Chapter 3 Protecting long-term commitment: legal and organizational means

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3. 1 Introduction

The idea that corporations exist solely for the benefit of their shareholders has been termed “one of the fundamental fault lines of our economic model” (Purpose of the Corporation Project, 2015). The ‘fault’ with shareholder primacy thinking is registered in broad evidence that the dominant corporate governance framework encourages excessive short-term risk taking and so detracts from long-term investment strategies, including research and development (Lazonick, 2013, 2014; this volume, chapter 6). This has adverse effects on future profitability and resilience with regard to the mitigation of systemic risks (Perotin and Robinson, 2004; Webb et al., 2014). To address this situation, it can be argued first, that there is a ‘business case’ for engagement with ESG issues, and second, that there is, in principle, no *legal* obligation for directors to focus exclusively on the maximization of shareholder value.

In relation to the first point, establishing a clear relationship to financial performance is a problematic endeavor (see McWilliams and Siegel 2001). Nevertheless, an increasing amount of research has focused on the benefits of considering the long-term interests of a large group of constituencies. For instance, a meta-study found that companies that engaged with, and reported on, environmental, social, and governmental (ESG) issues outperform their industry peers on the stock market and benefit from the lower cost of capital (Eccles et al. 2014; Cheng et al., 2016). Eccles et al. (2014) also found that companies which assign responsibility to boards of directors for sustainability and the alignment of executive compensation with ESG ratings and customer satisfaction metrics are more likely to outperform their counterparts over the long-term. Such ‘responsible’ firms actively cultivate an investor base that shares a long-term strategy, thereby lending support to boards with a commitment to ESG factors, for example, in their strategizing (Veldman et al., 2016).

In relation to the second point, it is often argued that there are legal grounds for prioritizing shareholder value over other goals. However, according to leading company law scholars worldwide, there is no legal obligation for companies to adopt shareholder primacy as a guiding principle (Modern Corporation Company Law Statement, 2014). To the contrary, it has been forcefully argued that the notion of the public corporation as a specific kind of legal construct points to the fiduciary duties of directors being owed to the corporate entity, not to its shareholders (Veldman et al., 2016). In this view of the public corporation, shareholders have, at best, limited rights; while the board, as a separate organ, functions as a ‘mediating hierarch’ between multiple claims on the entity. In this conception of the modern public corporation, it is justifiable for directors to focus on delivering long-term sustainable value creation in the interest of multiple constituencies and goals[1], take into account environmental, social and governance (ESG) factors in their strategy and report on those factors as an integral part of long-term business strategy, while satisfying the interests of shareholders as a by-product of the success of the corporation (Biondi et al., 2007; Blair and Stout, 2011; Company Law Statement, 2014; Deakin, 2012; Khurana, 2007; Johnson and Millon, 2005; Millon, 2014; Parkinson, 2003; Robé, 2011; Sacconi et al., 2011; Sjafjell et al., 2015; Veldman et al., 2016).

[1] Historically, all types of group representation, including for commercial purposes, stipulate their public or social purpose (Beverungen et al., 2014). Within this framing, identifying ‘hybrid organizations’ as an example of ‘alternative’ institutional logics misses the point. It is exactly the contemporary notion of the modern corporation, i.e. the for-profit corporation with no ex ante defined purpose, that is the outlier, as it allows for major privileges and protections, but the definition of its broader purpose is left up for grabs, allowing that definition and its control to be shifted to one, largely external and uninvolved constituency.

Despite firms having economic incentives to achieve long-term goals and despite there being no obligation on them to prioritise short-term shareholder value, the presumption that responsible behavior will emerge spontaneously seems problematic:

First, financial reasons may propel firms spontaneously to engage with ESG issues. . Nevertheless, as there is a reported lack of such spontaneous engagement with issues on the risk side, such as environmental and social concerns, with a continued focus on shareholder value as the driving interest in corporate governance theory and practice (Ireland and Pillay, 2010), it seems likely that an understanding of broad economic interests and risks may only provide a limited push toward such 'responsible' behavior.

Second, although the notion of fiduciary duties toward the 'entity' or the 'corporation' provides a reference point in relation to which, the choice of purpose remains potentially open; strong claims by a singular constituency like shareholders may be mitigated; and the entity or corporation achieves a standing as a valid purpose; this 'open' approach still provides a problematic basis to determine a *positive* conception of corporate purpose or duty for boards (Mansell, 2013). The 'open' legal view does not challenge or explain the attribution of ultimate (though not direct) control rights to shareholders – notably, the right to appoint and dismiss directors without cause. In this key respect, company law remains asymmetrical in the way it conceives of the rights, claims and obligations of corporate constituencies (Segrestin & Hatchuel, 2011). Consequently, the implicit view of the corporation as a (neutral) collection of procedures, on which the notion of duties toward the corporation or entity implicitly rests, is necessary but insufficient to remove the enchantment in corporate governance theory and practice with shareholder primacy and the short-term maximization of shareholder value. Similarly, the notion of "stakeholder engagement" in current observable practices does not engage with the conditions for a legal commitment of the corporation or of its executives towards the long-term interests of various constituencies (Kaufman & Englander 2005, Segrestin & Hatchuel, 2011). Under these conditions, a change in the economic context or in the ownership structure could easily jeopardize a prior engagement with such broader interests.

In any event, the ‘open’ legal view is increasingly challenged by the development of new legal provisions that have recently been adopted in corporate law in various states in America and Europe that explicitly enable corporations to follow and embed social or environmental purposes and to which we now turn.

To explore alternative frameworks to build long-term sustainable socially useful value and profitability, this chapter will engage with the ‘open’ legal view as the point of departure to address corporate governance as an explicit model for organizational structuring which can be explored in a fundamentally open way. Engaging with the broader issues identified, we will build on this open approach to present different legal mechanisms and frameworks designed to protect a societal orientation of the corporate purpose, by establishing locks on assets, profit, mission and values sufficient to enable the recognition, embedding and protection of the interests of constituencies and multiple time-horizons, and to guard against ‘mission drift’.

Our point of departure is the literature on Social Enterprise (SE). Taking the current legal and regulatory framework in the UK as our point of reference, we consider the variety of state sponsored legal forms, architectures and mechanisms, that allow for the provision of locks on assets, purpose, mission and values. We build upon this analysis to explore how a different, more sustainable framing of the ‘for-profit corporation’ might be advanced. Specifically, we engage with articles of association, share structures, sets of rights attached to shares, fiduciary duties, reporting standards, incentive structures, and external regulation. We then consider the ‘profit with purpose corporation’ (PPC) model and engage further with ideas around certification and articles of association before addressing the variety of approaches to shares and shareholder relationships. These approaches and instruments provide, we argue, various means to develop, safeguard and, under specific circumstances, also restructure the organizational architecture and to create a legal commitment by shareholders that opens a new avenue beyond the usual concept of “stakeholder engagement”.

The chapter is intended to examine the conditions for for-profit corporations to be able to acknowledge, and credibly embed in their purpose a fuller range of corporate constituencies, interests and time-horizons. We show that supporting a broader notion of purpose for the for-profit corporation requires new and innovative legal provisions, the need for which has, to date, been insufficiently theorized. Such legal provisions open a new theoretical debate, which we delineate in the discussion.

3.2 Social Enterprise: Co-operatives and Community Interest Companies

A 2012 report from the Ownership Commission lamented the lack of corporate diversity within the UK economy. Social Enterprise (SE), for example, provides a fundamentally different form of structuring business;presents a rich area for exploring corporate diversity (Ridley-Duff and Bull, 2015); and a means that may promote a more corporately diverse economy (Michie, 2014: 64). In the following, we explore co-operative and mutual structures, as well as the Community Interest Company (CIC) in the United Kingdom. The field of social enterprises[2] (SE) provides a different approach to business whereby goals of profit and growth are given equal status with social and environmental objectives (Defourny and Nyssens 2007, Jones and Keogh 2006, Kerlin 2006, Kelley 2009). Surplus and profits in SE, subsequently, are reinvested in meeting social and environmental objectives as well as maintaining long-term profitability and sustainability. We reflect also upon what may be learned from social enterprise for the solely 'for-profit' corporation.

3.2.1 Co-operatives

There is increasing academic interest in co-operative practices and the resilience they appear to provide, specifically after recent downturns in the economy (Alperowitz, 2013; Atzeni, 2012; Birchall, 2013, Novkovic, 2008, Schneider, 2016; Parker et al, 2014; Roelants et al, 2012; Webb and Cheney, 2014).[3] In many countries - Japan, Germany, New Zealand, Spain, Italy, Denmark, Switzerland, Finland and France - co-operatives are central and even dominant players in a variety of sectors (see http://monitor.coop/ for a list of the 300 biggest worldwide cooperatives). Co-operatives

[2] We exclude nonprofit associations and foundations from our analysis. Although they conduct business activities that create economic risks, they rely on the requirement not to distribute any profit or any assets to the providers of finance (see chapter 4).

[3] For those interested in comparisons between co-operatives and non-co-operative enterprise we recommend the work of Restakis (2010) and the review of Lampel et al (2010).

produced US$2.98 trillion in annual revenue in 2014 (Grace Associates, 2014), while Roelants et al (2014) calculate that 250 million people are employed by co-operatives around the world. China, India, South Korea and Turkey, along with four OECD countries with high GDP growth, now have more than 10 per cent of their populations working 'within the scope of' co-operatives (Roelants et al, 2012: 31). There has also been renewed interest in participation and democracy in organizations and the rise of what is called 'platform co-operativism', specifically in the IT industry.

There are several types of co-operatives depending on industry and market. In agriculture there is an abundance of 'producer co-operatives' comprising groups of smallholders using a co-operative structure as a means of collective bargaining (Lacey, 2009). Other types of co-operatives include worker co-operatives owned and governed by employees and member co-operatives where customers can buy into the co-operative. In addition, an increasing number of non-capital intensive professional services and small-scale manufacturing firms are organised as co-operatives (Dow, 2003). Co-operatives can be differentiated also by looking at members' role in decision making; this is done either collectively, based on consensus, or through delegation to a board that contains several members who represent the whole enterprise. There are also multi-stakeholder and solidarity co-operatives "involving different types of membership and attendant variations in voting rights and influences on policies" (Cheney et al, 2014: 592).

It is evident from the above that co-operatives are governed in diverse ways even if they are constituted within a broadly shared set of overarching principles stemming largely from the 19th century Rochdale Pioneers. The International Co-operative Alliance has established seven principles and values that characterize co-operatives: (i) Voluntary and open membership; (ii) Democratic member control; (iii) Member economic participation; (iv) Autonomy and independence; (v) Education, training and information; (vi) Co-operation among co-operatives; and (vii) Concern for community. In successful worker co-operative networks like Mondragon in Spain, other principles have been added relating to the instrumental and subordinate nature of capital, payment solidarity and the sovereignty of labour.

These principles formally lock in rules pertaining to members, democracy, autonomy, co-operation, education and concern for community. Although their substantive operation varies, what remains constant is the right (and power) of members (e.g. producers, workers and consumers) to shape the direction and future of the co-operative through democratic means. As there is a legal obligation to consult and satisfy members (including board members) who own the co-operative and because the members/shareholders of co-operatives will have a direct link to the performance of the corporation, much like in traditional investor-partners, the link between ownership and control is far less dis-associated than with the temporary, and largely external shareholders of the public corporation (Kay, 2015; Veldman and Willmott, 2017). Moreover, a co-operative structure can improve corporation performance and provide resilience (De Jong and van Witteloostuijn, 2004). This structure does not, of course comprehensively "solve' the fabled principal-agency problem but co-operatives do have -- as a consequence of adopting, instilling and defending the original seven principles -- a good track record for maintaining long-term thinking.

Problems with the Co-operative Model

Some of the problems associated with co-operative governance include the challenge of recruiting qualified and experienced co-operative members in the boardroom (Kenkel, 2012); establishing a well-defined purpose that goes beyond the co-operative principles; and the time it can take to make decisions while simultaneously maintaining the democratic elements of a co-operative (Grott et al, 1987; Harrison and Freeman, 2004). Members disagreeing on the correct course of action through a lack of experience, knowledge and education, or pushing their own agenda may also lead to harming the long-term sustainability of the organization. Moreover, co-operatives do not necessarily incorporate or ensure a concern for the environment (Bibby, 2013; Toynbee, 2012). Finally, pressures to conform to external demands (from policy makers, government regulators, market institutions and supply chain partners) can be translated into a problematical "up-scaling" of operations to keep pace with the market (Roelants et al, 2014) and/or a resort to short-term measures (Mellor et al, 2016).

Take, for example, the significant failings at the Co-operative bank. In 2009, the Co-operative Bank, under pressure to up-scale and increase retail customers, resorted to an ill-advised and rushed purchase of Britannia Building Society, another mutual organization. The aim was to create a mutual bank capable of taking on the larger corporates in finance. Unfortunately, a lack of diligence meant that loans inherited from Britannia were of poor quality and the Co-operative bank suffered huge losses. Being a mutual meant that it was not possible to issue further shares, as other banks did, to ease their difficulties. Unlike other banks, however, the bank was part of the much larger and stable co-operative group who have been able to absorb some of the costs. Such failings are not quite comparable with the poor governance in mainstream finance that led to the financial crisis, but balancing issues of growth and other market pressures with concerns for the future and benefits to co-operative members will also remain an issue in the governance of co-operatives.

In addition we can consider the example of mutuals. The support of external institutions, including the legal framework, is fundamental for sustaining the use of the assets for a specific purpose/mission of organization. Like co-operatives, mutuals rely upon a membership structure and member investment capital to weather crises and resist takeovers, while profits are distributed among, and for the mutual benefit of, members (Michie, 2013: 64). They are designed to share risks amongst members and in the UK they have become popular in insurance, savings, healthcare and pensions industries as well as credit unions and friendly societies. In this regard, it is relevant to consider how, 30 years ago, the UK Building Societies Act (1986) provided the opportunity for many mutual building societies to be de-mutualized and privatized.

It is notable that none of the mutuals that were privatized withstood the financial crisis. They either failed or were taken over by larger private banks – thus reducing the number of competitors and the number of alternative corporate forms (Michie, 2014: 64-65). In Continental Europe, in contrast, since the financial crisis the combined market share of mutuals in the financial sector has risen from 22.6% to 28.1% (Ridley-Duff and Bull, 2015: 28). New figures in the ICMIF (International Co-operative and Mutual Insurers Federations) global report (2015) indicate that this market share is no longer growing in dollar value terms (due to local currency depreciation against the US dollar). However, the number of members/policyholders continued to grow in every region (average 3.5%) to reach 955 million people.

It is important to note, our focus in studying co-operatives and mutuals is not one of finding the most effective capitalistic form. Instead, we believe that co-operative principles of long term thinking, democracy, empowerment, local communities, equality, commitment to education and resilience deserve attention. One example is stability; despite a variety of attempts to de-mutualise Mondragon co-operatives, workplace democracy and democratic assembly have provided protection against such actions. To protect and strengthen principled co-operation in mutuals, it is of course necessary to have a stable and supportive legislative framework.

Cooperative members' objective of having control of policy contrasts with metrics such as market share, profits and dividends and means that priorities differ for non-cooperative businesses when considering profit margins sought or short term fluctuations in market share. Indeed, for co-operatives and mutuals, wealth is created, measured and assessed in a variety of different ways in comparison to traditional companies.

3.2.2 New legal forms for SE

Addressing the reduced provision of public services by the state (Defourny, 2001), governments around the world have started to introduce hybrid company forms that provide stability and lock in purpose, like the *'vennootschap met sociaal oogmerk'* (VSO) in Belgium, the 'Social Co-operative Enterprise' popularised in Italy and adopted across the EU (most recently in Greece), and not-for-profit corporations (NFPC) in Canada (Galera and Borzaga, 2009; Lambooy et al, 2013). In the following we explore the community interest company (CIC) in the UK.

Introduced in 2005, a community interest company (CIC) provides a legal form for social enterprises that permits the use of profits and assets for societal good. Prior to this, the only legal forms available for entrenching 'community benefit' were charities, charitable companies (which required dual registration) and community benefit societies. The Labour government sought a low cost, lightly regulated, legal form that suited the needs of social entrepreneurs. It responded by reforming both company and charity law, placing more emphasis on 'public benefit' in the Charities Act 2006, and introducing the CIC to satisfy community needs (Morgan, 2013; Ridley-Duff and Bull, 2015).

To become a CIC, a 'community interest test' must be submitted and approved by the registrar of companies for England and Wales. Company Law is flexible enough for CICs to organise themselves as mutuals, co-operatives, community enterprises as private companies limited by guarantee, shares, or as a PLC (albeit with restrictions on dividend and asset allocation). These arrangements enable social entrepreneurs to register a regulated company form for their social enterprises without dual registration for charity status. Easy to set up, yet providing the stability of limited liability, CICs have proved popular in the UK with 12,000 registered in the first 11 years. Indeed, many co-operatives and mutuals have used the CIC structure to make an IPO and retain PLC status. Many charities also have a CIC subsidiary or have converted their subsidiary enterprises to CICs.

Finance for CICs can come from shareholders, employee shares, grants and donations. Typically, it is necessary to generate over 50% of income from trade or commercial activities to secure recognition as a social enterprise (Ridley-Duff and Southcombe, 2012). The assets of a CIC are locked, so they cannot be freely transferred or distributed to any organization that is not a charity, or without consent of the CIC regulator. The asset lock maintains the assets of the CIC for the benefit of the community[4] and ensures the long term commitment to such a cause. Similarly, a dividend cap was introduced to enable a balance between appearing attractive to investors but also ensuring the bulk of profits are used for the benefit of the company. This cap was raised to 20 per cent of the paid-up value of a share from 2010, and was completely removed from the CIC in 2014[5]. The maximum aggregate dividend in

[4] Community for a CIC can be defined as a local community or the entire population. The CIC regulations state that a community is defined as a group of people who share a common characteristic which distinguishes them from other communities. The distinguishing features of the community are ascertained via a "community interest test", whereby a potential CIC puts together a community interest statement. From this statement the regulator decides whether the CIC will conduct activities that a reasonable person might consider are for the benefit of the community. See https://www.gov.uk/government/publications/community-interest-companies-how-to-form-a-cic for more information.

[5] See http://legislation.data.gov.uk/uksi/2005/1788/part/7/made/data.htm?wrap=true (accessed 2 May 2013)

the CIC remains 35 per cent of the distributable profits[6]. Both the asset lock and dividend cap are fundamental parts of having CIC status. The CIC form is therefore a way of ensuring assets and profits are used predominantly for the benefit of a specified community, whilst allowing companies access to different forms of finance beyond grants from charitable bodies. All of this is overseen by a purpose-built regulatory body.

Problems with the CIC Model

The CIC is becoming the legal form favoured by state authorities to increase the amount of wealth channeled into purposeful investment through low cost company structures that prioritise purpose over profit distribution. However, the community interest test (see above, footnote 4) does not require direct engagement with the community beneficiaries other than a short written report on measures attempted. The decisions about a CICs status rely upon the subjective decision of the regulator who has to decide whether '*a reasonable person might consider the company's activities to be beneficial for the community'* (Lambooy et al, 2013). In practice, as noted by a CIC regulator (Jump, 2007), this consideration rules very few non-political organizations out from being CIC. Moreover, as there are no mandated governance structures, it is the responsibility of the members/directors to pursue the community interest and maintain links to stakeholder groups. Finally, stakeholder groups do not have to be represented at board level. In effect, CICs are only held accountable to the regulator every year through a form in which the directors of a CIC must prepare a community interest report. As a result, the recognition and operation of the CIC has become reliant on the regulator.

As a business form, the CIC is subject to additional regulation, but attracts no tax benefits. Perhaps for this reason, as legislative changes show, the operations of the asset lock has come under sustained pressure to allow higher dividend payments to social entrepreneurs, and flexibility in the disposal of assets at market value (Ridley-Duff and Bull, 2015). And unlike charities, the additional regulatory effort provides only intangible reputational benefits, rather than tangible financial benefits. With

[6] The available portion of a corporation's profits, net of realized losses, which are available for dividend distribution.

limited returns for both investors and members, it may be more difficult to scale operations and grow as a consequence of the combined effects of lack of investment and extra regulatory costs. CICs may also not be the optimum choice for staff-controlled social enterprises as they deny capital growth to the parties that create value. CICs are designed to invest not distribute, and this weakens its appeal where staff are responding to their own disadvantages or low pay because the cap limits the way the surplus can be shared in good trading years. In short, asset locks may be regarded as a problem by social entrepreneurs and worker-members if they are concerned to respond flexibly to internal/external pressures for growth.

Due to its limitations and vulnerabilities, the CIC may be seen as exploitative insofar as the asset lock shifts surpluses into indivisible capital reserves without adequately compensating entrepreneurial or productive labour. As part of an indivisible reserve, capital is commonly owned for community benefit and - upon dissolution - would have to be transferred to an organization pursuing a similar goal (much like a charity). However, without a *requirement* for co-operative management, there is no democratic control of this capital and entrepreneurs can use it to buy assets and then sell them to private ventures so long as the regulator is satisfied that such sales are at ‘market value’ and in line with the provisions of their Articles of Association. Consequently, legal models that provide for greater democratic control over the use of capital, such as Spanish style co-ops (Holmstrom, 1993; Whyte and Whyte, 1991), trade-union led ESOPs (Spear, 1999), trust-based ESOPs (Erdal, 2008) and FairShares Model enterprises (Ridley-Duff and Bull, 2015) merit active consideration as alternatives to the CIC (see also Hockerts, 2015).

3.2.3 For-profit Companies

The SE literature offers a number of interesting ways to consider corporate governance, which may appeal to an increasing number of top executives wishing to engage in socially responsible initiatives but it has a major drawback in relation to existing for-profit corporations. Adopting a different organizational form is often highly problematic once a corporation is listed as it may involve changing the corporation’s formal and informal governance processes and may deter external financing

(Levillain, 2015). To explore the means available to engage with the concept of purpose in the context of the for-profit corporation we first investigate more generic means, including mission statements, certification, share rights, and share structures. We then continue the discussion in 3.2.4 looking at recent research on profit-with-purpose companies (PPCs), where it is argued that off-the-shelf organizational architecture of the public corporation is implicitly structured in such a way that the shareholders are favoured over other constituencies (Segrestin et al., 2014). The profit-with-purpose approach provides several means to deal specifically with this implicit imbalance.

Statement of purpose

It has been argued that a clear mission statement or statement of purpose, normally provided by a CEO or board, can have numerous benefits for a companies' governance and management (Ellsworth, 2002; Ownership Commission Report, 2010: 11). It may clarify which audiences matter to the board; introduce clarity about investment and payout horizons to investors; and clarify what time-horizons the board wants to adopt in the pursuit of its strategies. As such, a clear statement of purpose can create a better alignment between the expectations of boards and investors; and it may help boards to develop an active policy of encouraging investment by strategic investors with a consistent track record of responsible and long-term engagement with corporate strategy.

The drawback of a statement of purpose is that it is usually connected to strong leadership and can be challenged, either from within or from outside the corporation. Examples such as the Cadbury-Kraft and the Unilever takeover bids show how support for the stated purpose by specific shareholders is a decisive factor for its strength, but that this support may not be forthcoming when shareholders have different agendas. In the light of such pressures, the strength of a statement of purpose should not be considered stable when pressure is applied by shareholders with different agendas for a corporation (Tsagas, 2014).

Certification

Another way to integrate purpose is by external validation and certification of specific aspects of a corporation's strategy and reporting. The most well-known example of external certification is the B-corp standard. Not to be confused with the state sanctioned benefit corporation status, this is a private certification process that assesses the corporation's impact on the communities where it operates, its relationship with employees, its impact on the environment, and the corporation's governance. It aims to indicate as to whether a corporation meets certain standards of accountability, transparency, performance and sustainability by requiring that the corporation integrate a commitment (i.e. broader societal purpose) to stakeholders in its governing documents and provides a comprehensive model for embedding a broader, socially aligned purpose in the governance of a for-profit corporation (Veldman et al., 2016).

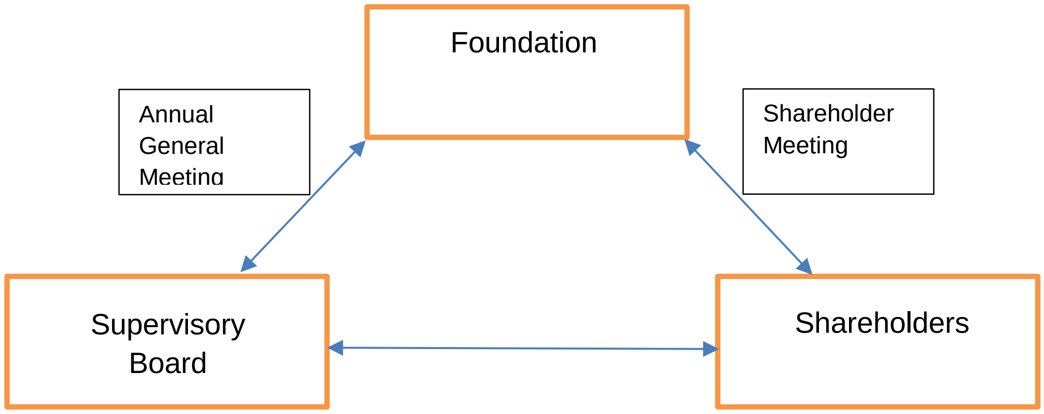
However, just like a statement of purpose the B-corp standard is dependent on continued shareholder engagement and support. The absence of a formal legal status makes the effectiveness of such provisions, especially under stress, uncertain. Also, it is not clear how far down the line of subsidiaries such accreditation goes. Finally, certification by alignment with a particular brand-marker or certificate has been critiqued for permitting and perhaps inviting symbolic adoption and decoupled talk and action (see Brunsson et al, 2012; Sandholtz, 2012).

Share rights

A third way to embed a broader purpose is to engage with shares and the rights they provide. More traditional approaches to shareholder engagement, such as enlightened shareholder value or a stewardship approach, typically do not question the fact that shares offer a number of rights that can be differentiated, such as whether they are 'original' shares or not, the time period in which they are held, the types of influence they offer, and the types of return they bring. What, then, if share rights are not viewed as bundles of rights with a fixed content, but rather as coupons that can be attributed with various cross-sections of rights dependent on specific choices, and with rights that can be changed, dependent on circumstances? We first consider the foundation structure as a relatively common way in which share rights can be used to embed the purpose of the corporation.

Below is a typical foundation structure for a financial services firm in which a triangle of three inter-related groups determine the strategy and ensure the vision and mission of the corporation:

Fig 3.1. Typical Foundation Structure



At the top of the triangle sits a foundation that monitors the sales of shares or depository receipts. Although shares are available, they are held in trust by this foundation. The foundation board votes on particular issues and is guided by the mission of the corporation and the interests of the depository receipt holders. The 'shareholders' vote on who should be on the board of the foundation. Typically, shareholders are limited to a maximum number of votes and cannot own more than a certain percentage of all depository receipts/shares that are issued. Even when the shareholders votes are counted, the recommendations must be approved by the final part of the triangle: the supervisory board. The interplay between the three parts of the triangle allows for the retention of control over the purpose, vision, mission and strategy of an organization. Such structures rooted in Trust Law are favoured amongst foundation-owned businesses like Novo Nordisk and trust-owned businesses with high levels of employee involvement like John Lewis, Arup, and Swann Morton (see chapter 4).

Multi-class share rights structures

The foundation structure shows how the creative use of rights attached to shares can be used to establish or strengthen a 'lock' on a specific aspect of the corporation. This use of share rights can be expanded considerably. Voting rights, for instance, can be split between shares with voting and non-voting rights, or preferred voting rights, as with golden shares. Voting rights can also accrue to specific types of shares and conditions, so that their accrual can be made proportional to the continued presence in a firm's capital; and they can be made conditional on whether they are traded to another party. The length of a shareholding may determine the type of proposal that a shareholder can make or the level of dividends, a minimum time can be stipulated before dividends are paid at all, and time-weighted dividends can lead to increasing payments over time. 'Loyalty shares' may also give the right to buy additional shares at an advantageous price, or those shares may carry special bonuses (Bolton and Samama, 2013).

Such diversified approaches to share rights can be beneficial for making a distinction between the status of a share in a liquid market, and specifically in relation to high frequency trading; and they can also be helpful in engaging with the rise of intermediaries who do not possess shares but hold stock with which they vote (Veldman et al. 2016). Moreover, such approaches can be used to retain (preferred) voting rights for a specific group of shareholders, such as the founders, employees, state and other groups of stakeholders. As these structures allow the retention of control over long-term business strategy and vision, and the increased capacity to resist takeover bids, such approaches are of particular interest for boards of companies that do not have a major controlling shareholder and/or in markets that do not permit protection against takeovers.

The creative use of multi-class share structures has been pioneered in Employee-Owned Businesses (EOBs) such as Gripple which has developed a structure with two golden shares for each corporation in the group. The employee shareholders of each EOB become members of a holding corporation, in which one golden share is controlled by the members of GLIDE (i.e. employees across all member companies) and the other by a foundation. A member corporation cannot be de-mutualised without both golden shareholders reaching agreement. The intention of this structure is “to prevent the break-up of companies for the sole purpose of profit” (Gripple, 2017, online).

The FairShares approach (Lund, 2011; Ridley-Duff, 2015) also adapts existing legal forms (for companies, co-operatives, partnerships and associations) through model constitutions that illustrate how founders, labour, users and investors can be enfranchised. This allows them to share the power and wealth generated through a joint venture. Moreover, rights are allocated to different classes of shares dependent on the circumstances of the firm, and the nature of members’ capital contributions (McCulloch and Ridley-Duff, 2016). By allowing for particular ‘sunset moments’ (e.g. reaching a particular pre-defined amount of turnover or profit), control and dividend rights can be dynamically realigned to re-balance how power and wealth is distributed over time (Ridley-Duff, 2017). Also, share purchases can include time-limited rights which are granted in return for different kinds of capital contribution. For example, workers’ intellectual capital contributions could be treated more like financial capital contributions by returning some capital rights to them if they leave the firm. Splitting and recombining rights and time periods can be used to develop new structures that give controlling or monitoring rights to stakeholder groups and help to transform conceptions of the purpose of a corporation (Mayer, 2013).

3.2.4 Profit-with-purpose companies (PPCs)

Having examined various ways in which purpose can be embedded and protected in for-profit companies, we now return to the question of their relevance for the future development of public corporations with a profit motive. In relation to the Social Enterprise literature we argued that the means found there are interesting, specifically because they allow us to think of corporate governance as an open structure of rights and obligations, in which various types of locks can protect the interests and timeframes of various constituencies. We continued our exploration with mission statements, certification, and share rights structures that embed organizational purpose into for-profit corporations. However, the mission statement and certification approaches rely primarily on long-term engagement by shareholders without designing the means of securing this engagement. As shareholders in public companies hold shares for increasingly limited time and can be easily replaced by others that tend to prioritize market value over firm value (Kay, 2015; Williams and Zumbansen, 2011), this can be a problematic proposition. Rethinking share rights structures presents its own issues. Vesting rights in specific classes of shares is a two-way proposition and may entrench the position of constituencies by providing a lack of accountability and/or a lack of means for engagement by other constituencies on the basis of those rights (Hong Kong Stock Exchange, 2014). An example is the foundation structure, which offers insulation from both external and internal stakeholders, including employees and customers.

Beyond these general drawbacks, such approaches do not deal explicitly with a further issue specific to the way company law deals with the for-profit corporation. The work of Hatchuel, Levillain, and Segrestin (e.g. Segrestin et al., 2014) shows how the organizational architecture of the public corporation creates a strong asymmetry, as it tends to favour shareholder rights over those of other constituencies, thereby supporting shareholder-oriented and short-term financial-oriented interests over broader and more socially responsible ones (Kay, 2015; Mayer, 2013; Sandberg 2011; Strine 2010, 2014). In the US, this asymmetry was recently reinforced by several judicial decisions that have reaffirmed the primacy of shareholder interests, particularly in situations of a change of control (Yosifon 2014).

We next turn to a number of recent legal innovations that have been adopted in several countries, the most significant ones of which have been the Benefit Corporation and the Social Purpose Corporation (SPC).The PPC approach engages with this issue by looking at means that will foster a commitment of shareholders and directors towards an explicit not-for-profit purpose within usual for-profit structures but without the asset-lock or profit-lock that mostly characterises SEs (Clark and Babson 2011, Levillain 2015, 2017). The main objective that has guided the design of PPCs is the creation of models that they can be used for existing as well as for newly formed public and private corporations (Social Impact Investment Taskforce: 38-39) and that will protect corporate engagements towards broader purposes than financially oriented ones, and increase the credibility of such engagements.

To do so, the PPC allows purpose or mission to be regularly revised following the corporation's development; demands the commitment of shareholders towards the stated purpose by introducing it in the articles of incorporation of the firm; and requires super-majoritarian shareholders' approval for the change of the purpose. This provides four distinctive features for the PPC: the definition of collective purpose; shareholder commitment towards the stated purpose; assessment standards; and control mechanisms (Levillain et al., 2015).

Definition of a collective purpose

Profit-with-purpose companies require the adoption of one or several purposes that are different from profit seeking but do not exclude or contradict it. These purposes do not justify asset-lock or profit-lock, and do not appear to be necessarily in contradiction with a financial objective. Two different types of purposes can be chosen. One is a generic purpose of creating positive impact simultaneously upon a large number of constituencies - what is referred to as "triple bottom line" objective. For instance, all Benefit Corporations must create a "General Public Benefit", defined as "a material positive impact on society and the environment, taken as a whole", which must be assessed against a comprehensive set of "ESG" (Environmental, Social and Governance) criteria. The other type is to define more specific purposes, for example addressing a specific impact, a specific constituency, or an issue that needs entrepreneurial action (Mac Cormac and Haney, 2012; Clark and Babson, 2011).

Shareholder commitment towards purpose

The appraisal of shareholders regarding the long-term strategy of the corporation has a major influence on the capability for top executives to make decisions that consider the best interests of all constituencies (Sandberg, 2011). Therefore, it is essential to require a commitment on the part of shareholders to enforce the discretion of directors and managers to work towards the purpose. To give 'teeth' to this commitment, PPCs suggest it be introduced into key governance documents with legal force, including – if possible – constitutional documents such as articles of association (Social Impact Investment Taskforce, 2014: 30; Levillain 2017). For instance, both SPCs and Benefit Corporations may require a positive vote by two thirds of each class of shares to adopt, change or repeal the

Flexible Purpose or Benefit Corporation statute. Significantly, this commitment also applies to potential buyers of the corporation. For FPCs and Benefit Corporations, the same qualified majority is required to authorize an acquisition or a merger of an FPC or Benefit Corporation if the acquirer refuses to adopt the same corporation form, with the same purposes.

The PPC as a legal form has the explicit objective of providing protection for the purpose, and to protect the directors against derivative suits and other types of pressure from activist investors. The requirement of a super-majority to modify the purpose anchors the mission in the long term, and serves as a protection in a situation of change of control, so long as two thirds of the shareholders do not change at the same time. The legitimacy of directors in following this purpose is thereby safeguarded, even if this purpose leads to decisions that do not maximize short term financial return (Yosifon 2014, Mac Cormac & Haney 2012).

Accountability and assessment standards

Requiring shareholder commitment is not meant to give free rein to executives to prioritize one purpose above the others. To assess whether the corporation's strategy and activities indeed make progress toward a broader set of criteria than exclusively financial ones, new accountability mechanisms must be defined. Similarly to CICs (see above), it could be a requirement that a designated qualified third party (for instance a public regulator) assesses the purpose, or the impact of the companies' activities, to ensure that it pursues a public benefit. A second approach, followed by the Benefit Corporation, is to require companies to choose a third-party assessment standard, which must be independent, transparent and comprehensive, in order to measure these impacts along "ESG" criteria. Numerous Benefit Corporations choose the B Impact Assessment grid, to evaluate their impact. A third approach, relying on transparency and more akin to usual extra-financial reporting mechanisms, is to require corporations to provide specific reports, made accessible to the public, that present the efforts undertaken and expected to achieve their purpose, a breakdown of the tangible results along operational objectives, and a statement of the future strategies to be deployed for the year to come.

Control mechanisms

Embedding the purpose into corporate documents must also serve to make the pursuit of such a purpose legally enforceable, creating new protection rights and new duties for executives. Corporate law requires that corporate documents clarify the rights and responsibilities of corporate governance actors, in particular directors and shareholders, and possibly other non-shareholder stakeholders (including society and the environment at large). Some stakeholders can be granted the right to enforce the specified purpose, and to sue the corporation for breaches of its commitment. Benefit corporations, for example, provide for a "benefit enforcement proceeding", giving shareholders or directors or the corporation itself the right to file a suit whenever the corporation is deemed not to have achieved its purpose. Lastly, dedicated governance can be designed - for example, by creating a second, purpose-oriented board, composed of experts and committed parties and the Board of Directors - to evaluate the corporate strategy and assess the corporation's performance regarding its extended corporate purpose. (Social Impact Investment Taskforce, 2014: 41; Segrestin et al. 2015).

By adopting such features, the social purpose of a for-profit corporation can be embedded in multiple ways and become, in principle, legally enforceable, not only on the shareholders' initiative, but also on the initiative of broader stakeholders. These principles are the basis for various proposals for legal forms of PPCs, such as the recently adopted "Public Benefit Corporation" in Delaware (US), the "Società Benefit" in Italy, and the proposed "Société à Objet Social Etendu" in France (Segrestin et al., 2015).

3.3 Discussion and Conclusions

Slowly but increasingly, concerns are being voiced about the purpose of the modern public corporation and pressures are building to direct it to create long-term sustainable value for its many stakeholders (e.g. employees, customers, suppliers, creditors and shareholders) along multiple timeframes, while at the same time contributing to societal well-being and environmental sustainability (Veldman et al., 2016). In responding to these concerns, we have engaged with the literatures on SE and PPC to provide an extensive review of mechanisms that are intended to improve the alignment of a broader sense of corporate purpose with corporate governance theory and practice.

Unpacking and critically evaluating governance mechanisms, organizational forms and business activities most closely associated with SE, we examined an extensive set of devices capable of establishing, embedding and protecting organizational purpose, the interests of multiple constituencies and time-horizons and "mission drift" in relation to organizational architecture. Beyond the direct description of these various instruments, this exploration showed how these mechanisms can be used as a broad set of means that can help create governance architectures for different types of organizations, including for-profit corporations. By approaching corporate governance as a fundamentally open structure of rights and obligations, the use of specific means - like articles of association, purpose statements, certification, share structures, sets of rights attached to shares, fiduciary duties, reporting standards, incentive structures, and external regulation - can then be used to unpack existing configurations of rights and obligations. It can also provide new configurations that can help embed and protect specific privileges, claims, and protections in the governance architecture of organizations, including for-profit corporations.

Conflicting goals, interests, and time-horizons (Ashta and Hudon 2012, Hai and Daft 2016) are perennial problems when pursuing any organizational target or goal (Mansell, 2013; Selznick, 1949, 1957). But such problems are exacerbated by the hard-wiring of a very limited number of such configurations as 'optimal', and especially after the financial crisis of 2008 showed the limited social and economic utility of this supposed optimality. A view of organizational governance as a fundamentally open structure of rights and obligations offers an opportunity to: question the 'optimality' and 'neutrality' of existing configurations; unpack how these configurations 'hard-wire' the interests of specific constituencies and time-frames; and assess the continuing use of such configurations as the outcome of conscious choices and decisions, rather than as the outcomes of legal or economic necessity.

This approach is underscored by the PPC proposal, which reveals that although existing company law arrangements implicitly provide configurations of purpose, rights, and protections that favour the shareholder constituency, new arrangements might be designed to open different configurations. This view of corporations and corporate law is, as we have shown, based on a highly stylized type of thinking about corporations, corporate governance, and corporate interests, in which underlying discussions about goals, interests, time-frames, and their relevance for specific constituencies are consistently left unaddressed (see also Veldman and Willmott, 2016, 2017). To break out of this shareholder-centric framework, it is necessary to embrace a more expansive approach to corporate governance which centers on the corporation and on management, and which is based on the view of organizational structuring as a fundamentally open set of choices. In opening up the theory and practice of corporate governance, it is necessary to appreciate the asymmetry of corporate law that allocates significant control rights to shareholders (Segrestin & Hatchuel, 2011), thus allowing for marginalizing the long-term interests of stakeholders – from employees, through local and national communities who depend upon the raising of sufficient taxes, to creditors and the environment (Blair and Stout, 2011; Reich, 2016). Accordingly, the landscape of new legal provisions we provide in this chapter demonstrates that changes of corporate policies and representations of corporate purpose are not sufficient to provide a sound framework to protect socially-oriented purposes. Legal changes, for instance through new corporate structures or mechanisms appear necessary. As a result, we advocate a reappraisal of the usual theoretical framework employed to conceive of the corporation.

To this end, it is necessary – socially, politically and environmentally as well as economically – to engage in a broad-ranging discussion of central assumptions behind, coherence between, and outcomes of assumptions between corporate law, finance, management, accounting and economics. Within and between these domains coherent concepts, structures, mechanisms and devices need to be developed further to help assist the generation and distribution of long-term sustainable, socially useful value and to address broad systemic risks, including climate change and growing inequality (Veldman et al., 2016). Our intention in this chapter has been to contribute to this process of opinion formation and policy formulation by highlighting corporate purpose as a normative choice in relation to an array of possible corporate architectures.

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