benefits to the world.

These constituencies may perceive the PBC as special and provide favored treatment that ultimately leads to greater profitability. There are five groups that might provide such benefits to PBCs: customers, employees, communities, suppliers, and prosocial investors. For-profit investors who believe that a company's PBC status will confer a material advantage might choose to invest despite the risk that these forms may sometimes sacrifice profit for other values, so long as they believe that on net, the advantage will translate to higher profitability.

Consumers increasingly want the companies that make their products not only to provide excellent merchandise but also to demonstrate that they function as responsible citizens. A 2014 Nielsen study reported that over half of global online shoppers would willingly pay a premium for items furnished by producers committed to positive social and environmental policies.[60] Many companies advertise their brand as

[60] *See* Nielsen, *Global Consumers Are Willing to Put Their Money Where Their Heart Is When It Comes to Goods and Services from Companies Committed to Social Responsibility* (Jun. 17, 2014), available at https://www.nielsen.com/us/en/insights/reports/2015/the-sustainability-imperative.html; *see also* Mehdi Miremadi, Christopher Musso, and Ulrich Weihe, *How Much Will Consumers Pay to Go Green?*, MCKINSEY QUARTERLY (Oct. 2012),

being prosocial in an effort to encourage consumers to feel good about buying their products, even if those products are more expensive than competing items of comparable quality.

For example, Patagonia, a BC that sells outdoor clothing and gear, markets its strong commitment to environmentalism and its generous treatment of its workers.[61] State Bags, a PBC that sells backpacks, advertises that it gives away backpacks full of school supplies to those in need.[62] If consumers are willing to choose one product over another because of the manufacturer's prosocial policies, or even pay a premium for a product that appears more prosocial, then a company's PBC status might enhance that marketing message and drive profits.

Just as consumers want to inject meaning into their purchases, employees now often prefer to suffuse their work with purpose. Millennials are particularly likely to desire work to have some meaning over and above an earned wage. In a recent international survey, some 87% of millennials said they thought that financial performance should not be the only measure of a company's success.[63] And in recent interviews of founders of PBCs, half of respondents indicated that their company's prosocial mission made it easier to attract and retain employees.[64] Even the Delaware government, in a press release announcing the governor's signing of the public benefit

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https://www.mckinsey.com/business-functions/sustainability/our-insights/how-much-will-consumers-pay-to-go-green (as many as 70% of consumers would pay 5% more for green products of similar quality).

[61] *See* Patagonia, *Corporate Responsibility*, http://www.patagonia.com/us/patagonia.go?assetid=67372.

[62] *See* State Bags, *How We #Givebackpack*, https://www.statebags.com/pages/give-back-pack.

[63] *See* Deloitte, *The 2016 Deloitte Millennial Survey,* available at http://www2.deloitte.com/content/dam/Deloitte/global/Documents/About-Deloitte/gx-millenial-survey-2016-exec-summary.pdf.

[64] *See* Michael B. Dorff, *Why Public Benefit Corporations?*, 42 DEL. J. CORP. L. 77, 93 (2017). A similar percentage stated they had an easier time attracting customers. *Id.*

corporation statute, stated that the PBC would help companies "attract talent."[65]

Companies may rise or fall based on the talent and dedication of their employees.[66] Also, searching for and training new hires can be a major expense, so companies' retention rates can be a major factor in their profitability.[67] If PBC status can help attract talented workers, inspire them to work harder, and encourage them to remain with the company for a longer period, then it may improve the business' bottom line.

Adopting a PBC status could help companies attract lucrative incentive packages from cities and states by making companies' promises to produce concrete, long-term benefits more credible. The city of San Francisco provides early evidence of this possibility. San Francisco now grants an advantage to BCs bidding for city contracts equivalent to a 4% discount on the bid price.[68] Investors who believe that communities will provide material financial benefits to PBCs might

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[65] Press Release, Delaware Office of the Governor, Governor Markell Signs Public Benefit Corporation Legislation (Jul. 17, 2013), http://news.delaware.gov/2013/07/17/governor-markell-signs-public-benefit-corporation-legislation.

[66] *See* Charles Fishman, *The War for Talent*, FAST COMPANY (Jul. 31, 1998), https://www.fastcompany.com/34512/war-talent ("According to a yearlong study conducted by a team from McKinsey & Co. – a study involving 77 companies and almost 6,000 managers and executives – the most important corporate resource over the next 20 years will be talent: smart, sophisticated businesspeople who are technologically literate, globally astute, and operationally agile."); Susan Sorenson, *How Employee Engagement Drives Growth*, GALLUP (Jun. 20, 2013), https://www.gallup.com/workplace/236927/employee-engagement-drives-growth.aspx ("Given the timing of the eighth iteration of this study, it also confirmed that employee engagement continues to be an important predictor of company performance even in a tough economy.").

[67] *See* Theresa Agovino, *To Have and to Hold*, SHRM (Feb. 23, 2019), https://www.shrm.org/hr-today/news/all-things-work/pages/to-have-and-to-hold.aspx ("Each employee departure costs about one-third of that worker's annual earnings, including expenses such as recruiter fees, temporary replacement workers and lost productivity, according to the Work Institute.").

[68] *See* 14C San Francisco Administrative Code §14C.3.

decide that this advantage outweighs any competing concerns about these business entity types.

Suppliers might privilege PBCs as customers to the extent they perceive PBCs as more likely to behave honorably in their dealings and to comply with their contractual agreements. The legal remedies for breach of contract routinely fail to provide a complete remedy to the aggrieved party, particularly in their traditional failure to offer compensation for attorneys' fees and the time and inconvenience involved in suing.[69] If suppliers believe that PBCs will be more likely to comply with their contractual promises, they might prefer to deal with those entities and even offer them more favorable terms in exchange for a perceived reduction of the risk of breach.

Nothing in the PBC statute expressly forbids breach of contract, but the statute does require PBCs to take into account the impact of their decisions on all those materially affected by them. This rule should certainly include their contracting partners. Also, some suppliers might believe that founders who opt for the PBC form – and the employees who choose to work for them – might also have greater personal integrity (or at least want to be perceived that way). In addition, suppliers who are themselves PBCs might feel a sense of commonality with customers who share their entity status and therefore offer them better terms. B Lab has encouraged the companies it certifies to connect with one another in the "B Hive" in order to network and

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[69] *See Burnside v. State Farm Fire and Cas. Co.*, 528 N.W.2d 749, 751 (Mich. Ct. App. 1995) ("Under the American rule, attorney fees are generally not allowed, as either costs or damages, unless recovery is expressly authorized by statute, court rule, or a recognized exception."); Melvin A. Eisenberg, *Actual and Virtual Specific Performance, The Theory of Efficient Breach, and the Indifference Principle in Contract Law*, 93 CALIF. L. REV. 975, 995 (2005) (arguing that contract damages are insufficient to make the victim of a breach indifferent between performance and damages because, *inter alia*, damages do not include the costs involved in obtaining a remedy from the court, including the value of the victim's time and other costs of litigation and the time value of the expected gains from the contract's performance).

obtain discounts on products and services.[70] The separate but overlapping PBC community might do likewise, even if less formally.

Finally, for reasons we discuss below, prosocial investors might prefer to deal with PBCs rather than traditional corporations that claim to have adopted a social mission.[71] To the extent this is true, for-profit investors might also prefer to invest in PBCs. Any subsidy the prosocial investors provide in the form of more favorable investment terms will redound in part to the benefit of the for-profit investors who demand (better) market terms. For-profit investors who believe that PBCs will be able to persuade prosocial investors to provide capital at a lower cost might themselves therefore see a profit advantage in investing in those forms.

In this section, we have discussed the pecuniary advantages PBCs might accrue through the goodwill potentially associated with their social missions. It is important to note that a social mission is not the exclusive province of PBCs. To the contrary, many traditional corporations state that they have a social mission and can gain the benefits we have discussed above.[72] If PBCs are gaining an advantage due to the goodwill associated with their legal status, it must be because the legal status somehow makes their social mission claims

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[70] *See* B Lab, *Join the Community of B Corps on the B Hive*, https://bcorporation.net/for-b-corps.

[71] *See infra,* notes 101-105 and associated text.

[72] *See* Mark Sullivan, *Google Is Searching for a Way to Be Zero Emissions All the Time*, FAST COMPANY (Oct. 17, 2018), https://www.fastcompany.com/90251085/google-aims-for-100-percent-renewable-energy-all-day-every-day ("With its sizeable purchase of renewables, Google says it's currently matching all of its total energy use with clean energy sources.");Vicki Valet, *The World's Most Reputable Companies for Corporate Responsibility 2018*, Forbes (Oct. 11, 2018), https://www.forbes.com/sites/vickyvalet/2018/10/11/the-worlds-most-reputable-companies-for-corporate-responsibility-2018/ (Lego announced plans to manufacture its blocks from plants); Sarah Witten, *Starbucks to Create 240,000 Jobs by 2021*, CNBC (Mar. 22, 2017), https://www.cnbc.com/2017/03/22/starbucks-to-create-240000-jobs-by-2021.html (Starbucks hired 10,000 veterans and military spouses).

more credible, elevating them above mere "cheap talk" that all companies are free to engage in. The legal form *per se* seems unlikely to generate much enthusiasm from external constituencies apart from the behavior the status is supposed to promote.

In the next section, we analyze the strength of the legal tools the PBC statute provides to ensure that these entities are producing tangible social goods in a way that is meaningfully distinct from a traditional corporation. That discussion stems from a third reason why for-profit investors might seek out companies organized as PBCs: purpose washing.

c. Purpose Washing

A less hopeful rationale why profit-seeking investors might be willing to invest in PBCs is that investors may believe that these forms will behave identically to traditional corporations. If PBCs will not divert resources towards producing positive externalities but will instead focus exclusively on maximizing profits for shareholders, then there is no reason for investors to shy away from investing in these entities. In fact, if these entities succeed in persuading some external constituencies that they are better for them than traditional corporations along the lines discussed above, without bearing the costs of actually being better for these groups ("purpose washing"), investors might prefer PBCs to traditional corporations.

Oil producers, for example, are often seen to be harmful to the environment. The processes of extraction and transportation generate significant negative externalities and carry the risk of spills and other environmental disasters.[73] However, an oil company that can market

[73] *See* Stephen Leahy, *Exxon Valdez Changed the Oil Industry Forever—But New Threats Emerge*, NAT. GEO. (Mar. 22, 2019), https://www.nationalgeographic.com/environment/2019/03/oil-spills-30-years-after-exxon-valdez/; Christine Mai-Duc, *The 1969 Santa Barbara Oil Spill That Changed Oil and Gas Exploration Forever*, L.A. TIMES (May 20, 2015),

itself as environmentally conscious might be able to claim market share from its competitors, as consumers who are concerned about global warming or the impact of off-shore drilling on ocean life seek to support apparently "green" companies. Unsurprisingly, many major oil companies do indeed attempt to market themselves as pro-environment.[74] This type of "green washing" may allow companies to enjoy some of the pecuniary advantages of an environmentally friendly brand reputation, without actually modifying their core damaging behavior.

While at first blush, investors seem unlikely to perceive PBCs as an opportunity for purpose washing – the point of these entities is, after all, to ensure they balance the quest for profits against other social concerns – a careful analysis of the legal requirements might support this view. There are two legal mechanisms PBCs use to enforce the requirement that boards balance profit against other goals: litigation and disclosure. Investors could reasonably believe that neither of these mechanisms – nor the combination of the two – will meaningfully constrain a board that is not sincerely dedicated to pursuing goals other than profits.

The litigation remedy is severely limited in terms of who has standing to sue,[75] and even if a claim is launched successfully, the plaintiffs will

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https://www.latimes.com/local/lanow/la-me-ln-santa-barbara-oil-spill-1969-20150520-htmlstory.html.

[74] *See, e.g.,* ExxonMobil, *Environmental Initiatives*, https://corporate.exxonmobil.com/energy-and-environment/environmental-protection/environmental-initiatives (last viewed Jul. 23, 2019); Chevron, *Environment*, https://www.chevron.com/corporate-responsibility/environment (last viewed Jul. 23, 2019).

[75] The Model Act provides that claims based on a BC's failure to pursue or create a general public benefit (or any adopted specific public benefit), as well as claims rooted in the violation of any other obligation, duty, or standard of conduct under the Model Act, can only be brought in a "benefit enforcement proceeding." Only the BC itself and shareholders who own sufficient stock (at least 2% of a class of shares of the BC or at least 5% of the equity of a BC's parent company) may bring a benefit enforcement proceeding either directly (by the BC) or derivatively (by shareholders).

generally find it very difficult to win a judgment against directors in court due to the difficulty of the substantive standard of liability. In traditional corporations, directors' liability for violating their duty of care by making a poor business decision is determined by the highly deferential business judgment rule.[76] The Delaware Supreme Court has described this rule as "'a presumption that in making a business decision, the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company.'"[77] Directors who acted in good faith and without self-interest are liable under the rule only if they were grossly negligent in informing themselves before making the decision, or if their decision was irrational or constituted corporate waste.[78]

The Delaware PBC statute applies the business judgment rule to balancing decisions made by a PBC board. PBC directors who inform themselves and are not interested in a decision will not bear personal liability for any improper balancing of the profit goal against the interests of others affected by corporate activity and the public benefit

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The intended beneficiaries of the general public benefit – or any specific public benefit – cannot launch a benefit enforcement proceeding.
Similarly, under Delaware law, only shareholders who own at least 2% of a PBC's outstanding shares, either individually or as a group, may bring a derivative action to enforce the board's obligation to balance the pursuit of profits against the best interests of other corporate constituencies and the public benefits (general or specific) the PBC must pursue. The directors have no duty to any beneficiary of the public benefits the PBC is required to provide.

[76] *See Smith v. Van Gorkom,* 488 A.2d 858 (Del. 1985).

[77] *Id.* at 872 (quoting *Aronson v. Lewis,* 473 A.2d 805, 812 (Del. 1984)).

[78] *See id.* at 873 ("We think the concept of gross negligence is also the proper standard for determining whether a business judgment reached by a board of directors was an informed one."); *Saxe v. Brady*, 184 A.2d 602, 610 (Del. 1962) (defining waste as "whether what the corporation has received is so inadequate in value that no person of ordinary, sound business judgment would deem it worth what the corporation had paid."); *Calma on Behalf of Citrix Systems, Inc. v. Templeton*, 114 A.3d 563, 590 (Del. Ch. Ct. 2015) ("Under Delaware law, directors waste corporate assets when they approve a decision that cannot be attributed to 'any rational business purpose.'") (quoting *Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 720 (1971)).

the PBC must provide.[79] The only limitation on this protection is for decisions that "no person of ordinary, sound judgment would approve." It is very rare for courts to find a violation of the business judgment rule in the absence of a self-interested or bad faith decision.[80]

Plaintiffs who manage to overcome both the limitations on standing and the rigorous standard for liability, may still find themselves dissatisfied with the resulting remedy. Delaware law permits its PBCs to eliminate their directors' liability for breach of the duty of care in the absence of bad faith or a breach of the duty of loyalty.[81]

In sum then, as long as the shareholders remain aligned in their view of the proper balance between profit and other goals, there is little threat of litigation over the boards' balancing decisions. The primary expected source of complaints – non-shareholder constituents complaining of overly profit-centered decisions by the board – are barred from suit.[82] Even if a shareholder disagrees with the board's decision and chooses to sue, the shareholders must overcome a very challenging substantive liability rule. Then, if the shareholders surmount the protections of the business judgment rule, the directors

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[79] *See* 8 Del. Gen. Corp. L. §365(b) ("[W]ith respect to a decision implicating the balance requirement in subsection (a) of this section, will be deemed to satisfy such director's fiduciary duties to stockholders and the corporation if such director's decision is both informed and disinterested and not such that no person of ordinary, sound judgment would approve.").

[80] *See Steiner v. Meyerson*, Civ. A. No. 13139, 1995 WL 441999, at *5 (Del. Ch. July 19, 1995) ("Absent an allegation of fraud or conflict of interest courts will not review the substance of corporate contracts; the waste theory represents a theoretical exception to the statement very rarely encountered in the world of real transactions. There surely are cases of fraud; of unfair self-dealing and, much more rarely negligence. But rarest of all-and indeed, like Nessie, possibly non-existent-would be the case of disinterested business people making non-fraudulent deals (non-negligently) that meet the legal standard of waste!").

[81] *See* 8 Del. Gen. Corp. L. §§ 365(c), 102(b)(7). The Model Act goes further for BCs, rendering BC directors immune from financial liability for any failure to create a general or specific benefit. *See* Model Act §301(c).

[82] *See* Model Act § 301(d); 8 Del. Gen. Corp. L. § 367.

may be protected from liability for breaching the duty of care in PBCs that elect to do so.[83]

The statutes also seek to enforce the balancing requirement through disclosure. Delaware law requires PBCs to provide their shareholders with a statement at least biennially regarding the company's furthering the public benefit(s) listed in the certificate of incorporation and the best interests of those affected by corporate activities.[84]. Mandating disclosure – at least to shareholders – of companies' degree of success in promoting the public benefit and the welfare of other corporate constituencies might have the effect of increasing the pressure on PBC directors to sacrifice profit in favor of these other interests. Disclosure of poor efforts to create a social benefit, or of corporate behavior that negatively impacts workers or the environment, might motivate shareholders to vote for different directors and, to the extent the public receives the disclosure, lessen any halo effect the company's legal status might generate.[85]

Investors might reasonably believe, though, that this disclosure obligation will not have this effect, and PBCs will remain free to focus their efforts on profits alone regardless of the disclosure obligation. Despite the legal mandate, many PBCs have not been creating benefit reports or statements for their shareholders or the public.[86] Secretaries of state have not been enforcing even the requirement to create a

[83] *See* Model Act § 305(b); 8 Del. Gen. Corp. L. § 365(b).

[84] *See* 8 Del. Gen. Corp. L. §366(b). The Model Act requires the company to prepare a "benefit report" every year which must include, inter alia, a narrative description of the general public benefit (and any specific public benefit) the company generated that year and an assessment of the firm's overall environmental and social performance, measured against a third-party standard. *See* Model Act §401(a).

[85] *See supra,* notes 39-59 (discussing possible pecuniary benefits of PBC status).

[86] *See* J. Haskell Murray, *An Early Report on Benefit Reports*, 118 W. VA. L. REV. 25, 34 (2015-16) (finding only 8% of BCs in a hand-collected data sample had produced a benefit report).

report, and certainly have not been policing the reports' quality.[87] As a result, PBCs that want to circumvent or avoid this requirement seem free to do so. Investors might therefore reasonably believe that the disclosure requirement will not impede PBCs' ability to focus solely on profit should their boards so choose.[88]

2. Scarcity of High-Potential Investments

So far, we have discussed reasons why profit-seeking investors might believe PBCs will be more profitable than traditional corporations and therefore might choose to buy equity in PBCs. These reasons include (1) that PBCs' legal characteristics might encourage profitable business strategies, (2) that PBCs' more credible claim to prosocial behavior might attract favorable treatment from important constituencies, and (3) that PBCs might engage in purpose washing. In this section we will discuss an alternative possibility for why profit-seeking investors might prove willing to buy equity in PBCs: the scarcity of high-potential investments.

There is evidence that there is now more venture capital chasing the available investment opportunities, without a corresponding growth in high-quality startups. In 1995, total VC investment in the U.S. was $8.1 billion; in 2018 it was nearly $100 billion.[89] VC investment in the U.S. during the late 1990s averaged $28.8 billion a year; from 2014-2018 it averaged $75.66 billion.[90] Other than the massive outlier year

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[87] *See id.* at 44 ("None of the four state benefit corporation statutes relevant to this Article's data require filing of the benefit report with the state or provided express penalties for non-compliance.").
[88] The Model Act provides a third method of policing against purpose washing by permitting BCs to appoint a benefit director and/or a benefit officer. *See* Model Act §302(a).
[89] *See* Statista, *Value of Venture Capital Investment in the United States from 1995-2018*, https://www.statista.com/statistics/277501/venture-capital-amount-invested-in-the-united-states-since-1995/.
[90] *See id.*

of 2000, after which VC investment in the U.S. collapsed for a time, 2018 was the largest year on record.[91]

There is also evidence from average investment returns that the number of high-quality issuers has not grown in proportion. In venture capital's heyday in the second half of the 1990s, average venture returns were over 88%/year, but in in the five years ending in 2017, they have declined to 14.9%.[92]

Venture capital firms' investment returns are driven by a relatively few "hits" to make up for the many companies that achieve only low growth or fail altogether.[93] The key challenge for VC firms, then, is to find one or two companies that will experience truly explosive growth. In a universe with excess capital chasing relatively few prime investment targets, a company with good prospects of achieving explosive growth might be attractive to investors even if some portion of its profits will be diverted away from the company's business needs.

Profit-seeking VCs might prove willing to overlook the company's suboptimal legal structure (from a purely profit-seeking perspective) when the company's core business model, management team, and/or intellectual property portfolio are otherwise sufficiently appealing. In other words, VCs might concede to founders' desires to organize as a PBC even though the form is suboptimal in much the same way as they accept less equity or fewer governance protections. In all these

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[91] *See id.*

[92] *See* Cambridge Associates, *US Venture Capital Index Selected Benchmark Statistics* at 11 (Dec. 31, 2017), https://www.cambridgeassociates.com/wp-content/uploads/2018/05/WEB-2017-Q4-USVC-Benchmark-Book.pdf (providing annual average return data for U.S. VCs).

[93] *See* John H. Cochrane, *The Risk and Return of Venture Capital*, 75 J. FIN. ECON. 3, 5 (2005) (large average returns from venture capital stem from small chance of very large payoff); Deborah Gage, *The Venture Capital Secret: 3 Out of 4 Start-Ups Fail*, WALL STREET J. (Sept. 20, 2012), https://www.wsj.com/articles/SB10000872396390443720204578004980476429190.

cases, while investors might prefer an alternative arrangement, the investment as a whole seems to promise rich returns.

Helpful to this line of thinking, some PBCs may manage to generate social benefit without incurring impactful costs. There are at least two ways a business could do this. We have already discussed the first possibility – if important corporate constituencies such as customers or employees are willing to sacrifice some degree of their own interests to promote the social good the company provides, the cost of providing social goods may be offset to a degree by other pecuniary gains (and the prosocial form may even provide a net gain in profitability).[94]

The other possibility is that providing social goods may sometimes be cheap when compared to the company's profit margin. For example, some companies donate a certain percentage of their employees' time to various charities. The percentage may be rather small yet still have a meaningful impact on the charity, especially if the company has a large workforce or can provide the charity with particularly valuable services. Yet if the company's expectations for the work its employees must complete do not diminish, the net effect may be that the employees work more productively to achieve the same or similar results in somewhat less time.

Another example of a potentially cheap social good occurs with companies that adopt a "buy-one-give-one" policy. Warby Parker – which is not a PBC[95] – donates one pair of eyeglasses for every pair it sells.[96] This policy is much cheaper than first appears, however,

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[94] *See supra,* notes 60-71.

[95] State of Delaware Department of State – Division of Corporations, *Entity Details for Warby Parker Retail, Inc.*, https://icis.corp.delaware.gov/Ecorp/EntitySearch/NameSearch.aspx.

[96] *See* Warby Parker, *Buy a Pair, Give a Pair*, https://www.warbyparker.com/buy-a-pair-give-a-pair ("[W]e work with a handful of partners worldwide to ensure that for every pair of Warby Parker glasses purchased, a pair of glasses is distributed to someone in need.").

because the glasses the company donates are not the same type as those it sells. To the contrary, the company describes the glasses it donates as "radically affordable."[97]

Companies may also provide social goods by granting employee benefits such as generous parental leave policies. Such policies may boost employee morale significantly without imposing a prohibitive cost.[98] Or companies may declare themselves to be carbon neutral by buying carbon offsets from providers who plant trees. Such offsets are, like the examples above, relatively cheap.[99]

The relative scarcity of high-quality investment opportunities may therefore lead VCs to invest in PBCs despite the risk that resources will be diverted away from profit generation to the provision of social benefits, especially if the social benefits can often be provided fairly inexpensively.

C. Prosocial Investors

Prosocial investors are those willing to accept a reduction of return for investments that create societal good. Note that this category excludes

[97] *See id.* ("We've supported [VisionSpring's] social entrepreneurship model internationally, which makes it possible for low-income men and women to acquire and sell radically affordable eyeglasses, earn a living, and care for their families.").

[98] *See* Trish Stroman, Wendy Woods, Gabrielle Fitzgerald, Shalini Unnikrishnan, and Liz Bird, *Why Paid Family Leave Is Good Business*, Boston Consulting Group Henderson Institute (Feb. 7, 2017), https://www.bcg.com/publications/2017/human-resources-people-organization-why-paid-family-leave-is-good-business.aspx ("In EY's study . . . 92% of companies with a paid family leave policy reported that it had a positive effect or no effect on profitability. At the same time, the retention benefits of paid family leave can offset its costs. Those costs vary widely by industry, but a 2012 review found that replacing an employee typically costs around 21% of his or her salary.")

[99] *See* Kelley Hamrick & Allie Goldstein, *Raising Ambition: State of the Voluntary Carbon Markets 2016* (May 2016), https://www.forest-trends.org/wp-content/uploads/imported/2016sovcm-report_10-pdf.pdf (reporting the volume-weighted average price for carbon offsets was $3.30/ton in 2015, though there was considerable variability).

those investors who adopt the strategy of investing in high ESG companies as a means of increasing returns or reducing risks. (Though such profit-seeking investors might profitably focus their investment search on PBCs if they believe PBCs are more likely to also have high ESG scores.) Prosocial investors sacrifice some degree of return for the sake of other social benefits; the social benefits are ends in themselves, not merely a means to increase financial returns. While estimates of the amount of capital available to prosocial investors vary, it seems quite substantial, on the order of hundreds of billions of dollars and perhaps even trillions.[100]

Prosocial investors might prefer PBC investment targets if the PBC status makes companies' prosocial claims more credible. And there are some reasons prosocial investors might believe the PBC statute could help promote prosocial behavior by PBCs. The Delaware PBC statute imposes a balancing requirement on the board of directors, making balancing part of the directors' fiduciary duties.[101]

Also, the statute imposes a disclosure requirement regarding the extent to which the corporation has successfully promoted social good. Delaware law requires PBCs to provide their shareholders with a statement at least biennially regarding the company's furthering the public benefit(s) listed in the certificate of incorporation and the best

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[100] *See* Abhilash Mudaliar & Hannah Dithrich, *Sizing the Impact Investment Market* (April 2019), https://thegiin.org/assets/Sizing%20the%20Impact%20Investing%20Market_webfile.pdf (finding that there were over 1,300 investment organizations managing $502 billion in impact investment capital in 2018); US SIF The Forum for Sustainable and Responsible Investment, *Sustainable Investing Assets Reach $12 Trillion as Reported by the US SIF Foundation's Biennial Report on US Sustainable, Responsible and Impact Investing Trends* (Oct. 31, 2018), https://www.ussif.org/files/US%20SIF%20Trends%20Report%202018%20Release.pdf (reporting that sustainable, responsible, and impact investing assets account for $12 trillion in assets under management in the U.S. alone).

[101] *See supra* notes 22, 32 and associated text.

interests of those affected by corporate activities.[102] Prosocial investors therefore should have access to periodic information about the extent to which PBCs are creating social good, and knowing that they must disclose this information may induce boards to ensure that they can credibly claim to be doing so.

As discussed above, however, these provisions might be inadequate to ensure that companies are not simply purpose washing. Boards that wish to ignore their duty to balance the pursuit of profit with other concerns such as the welfare of their employees and the environment may do so with little risk of financial liability.[103] And secretaries of state have so far shown little inclination to enforce the social benefit disclosure requirements.[104] So while prosocial investors might be attracted to the new forms' statutory provisions to enhance the likelihood that PBCs will provide meaningful social benefits, they might also prove skeptical that the statutes provide material protection to the companies' prosocial goals.

D. Conclusion

In this section, we explored the reasons why either purely profit-seeking or prosocial investors might prove willing to invest in companies that have organized themselves as PBCs. We have also discussed why investors might be reluctant to invest in these new forms. In order to understand how investors' behavior matches up with these theoretical models, we gathered data on investment in PBCs and similar forms. In the next section, we will explain where we found this data and what it shows about investor interest in prosocial business forms to date.

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[102] *See* 8 Del. Gen. Corp. L. §366(b).
[103] *See supra* notes 82-84.
[104] *See supra* note 88.

II. HYPOTHESES & EMPIRICAL FINDINGS

A. Hypotheses

The debate over whether and how for-profit investors will participate in PBCs naturally leads to a set of testable hypotheses. The first hypothesis involves investment itself.

- ***Hypothesis 1A****: VC funds will invest significant amounts in PBCs, but at a lower volume than other investments.*
- ***Hypothesis 1B****: VC funds of all types (for profit, pro-social, etc.) will make these investments.*

We suspect that venture capital funds will invest in PBCs. They will do so because they believe that they will achieve a sufficient return to justify this investment. More particularly, we believe that PBC founders' profit motive will be aligned with their purpose motive in many circumstances, which alleviates any potential conflict between the two goals. Nonetheless, we hypothesize that this investment will be at a lower volume than other investments due to the novelty and limited number of issuing companies that have selected this new corporate form. The lower volume of investment may also be attributable to other factors which we explore in our next hypotheses.

We also hypothesize that all types of VC funds will invest in PBCs. Participation by a broad array of VCs – and not just prosocial investors – in PBCs would implicitly support the theory that a sufficient return is expected to be realized from these forms. Top-tier VC funds have a wider selection of investments than do prosocial funds.

VC support of PBCs could mean that the hypothesis that there is a paucity of high-quality early-stage investment opportunities is correct. Their support could also mean that these investments are not, in fact, inferior to investments in traditional corporations because of PBCs ability to garner profits from their prosocial status (for any or all of the reasons outlined in Part I), offsetting either partly or entirely the cost of their prosocial behavior. These hypotheses do not conflict, precisely, though the investment scarcity hypothesis does imply that VCs are driven to PBCs despite their allegedly inferior legal structure. The profit-from-doing-good hypothesis suggests that VCs should actively seek out PBCs because of their superior legal structure. Nevertheless, it is possible both that high-quality investments are relatively scarce and that PBCs may earn superior profits from their status, at least in some industries.

- ***Hypothesis 2A****: VC funds will invest smaller average amounts and in earlier rounds when investing in PBCs*

- ***Hypothesis 2B****: VC funds will invest in more consumer-facing businesses when investing in PBCs*

We hypothesize that, because the PBC is a nascent form, VCs will likely invest in smaller amounts and in earlier rounds than is typical for traditional issuers. By reducing the amount of their investments, VCs can limit their risk profile in investing in these relatively untested new forms of business organization. We also expect VCs to be investing in earlier rounds simply because these legal entity forms are most likely to be adopted by companies founded after the passage of the authorizing statutes, rather than by preexisting companies rethinking their corporate structure.[105] Since the issuers are likely to be younger, most of the available investment rounds at this stage will be relatively early.

We also believe that the bulk of this investment will be directed into PBCs which are consumer-facing: where the PBC form is likely to

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[105] Some established companies have changed their form of organization from a traditional corporation or LLC to a PBC or BC. Prominent examples include, amongst others, Patagonia and Ben & Jerry's, which both converted to BCs. Nevertheless, we believe these examples constitute a relatively small proportion of our sample.

have value with consumers and other purchasers of the product in line with the PBC business model. To the extent this hypothesis is true, it would support both the arguments of "purpose washing" and that the PBC form in and of itself may be profit maximizing.

B. Data

To address these questions, we compiled a novel dataset of every Delaware public benefit corporation which received funding between 2013 and 2019.[106] We received from the Delaware Secretary of State a comprehensive list of incorporated PBCs. Using this list, we manually checked each company for evidence of investment in our study period.[107]

For information about investment transactions, we evaluated multiple potential data sources. We began by obtaining REG D filings from the SEC's EDGAR website. Next, we obtained data on PBC funding from three subscription databases which hold information on early-stage investment: ThomsonOne's VentureXpert; Capital IQ; and Pitchbook. Of the four, we found only the last — Pitchbook — to be substantially complete, containing a superset of the other datasets. Using Pitchbook data, we have records of 707 funding rounds, involving 295 distinct public benefit corporations and 1,076 unique investors.[108] We then

[106] Although a number of the companies in our dataset were founded and operational (and clearly funded) beforehand, we begin our study window in 2013 to coincide with Delaware's introduction of the public benefit corporation form in 2013. *See* Press Release, Delaware Office of the Governor, Delaware Unveils Public Benefit Corporation Legislation (Apr. 18, 2013), https://news.delaware.gov/2013/04/18/delaware-unveils-public-benefit-corporation-legislation/

[107] Our analysis is limited to Delaware-incorporated firms since other states generally do not identify whether firms are benefit corporations or not. Since venture capital firms typically prefer to invest in Delaware firms, our analysis is likely to encompass a substantial portion of VC investment.

[108] We exclude one PBC—Laureate Education—from our sample. Laureate is a high-profile international provider of private higher education. It is the only publicly listed company in our dataset and has attracted significant funding (on the order of

supplement the transaction data with our own hand-coding of low-level target industries and the primary strategy of each investor (traditional profit-seeking or impact investing).

C. Summary Statistics

We begin with some general summaries of our data. Investment in individual PBCs ranges from one to seven rounds of funding (median = 2), with round sizes that range from the low six figures to as much as $300 million (in the case of fin-tech insurance company Lemonade). Table 1 shows the change in total number of deals and aggregate round size by year. As the table indicates, we find that investment in Delaware PBCs has been growing steadily over time, particularly in terms of dollars invested. In 2019, Delaware PBCs received over $870 million of investment, spread over 101 separate funding rounds.

Table 1: Aggregate investment over time ($m)

	2014	*2015*	*2016*	*2017*	*2018*	*2019*
Deals	64	82	101	128	146	101
Total investments	$139.2m	$330.0m	$218.6m	$335.3m	$632.9m	$870.7m

To give a sense of the kinds of companies which have received funding, table 2 lists the top 10 PBCs, ordered by total investment received. This list includes both well-known brands (for example Lemonade, the shoe producer Allbirds, and the charter-school operator Altitude Learning/AltSchool), in addition to somewhat less well-known companies (such as Qwil and Yerdle Recommerce). The table also demonstrates the lopsided character of PBC funding generally: a handful of companies take the lion's share of investment. In fact, the

several billion dollars), from both mainstream venture capital and private equity investors. For these reasons, Laureate is sufficiently idiosyncratic (and large) that we think it is best excluded from our general analysis of the PBC form.

ten companies in this list account for more than half of total PBC funding.

Table 2: Top PBC investment targets

Company	*Industry (sub-level)*	*Total investment (mil.)*	*# Rounds*
Lemonade	Finance	$479.84	6
Altitude Learning	Education	$174.10	4
Meow Wolf	Arts	$161.14	3
Qwil	Finance	$136.23	5
Ripple Foods	Food	$120.56	4
AppHarvest	Agriculture	$97.00	2
Allbirds	Apparel	$77.57	5
Change.org	Internet	$72.79	5
Yerdle Recommerce	Internet	$52.01	3
Lung Biotechnology	Health	$52.00	2

In table 3, we break down the investments by consumer- and non-consumer-facing target companies. In line with hypothesis 2B, *supra*, we expect the lion's share of investment to go to consumer-facing companies, where the non-pecuniary aspect of PBCs are more likely to appeal to consumers, and to drive purchasing behavior. The data lend substantial support to this hypothesis. While it is true that investors fund both consumer- and non-consumer-facing PBCs (two-thirds of the deals and two-thirds of the target companies are not consumer-facing), the average investment in consumer-facing companies is significantly higher. With data at this level of aggregation, however, investors' motivations remain ambiguous: we are not able to parse out the extent to which this investment simply reflects purpose washing on the part of companies and investors, or whether there is instead some pecuniary advantage to consumer-facing PBCs.

Table 3: PBC consumer orientation

	Known investment (mil.)	*Total deals*	*Number of companies*
Non-consumer facing	$1,262.85	418	191
Consumer facing	$1,289.11	223	94

In a similar vein, we consider the variation between industries which are targets for investment. Table 4 shows the PBCs at a fairly coarse level of classification. Companies operating in the information technology space account for the plurality of investment dollars, while consumer products and services have the highest number of investment rounds and distinct target companies. At a more granular level (not reported here), we find that finance—which includes fin-tech services and platforms, as well as more traditional lenders and insurers—accounted for $714m, or 25%, of total PBC investment. Education companies (predominately Altitude Learning and an international student loan provider called MPOWER) received around $290m in funding, while companies involved in sustainable food and beverages (almost entirely consumer facing) account for $420m. Beyond these three major categories, the funded companies reflect a broad swathe of industries, including apparel, direct-to-consumer retail, B2B services, and more.

Table 4: Target industries

Industry (high level)	*Total investment (mil.)*	*Total deals*	*Number of companies*
Information Technology	$1,003.70	188	90
Consumer Products and Services (B2C)	$951.93	226	98
Business Products and Services (B2B)	$328.77	101	42
Healthcare	$165.54	56	25
Financial Services	$48.56	29	13
Materials and Resources	$39.03	19	7
Energy	$14.43	22	10

For about half of the 707 PBC funding rounds, we were able to identify the specific investors involved. To help address hypothesis 1B, we code each of these firms along two dimensions: (a) the type of investor (angel, accelerator, venture capitalist, hedge fund, private equity, or other)[109]; and (b) the investor's primary strategy (traditional or impact investing). Table 5 reports the first of these results. In summary: we find little to distinguish firms that fund PBCs from the

[109] The "other" category is idiosyncratic, primarily comprising large entities (foundations, hospital groups, and so on) making single, ad hoc investments in synergistic companies. (For example, The Associated Press made a strategic investment in an open-data platform, Data.World.) It also includes government investments.

typical investor profile. Traditional venture-capital firms comprise the largest group of known investors in PBCs (45% of investors).

Table 5: Investor type

	Involved rounds	*Unique investors*
Venture Capital	361	466
Accelerator/Incubator	288	120
Angel	137	313
Other	136	121
PE/Hedge Funds	61	47

Finally, table 6 lists the top 10 PBC investors, by (a) number of deals, and (b) the aggregate round size in which each investor was involved. Table 6 is, in general, a strikingly conventional list. Panel 6A (ordered by number of deals) contains leading early-stage accelerators, such as Y Combinator and Techstars. Panel 6B (ordered by size of investment) includes high-profile technology startup investors such as Google Ventures and Andreessen Horowitz. The "strategy" column in tables 6A and 6B shows whether the investor is a "traditional" (profit seeking) or "impact" company. Except for Pierre Omidyar's firm, the top 10 by round size are all traditional, profit-seeking investors. Even the smaller accelerators that comprise the largest investors by volume are primarily traditional, pure-profit firms. Again, all this provides strong support for the contention that PBCs are receiving significant investment from conventional sources of investment.

Table 6A: Top PBC investors, by number of deals[110]

	No. of Deals	*Total of involved rounds (mil.)*	*Investor Type*	*Strategy*
Techstars	19	$26.77	Accelerator/Incubator	Traditional
Village Capital	17	$25.47	Accelerator/Incubator	Impact
Plug and Play Tech Center	16	$29.9	Accelerator/Incubator	Traditional
500 Startups	15	$108.6	Accelerator/Incubator	Traditional
XRC Labs	15	$3.32	Accelerator/Incubator	Traditional
Y Combinator	15	$34.75	Accelerator/Incubator	Traditional
MassChallenge	14	$0.54	Accelerator/Incubator	Traditional
Candide Group	11	$108.7	Venture Capital	Impact
First Round Capital	10	$162.3	Venture Capital	Traditional
Kapor Capital	10	$35.83	Venture Capital	Impact

[110] Note that the "round size" refers to the aggregate amount of all rounds in which the investor was involved. It does not indicate the total amount of *actual investment* by each firm (generally, only the total investment for a given round is disclosed, not the contribution of each individual investor). The measure thus provides a rough proxy of the total value of deals in which the investor was active.

Table 6B: Top PBC investors, by involved round size

	No. of Deals	*Total of Involved Rounds (mil.)*	*Investor Type*	*Strategy*
Google Ventures	7	$559.4	Venture Capital	Traditional
General Catalyst	9	$475.3	Venture Capital	Traditional
Thrive Capital	4	$453.2	Venture Capital	Traditional
Allianz X	4	$420.1	Venture Capital	Traditional
SoftBank Group	3	$420.1	Other	Traditional
OurCrowd	3	$312.0	Venture Capital	Traditional
Omidyar Network	9	$185.1	Venture Capital	Impact
Learn Capital	8	$181.5	Venture Capital	Traditional
Andreessen Horowitz	9	$168.3	Venture Capital	Traditional
XL Innovate	3	$166.8	Venture Capital	Traditional

D. Multivariable Analysis

The univariate results indicate that PBCs are, indeed, receiving funding at significant rates. The investors reflect a broad cross-section of traditional sources of venture capital funding, with many major investment firms represented. Still, we are interested in an explicitly comparative hypothesis: are PBCs receiving *different* early-stage investments from similarly situated pure-profit peers? To test this, we obtained comparative investment data for non-PBCs from Pitchbook.

We analyzed all non-PBC transactions (again, between 2013 and 2019) for every investment firm (or angel) that also funded at least one PBC—that is, for each entity in our set of 1,076 PBC investors. As discussed in Part I, our prevailing hypothesis predicts that PBC investments will be smaller and earlier, all else equal, than non-PBC investments by the same firms. At first glance, we do not find any indication that PBCs are receiving earlier investments than their purely profit-seeking peers.

Table 6 reports the percentage of investments by round number, separately for PBCs and non-PBCs. For both PBCs and traditional startups, around 30% of investment deals come in the first round of funding, and around 25% of deals in the second. Strikingly, there is no significant difference between the two distributions. This cuts against one part of hypothesis 2A: PBCs are not receiving investment at earlier stages than their for-profit counterparts.

Table 7: Proportion of deals across rounds

	1	*2*	*3*	*4*	*5*	*6*	*7*
non-PBC	28.6%	23.7%	17.7%	11.7%	7.4%	4.7%	6.3%
PBC	31.67%	23.4%	16.69%	11.08%	6.4%	5.77%	4.99%

Two-sided Kolmogorov-Smirnoff test: $p = 0.5819$

The second part of hypothesis 2A asserts that PBCs will receive smaller investments, all else equal, than for-profit startups. We find fairly clear support for this hypothesis. Table 8 shows descriptive statistics for the size of investments, across our entire dataset. On both mean and quantile-based measures, non-PBC targets receive higher investments. The median investment (across all rounds) in a traditional target is $2.6 million, compared to just $1 million for a PBC.

Table 8: Summary statistics for round size

	Average	*Median*	*25th percentile*	*75th percentile*	*Maximum*	*N*
non-PBC	$15.92m	$2.6m	$0.25m	$10.5m	$14,000m	23,441
PBC	$5.47m	$1m	$0.12m	$4.13m	$300m	467

To examine the bivariate results in more detail, we conduct a logit regression, reported in Table 9. Our dependent variable is PBC status (1/0), and we control for the round size (logged), round number, and age of the target company at financing (also logged). Because companies typically receive more than one round of funding, we cluster standard errors on the target company. We report the results without and with year fixed effects (model (3)), to account for any general time trends, and industry fixed effects (models (2) and (3)), but we find no substantive difference between any of the specifications.

As we might expect from the tables above, the stage of funding (round number) is not predictive of PBC status: PBCs do not receive investments at different stages in their growth cycles relative to traditional pure-profit companies. Similarly—and in line with our earlier findings—the coefficient for round size indicates that the likelihood that an investment target is a PBC decreases as the size of the round grows, even when controlling for stage of investment and age at financing. PBCs are receiving less funding, across industries and time.

Table 9: Logistic regression
Dependent variable: target company PBC status (0/1)

	(1)	*(2)*	*(3)*
Log(Round size, *millions*)	0.832 (-5.86)	0.842 (-5.43)	0.843 (-5.48)
Round number	0.98 (-0.44)	0.979 (-0.47)	0.966 (-0.77)
Log(Age at financing, *years*)	1.299 (2.07)	1.266 (1.94)	1.24 (1.73)
Constant	0.0175	0.0242	0.0115
Year fixed effects	No	No	Yes
Industry fixed effects	No	Yes	Yes
Observations	20,539	20,533	20,533

Note: Exponentiated coefficients (odds ratios); t statistics in parentheses, clustered at the company level.

III. A THEORY OF THE FUTURE OF PBCS

A. Initial Conclusions

Overall, our empirical results present a fairly consistent picture—and one that is somewhat at odds with the traditional view that PBCs would struggle for investment against their profit-maximizing peers.

We find that PBCs are receiving investment at significant rates, and that investment is coming from typical sources of venture capital. While a significant proportion of PBC investors proclaim prosocial motives of their own, the leading investors are traditional, profit-seeking VC firms: Sequoia Capital, Andreessen Horowitz, and others. Finally, funded PBCs occupy a wide range of different industries but are very often consumer-facing companies, which may reflect the salience of PBC status as a profit-driver amongst consumers.

These findings support our hypothesis that the PBC is a form that for-profit investors believe will yield sufficient returns to justify investments. However, as we predicted, this investment is concentrated in industry sectors where the PBC form is likely to be part of a conscious appeal to consumers aligned with the firm's prosocial messaging. This, together with our finding of investment coming from top-tier VC funds, supports the proposition that investors expect these PBCs to yield sufficient return commensurate with other venture capital investments.

Allbirds provides an example from our data. A certified B-Corp and PBC incorporated in Delaware, the company makes sustainable shoes from wool and recycled materials.[111] These shoes retail from $95 to $115 a pair.[112] Allbirds' CEO has stated that the company chose to become a PBC because the company wanted to be in partnership with the environment. What Allbirds calls its "environmental partnership" is extensively promoted throughout its website, where pictures of

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[111] *See* Mara Leighton, *B Corps Are Businesses Committed to Using Their Profit for Good—These 13 Are Making Some Truly Great Products*, BUS. INSIDER (June 6, 2019), https://www.businessinsider.com/b-corp-charitable-business-2018-8; *see also* https://www.allbirds.com/products/runner-lace-kit.

[112] *See* Tom Huddleston Jr., *How Allbirds Went From Silicon Valley Fashion Staple to a $1.4 Billion Sneaker Start-Up*, CNBC (Dec. 18, 2018), https://www.cnbc.com/2018/12/14/allbirds-went-from-silicon-valley-staple-to-billion-sneaker-startup.html.

sheep are prominent.[113] Allbirds has also devoted resources to this principle, committing to be carbon-neutral by 2019.[114]

Allbirds has had remarkable growth, and has received $78 million over five funding rounds from investors including T. Rowe Price, Fidelity Management and Research Co., and Tiger Global Management.[115] The company currently has a $1.4 billion valuation.[116] In an interview, the CEO stated that he viewed the PBC status as an asset for attracting investors, asserting that:

> For me it's a win-win for shareholders and for the environment in our case, and for other purpose-driven companies that elect to be PBCs and B Corps. The same logic would apply for whatever public benefit they're choosing. Great companies are going to come out and be PBCs and B Corps, and that's going to be a contributing factor for why they're such great companies.[117]

Allbirds is an example of a PBC which uses that status to promote its brand to customers, while maintaining a for-profit mantra amidst expectations that its returns will be equivalent to investments in traditional corporations. While we may not take the CEO's public

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[113] https://www.allbirds.com/pages/our-materials-wool

[114] https://www.allbirds.com/pages/our-commitment

[115] *See* Biz Carson, *Sneaker Startup Allbirds Takes Flight With $50 Million in Funding*, FORBES (Oct. 11, 2018), https://www.forbes.com/sites/bizcarson/2018/10/11/sneaker-startup-allbirds-takes-flight-with-50-million-in-funding/.

[116] *See* Rob Copeland, *Trendy Sneaker Startup Allbirds Laces Up $1.4 Billion Valuation*, WALL STREET J. (Oct. 11, 2018), https://www.wsj.com/articles/trendy-sneaker-startup-allbirds-laces-up-1-4-billion-valuation-1539281112; Jay Coen Gilbert, *Airbirds' Reported Billion-Dollar Valuation: What Makes These Strange Birds Fly*, FORBES (Jan. 9, 2019), https://www.forbes.com/sites/jaycoengilbert/2019/01/09/allbirds-reported-billion-dollar-valuation-what-makes-these-strange-birds-fly/.

[117] *See* Gilbert, *id.*

statements entirely at face value, the market has validated the business choice.

In this vein, our results have limitations which require further exploration in future academic work. Our finding of widespread PBC investment confirms that PBCs *can* attract for-profit investment. But our data does not tell us whether PBCs are engaging in purpose-washing or otherwise using their social branding to yield greater profits than a traditional corporation. To be sure, at least some PBCs (like Allbirds) are using their status to attract investment, and perhaps to drive growth, but the general use of the PBC status as a profit driver requires further study before it can be confirmed or rebutted.

Moreover, while our results show that PBC investment exists, and is not insignificant in dollar amounts, to date we are aware of are only 707 investments in 295 PBCs—and these investments come in smaller amounts than for traditional corporations and LLCs, controlling for investment round. This compares to over 50,000 VC investments as a whole during this time period.[118] These results support the idea that the PBCs are still nascent and that traditional investors, while willing to invest in this form, have yet to engage with PBCs in a widespread manner.

B. What does this mean for the PBC?

If PBCs are to grow into a commonly utilized form, the investment from VC funds is an optimistic sign of support. However, for the PBC to be more widespread, network effects need to be established. More specifically, the PBC must become a familiar model for VC funds and investors generally. This familiarity must also spread to the attorneys

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[118] *See PitchBook - NVCA Venture Monitor: 4Q 2018*, PITCHBOOK DATA (Jan. 9, 2019), at 4, https://files.pitchbook.com/website/files/pdf/4Q_2018_PitchBook_NVCA_Venture_Monitor.pdf.

and advisors who work with funds and entrepreneurs, and who provide counsel about selecting a corporate form.

A primary impediment to widespread PBC usage at this point in time seems to be the continuing uncertainty about the scope of fiduciary duties in PBCs.[119] In particular, there has been substantial concern among legal advisors and commentators that PBC directors may not be adequately protected in making decisions with regard to differing purposes.[120] Moreover, the interaction of the mechanism for auditing compliance with its purpose, and the parties who can enforce this mechanism requires further definition.[121]

These are not insurmountable barriers. Definition could come through litigation. Further clarity is also likely to come as lawyers who engage

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[119] *See supra,* note 11.

[120] *See, e.g.,* Gibson Dunn, *A Corporate Paradigm Shift: Public Benefit Corporations* (Aug. 9, 2016), https://www.gibsondunn.com/a-corporate-paradigm-shift-public-benefit-corporations/ (last visited Aug. 5, 2019) (noting the risks posed by the lack of legal precedent, especially in conflict-of-interest and takeover scenarios).

[121] *See* J. Haskell Murray, *Understanding and Improving Benefit Corporation Reporting*, AM. BAR ASS'N (Jul. 20, 2016), https://www.americanbar.org/groups/business_law/publications/blt/2016/07/04_murray/ ("The Model Benefit Corporation Legislation requires that the benefit report be completed using a third-party standard, but the third-party standards are of varying quality and ill-defined in the statutes. The current version of the Model Benefit Corporation Legislation requires third-party standards to be "recognized," "comprehensive," "credible," and "transparent," but does not provide much further guidance and does not appear to have an effective screening mechanism."); J. Haskell Murray, *An Early Report on Benefit Reports*, 118 W. VA. L. REV. 25 (2015) ("[T]he statutes merely require narrative descriptions of the ways public benefit was created by the company and the hindrances the company faced. The statutes do not require reporting of quantifiable items and give the benefit corporations an extreme amount of freedom in deciding what to report. Benefit corporation proponents claim that the third-party standard requirement is at the heart of the benefit corporation legislation and works with the reporting requirements for transparency. There is, however, little to no oversight or assurance of quality with regards to the third-party standards.") (internal citations omitted).

in high-profile corporate work become more comfortable with the form, and begin to recommend it to VC firms and founders—and advise on its potential risks.

It is important here to note that when we speak of definition in this context, we are talking about definition and practice under Delaware law. VCs desire certainty about legal risk. In this regard, there is a preference for the certainty which Delaware provides as the premier jurisdiction for corporate law and the existing situ of choice for incorporation of VC investments.

Still, we see room for optimism for supporters of these new forms, both in the surprising (to us) extent of conventional VC funding and in the adoption of these forms by a number of large companies. Laureate Education, a publicly traded company, is a PBC, and adopted that status before it went public, indicating that at least some institutional investors were willing to invest despite (because of?) its PBC status. Several large subsidiaries of public companies are also now PBCs (or BCs), including Unilever's Ben & Jerry's,[122] Campbell Soup's Plum PBC,[123] Danone's "Danone North America Public Benefit

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[122] *See Ben & Jerry's Joins the B Corp Movement*, available at https://www.benandjerry.com.au/about-us/b-corp (last visited Aug. 5, 2019).
[123] *See* PLUM ORGANICS, https://www.plumorganics.com/benefit-corp/ (last visited Aug. 4, 2019) ("Plum was one of the first to reincorporate as a public benefit corporation in the state of Delaware on August 1, 2013."); Ariel Shwartz, *Inside Plum Organics, The First Benefit Corporation Owned By A Public Company*, FAST COMPANY (Jan. 22, 2014), https://www.fastcompany.com/3024991/inside-plum-organics-the-first-benefit-corporation-owned-by-a-public-co.

Corporation,"[124] and Gap, Inc.'s Athleta.[125] Furthermore, an increasing number of large corporations are obtaining B Lab certification, which will eventually require them either to adopt PBC or BC status or to make comparable changes to their certificates of incorporation.[126] The penetration of the forms into both startups and large, mature companies creates the possibility of a sort of dialectic of credibility, with VCs' acceptance helping to justify adoption to large corporations and large companies' adoption helping to build credibility in the eyes of VCs.

That said, until further definition comes, we believe companies are unlikely to take up the PBC form in wide measure. This is likely to be a slow process, and we do not want to understate the obstacles involved for companies that wish to adopt these new forms, especially for companies that are already public. Etsy furnishes a cautionary

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[124] *See* DANONE NORTH AMERICA, http://www.danonenorthamerica.com/our-business/ (last visited Aug. 4, 2019) ("We made a bold commitment to our larger, shared purpose to change the way the world eats to benefit the health of people and the planet, by incorporating as a public benefit corporation"); *Achieving Certification as Largest B Corp™ in the World and Unveiling New Name: Danone North America Celebrates First Anniversary with Two Major Milestones*, CISION PR NEWSWIRE (Apr. 12, 2018), https://www.prnewswire.com/news-releases/achieving-certification-as-largest-b-corp-in-the-world-and-unveiling-new-name-danone-north-america-celebrates-first-anniversary-with-two-major-milestones-300628797.html.

[125] *See 2018 Annual Report*, GAP INC. at 2, available at http://www.annualreports.com/HostedData/AnnualReports/PDF/NYSE_GPS_2018.pdf) ("Athleta has been certified as a benefit corporation, furthering our commitment to using our business as a force for good to drive social and environmental impact") (internal reference omitted). Gap, Inc. has also announced that it will spin off its Old Navy brand, and the remaining companies will become the largest publicly traded B Corp, which presumably means it will become a PBC. *See* Sapna Maheshwari, *Gap Plans to Spin Off Old Navy After a Dismal Year*, N.Y. TIMES, Feb. 28, 2019, https://www.nytimes.com/2019/02/28/business/gap-old-navy-spinoff.html (last viewed Aug. 5, 2019).

[126] *See Legal Requirements,* B LAB, available at https://bcorporation.net/certification/legal-requirements ("Certified B Corporations are legally required to consider the impact of their decisions on all their stakeholders. B Corps make this legal change by updating their articles of incorporation, reincorporating as benefit companies, or making other structural changes").

tale—though it also supports our hypothesis that when for-profit investors invest in PBCs, the form is a secondary consideration.

Etsy, a publicly-traded company, began as a B Corp (a certification which requires conversion to a PBC or comparable changes to the company's corporate charter), but dropped this certification recently in the wake of a shareholder activist event.[127] In that event, Etsy went public with high hopes amidst commentary that "[i]t is also an experiment in corporate governance, a test of whether Wall Street will embrace a company that puts doing social and environmental good on the same pedestal with, if not ahead of, maximizing profits."[128] But the experiment arguably failed, at least in this case. The company realigned its mission and dropped its B Corp status, stating:

> One of the requirements of B Corp certification for corporations incorporated in Delaware is that a company must change its corporate structure from a C Corporation [sic] to a benefit corporation. As we have said publicly over the past year, Etsy will not seek conversion to a benefit corporation by the December 2017 deadline because converting is a complicated, and untested process for existing public companies. . . .Although Etsy will no longer be a Certified B Corporation, Etsy and B Lab share a long-term vision for the role of business in society and the positive impact companies can, and should, have on the world, and we look forward to

[127] *See* David Gelles, *Inside the Revolution at Etsy*, N.Y. TIMES (Nov. 25, 2017), https://www.nytimes.com/2017/11/25/business/etsy-josh-silverman.html; Ina Steiner, *Etsy Gives Up B Corp Status to Maintain Corporate Structure*, ECOMMERCE BYTES (Nov. 30, 2017), https://www.ecommercebytes.com/2017/11/30/etsy-gives-b-corp-status-maintain-corporate-structure/.

[128] *See* Hiroko Tabuchi, *Etsy I.P.O. Tests Pledge to Balance Social Mission and Profit*, N.Y. TIMES (Apr. 16, 2015), https://www.nytimes.com/2015/04/17/business/dealbook/etsy-ipo-tests-pledge-to-emphasize-social-mission-over-profit.html.

> exploring new opportunities to work with them to advance that shared vision.[129]

In other words, Etsy—which was experiencing business troubles—concluded there was not a clear enough path to be a PBC and a for-profit publicly-traded business. This is a telling admission, if taken at face value, and supports our hypothesis that the PBC format is a secondary factor in VC investment. We believe that given the path dependency and network effects embedded in corporate law practice, wider usage of PBCs is likely to occur only after these forms are widely accepted and utilized in the VC community and among a critical mass of larger companies. VC adoption seems particularly critical because it has the potential to provide a pipeline of prominent companies which can serve as a template for wider adoption of this form and as a feeder to the public markets.

In this regard, VCs ultimately require an exit from their investments. This is perhaps the most telling implication of our findings. More specifically, by making these investments, VCs are also assuming that PBCs like Allbirds and Lemonade will go public or otherwise find a way to substitute out or provide liquidity for these investors. A sale of a PBC to a traditional company raises significant legal issues, so it is likely that some of the more successful firms will conduct IPOs.[130] If this occurs, then the network effects and familiarity of this form in the public company context may spur more mature firms to contemplate this form. Alternatively, constituency-focused companies like Airbnb

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[129] *See Steiner,* id.

[130] *See* Frederick H. Alexander, Lawrence A Hamermesh, Frank R. Martin & Norman M. Monhait, *M&A Under Delaware's Public Benefit Corporation Statute: A Hypothetical Tour*, 4 HARV. BUS. L. REV. 255, 257, 266, 273 (2014) (noting issues unique to the sale of a PBC such as: unclear appraisal rights for PBC stockholders, difficulty balancing social benefit against stockholder profits in a sale, and social benefit promotion assurances to stockholders post-sale); Matthew R. Loecker, *Social Entrepreneurship and Public Benefit Corporations*, MORSE, BARNES-BROWN & PENDLETON, PC: VC SPOTLIGHTS (Oct. 13, 2016), https://www.morse.law/news/social-entrepreneurship-and-public-benefit-corporation.

may consider conversion prior to their IPOs under a similar theory. But at this point, this is speculation.

C. *Theory of PBCs Going Forward*

One of the criticisms of the PBC is that the traditional corporate form itself provides the same flexibility as the PBC to engage in similar social purposes.[131] More specifically, in the corporate form the firm can take on social purpose goals and other non-economic values and pursue them.[132] The only caveat is that such pursuit must be (ostensibly) related to the firm's for-profit mission.[133] In practice, this has allowed many companies to take on ESG goals and other social missions. For example, Dick's Sporting Goods stopped retailing assault weapons, high capacity magazines, and guns to people under the age of 21. The company's decision resulted in lost revenue of over $150 million or 1.7% of annual revenue,[134] but Dick's CEO Edward W. Stack justified their position by calling for gun control stating that "[w]e implore our elected officials to enact common sense gun reform

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[131] *See* Kim Alter, *Social Enterprise Typology* (Nov. 27, 2017) at 12, https://www.globalcube.net/clients/philippson/content/medias/download/SE_typology.pdf ("A social enterprise is any business venture created for a social purpose–mitigating/reducing a social problem or a market failure–and to generate social value while operating with the financial discipline, innovation and determination of a private sector business.").

[132] *See* Brian Galle, *Social Enterprise: Who Needs It?*, 54 BOSTON COL. L. R. 2025, 2037-2041 (Nov. 2013) (arguing traditional firms can hire outside auditors to oversee compliance with prosocial goals and that corporate law generally permits traditional firms to do so); Joseph W. Yockey, *Does Social Enterprise Law Matter?*, 66 ALA. L. REV. 767, 786 (2015) ("[E]xisting corporate law already provides virtually complete protection to managers who balance stakeholder interests or otherwise make socially motivated decisions.").

[133] *See e.g.*, *Dodge v. Ford Motor Co.*, *supra* note 125.

[134] *See* Eben Novy-Williams, *Restricting Gun Sales Cost Dick's $150 Million Last Year*, BLOOMBERG (Nov. 29, 2019), https://www.bloomberg.com/news/articles/2019-03-29/dick-s-dks-ceo-ed-stack-says-gun-shift-cut-sales-by-150m.

. . .".[135] No *business* justification for this maneuver was provided in the CEO's call. However, there was no legal challenge to the company's actions on fiduciary duty grounds. And Dick's is not alone. Other publicly traded corporations have stepped up to be carbon neutral or to oppose immigration restrictions, for example.[136]

We acknowledge this argument and have some sympathy for it, but argue that the PBC offers a differentiated form that is indeed broader. Specifically, the PBC provides a governance infrastructure in which alternative purposes are considered as a mission and purpose. While the corporate form does provide significant flexibility, the possibility of legal challenge always remains if a traditional corporation leans too far in favor of some social purpose at the expense of profits.[137] A PBC sidesteps these issues entirely, allowing the company to direct its energies towards non-economic goals without any threat of legal action.[138] While there are significant issues with compliance and accountability in the PBC arena—issues we do not deal with in this article—the PBC is simply a more flexible form for firms who wish explicitly to pursue multiple purposes.

This does not mean that we believe the PBC is the wave of the future, or that it will become the norm. Rather, we view these forms as a

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[135] *Here's what Dick's Sporting Goods CEO Ed Stack Wrote About His Company's Actions*, USA TODAY (Feb. 28, 2018), https://www.usatoday.com/story/money/retail/2018/02/28/heres-what-dicks-sporting-goods-ceo-ed-stack-wrote-his-companys-actions/381452002/.

[136] *See, e.g.,* Lorie Konish, *These Publicly Traded Companies are Doing the Most to Help Prevent Climate Change*, CNBC (Mar. 20, 2019), https://www.cnbc.com/2019/03/20/these-public-companies-do-the-most-to-help-prevent-climate-change.html (listing corporations including Unilever, Toyota and Alphabet); Aaron Smith, *Cards Against Humanity Buys Land on Mexican Border to Stump Trump's Wall Plan*, CNN (Nov. 16, 2017), https://www.cnn.com/2017/11/15/us/cards-against-humanity-land-grab-trnd/index.html.

[137] *See supra*, note 138.

[138] *See supra,* note 32.

serious choice for a minority of companies, though perhaps eventually a not insignificant number. The flexibility of the corporate form provides the majority of firms the capacity to consider other interests to a degree. However, the PBC remains available for firms that want to explicitly pursue profit and other goals or want to brand themselves in this manner to consumers. In this regard, we expect the steady flow of PBCs that receive for-profit investment to continue.

This steady flow of PBCs should create a network of companies that can form the basis for future entrepreneurs wanting the particular goals or branding of a PBC. The network will furnish needed familiarity and legal precedent related to these forms so that stakeholders can contract with less uncertainty. Our study shows that this foundation is already emergent. While the future is speculation, we expect this trend to continue. As the current cycle of PBC investments succeeds or fails we theorize these investments will create a path for future adoption and solidify the PBC choice. Our results lead us to believe that this choice will involve PBC selection in areas where the business models implicate direct consumer choice – and concomitantly, where the mission of the company, the investor, and the consumer align. These are areas where consumers gain utility from association with the company and its product. This will create a cycle supportive of the PBC. If the history of the corporation is hundreds of years, the signs for PBCs are good for continued usage.[139]

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[139] In putting forth this theoretical prediction, we assume that the legislative landscape remains the same. Senator Elizabeth Warren has proposed that corporations with one billion dollars or more in revenue, whether public or private, would have to consider the interests of all relevant stakeholders when making a decision. *See* Elizabeth Warren, *Warren Introduces Accountable Capitalism Act* (Aug. 15, 2018), https://www.warren.senate.gov/newsroom/press-releases/warren-introduces-accountable-capitalism-act. These and other proposals may implement alternative forms, but ultimately the *sine qua non* of the PBC is a dual purpose rather than a constituency statute, so we do not view such legislation as eliminating the utility of the PBC forms.

D. *Conclusion*

The PBC has stirred much debate and speculation about the future of the corporation. Some have called it the future while others decried the form as mere public relations or purpose washing. In this article we have attempted to add data to the debate. Using a hand-collected sample of all Delaware-registered PBCs that received investment between 2013 and 2018 we examine whether PBCs are the future or mere fancy.

We find that neither hypothesis holds. Instead, we find that there are 295 PBCs which have received investment from VC funds amounting to over $2.5 billion in the aggregate. This investment is significant because it shows that the PBC form is not a failure and that it is capable of attracting for-profit investment, a marker of success. This investment is coming not just from pro-social VCs but from top-tier firms.

Nonetheless, we also find that PBCs are being funded over a wide range of mostly consumer-focused industries (banking, food, education, technology, and more), implying that the form is a secondary consideration to the for-profit motive. In other words, the PBC form is most likely to receive VC funding when the PBC's business strategy suggests the form will benefit a for-profit mission. Our evidence also suggests that PBC round sizes are smaller than their purely profit-seeking peers, implying that VCs are taking less risk with these forms than with traditional corporations.

Ultimately, we theorize that, based on our findings, the future course of the PBC is uncertain. Networks of lawyers, investors and companies still need to familiarize themselves further with this form to build a foundation for continued usage at higher rates. Moreover, laws about auditing and fiduciary duty need testing and fleshing out, events which only continued usage of the PBC form can bring. Ultimately, though, our results portend a future for the PBC form, one that may see increased usage and scope.

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