A purpose-driven theory of the corporation?

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Abstract (171 words)

In the debate on the purpose of the corporation, corporate law plays an important role as the corporate entity, because the owner of the assets, can pursue objectives that differ from those of the shareholders. But can corporations be neutral despite shareholders being the only associates or are they necessarily shareholder-oriented? In this article we show how new profit-with-purpose corporate forms (such as FPC and Benefit corporation) revisit the debate on corporate purpose. These corporate forms confirm that corporate law allows but doesn't protect any corporate purpose. By locking a mission in the charter, they protect alternative purposes while still ensuring managerial accountability. We develop a purpose-driven model of the corporation, which, we argue, generalizes model of the corporation, revives the original corporate model and is more consistent with the managerial function. We also develop further avenue for research in management science.

Keywords: Benefit Corporation, corporate law, corporate purpose, Flexible Purpose Corporation, innovation, management, shareholder value, stakeholder, team production

A purpose-driven model of the corporation?

What is the purpose of the corporation? Doctrines have changed considerably over the last decades (Bradley, Schipani, Sundaram, and Walsh, 1999). Corporate purpose has been a troubling question for generations of corporate scholars and is still a matter of wide disagreement among economists, management scholars, managers and policy makers (Jensen, 2001; Stout, 2013).

Well-known controversies have opposed the advocates of Shareholder Value Maximization (SVM) and the proponents of Stakeholders Welfare (Freeman, Wicks, and Parmar, 2004; Greenfield, 2014; Sundaram and Inkpen, 2004b, 2004c). Against the shareholder primacy, it has been opposed that the firm is a nexus of team-specific assets, invested by various stakeholders, shareholders, who jointly bear the risks and hope to profit from "team production" (Gabrielsson, Huse, and Minichilli, 2007). It has also been shown that legally, rather than attributing ownership of the results to one party (in this case shareholders), the law entrusts it to a neutral third-party entity: the corporation, whose purpose can be various and not limited to the interests of shareowners (Blair and Stout, 1999; Deakin, 2005; Greenfield, 2014; Stout, 2013).

The problem is however that, if corporate law allows theoretically different and multiple purposes, the possibility is in practice highly contingent and rather limited (Sandberg, 2011): As long as the objectives are in keeping with shareholders' interests, they can be pursued; but this always depends on the shareholders, who may change over time. Directors making decisions that do not maximize shareholder value can fail in their fiduciary duties towards shareholders and fear accusations of "breach of fiduciary duties" (Clark and Babson, 2012; Greenfield, 2008; Millon, 2000; Yosifon, 2014).

In this article, we seek to contribute to the debate on the purpose of the corporate. We think that the introduction of new forms of corporations in the United States in recent years is likely to revive this debate (Clark and Babson, 2012). These new corporate forms, like the Flexible Purpose Corporation (FPC) and the Benefit Corporation (Hiller, 2013), present themselves as *profit-with-purpose corporations*. Although they are very similar to conventional corporations, their charters stipulate that, in addition to profit, they pursue the goal of a general positive impact, or a specific purpose (charitable, environmental, etc.). The duties or directors and the reporting procedures are modified consequently. To be sure, this type of statute represents a tiny minority: it concerns only a small proportion of companies. In and of itself, it does not solve the legal asymmetry problem. Flexible Purpose Corporations (FPCs) and other "for-benefit" corporations are in no way an "end of the history of corporate law" (Hansmann and Kraakman, 2000). But it reframes the debate on corporate purpose in three ways.

Empirically, this type of statute confirms the diagnosis that corporate law is assymetric: while corporate law allows multiple purpose, the new profit-with-purpose businesses show that entrepreneurs may be unsatisfied with current law and seek for techniques to protect specific

objectives against the associates' contingent desires. The new corporate forms, with a lock-in mechanism for their missions, offer a solid basis to revisit the debate on corporate purpose: rather than trying to beat the shareholder value with another measure of welfare (Stout, 2013), it suggests that the purpose of each corporation can be defined locally, as a constitutive basis for corporate contract and governance.

Second, we argue that purpose-with-profit corporations help to conceptualize what we call a "purpose-driven model of the corporation". This model is far broader than the sole case of FPCs or BCs and it is doubly relevant from a theoretical point of view: it revives the historical notion of corporate purpose in law and reconnects with the legal origins of corporations. But it is also more consistent with the management function: when the purpose calls for innovative strategies, corporate officers can neither be seen as agents nor as expert team members: their creative role and the risks it induces for stakeholders is made explicit.

Finally, we argue that the new forms of corporation suggest new avenues for research in management sciences: further research is needed to record the different forms that purpose-driven corporations can take and may have taken in the past, as well as the associated governance mechanisms. Companies also need to be helped in order to establish suitable procedures to define their purpose and evaluate the corresponding strategies.

The article proceeds as follows: in the first section, we briefly outline the terms of the debate between the stakeholder and shareholder views of corporate purpose, stressing the special role played by corporate law in this debate. In the second part, we present the case of the new corporate forms, which confirms both the asymmetry of corporate law and we consider the related implications for the debate on corporate purpose. In the third part, we develop a mission-driven model of the corporation and discuss the scope of this model from a legal and managerial perspective. We conclude by discussing avenues for further research in management science to analyse the different forms that purpose-driven corporations can take and have taken in the past, as well as the associated governance mechanisms.

The ever-blooming debate on corporate purpose

Shareholder value maximization

Shareholder value (SHV) maximization has been been well established today as a normative prescription for corporate governance. Since the work of Milton Friedman (Friedman, 1970), globalization and liberal policies have emphasized contractual freedom and the discipline of markets. Corporate practices have further consolidated the shareholder view of the firm. The SHV objective is now taken for granted in financial management textbooks (Duska, 1997) and in MBA courses (Khurana, 2007; West, 2011). For instance, we find in the handbook of a service law firm for its corporate clients a "primary obligation, above all others, to the stockholders, to maximize the value of the equity of the corporation" (Forrester and Ferber, 2001, p. 10, quoted by (Yosifon, 2014, p. 185).

What is this SHV criterion based on? It originated in economic theories of the firm as the most effective objective to frame its governance. Mainly four factors justify this criterion in the literature:

1.) **Aggregation of interests.** First, shareholder value is argued to be a legitimate criterion from a social point of view: it is said to aggregate the satisfaction of the different parties, as a company only derives shareholder value when it has fulfilled all its contractual obligations towards non-shareholder stakeholders (Fama and Jensen, 1983; Jensen and Meckling, 1976).
2.) **Managers' accountability.** Second, by focusing on the relationship between shareholders and executive officers, the literature has introduced a "principal-agent" setting between shareholders and the top executives: the former mandate top executives to run the company on their behalf monitoring role to the latter. But this delegation allows agents to opportunistically build their own utility at the expense of the principals' utility (Donaldson and Davis, 1991; Jensen and Meckling, 1976). Therefore, the SHV criterion becomes one of the crucial means for minizing agency costs and disciplining the corporate executives' actions through clear evaluations and incentives (Jensen, 2001; Tirole, 2001).
3.) **Managers' motivation.** Third, the managerial role of SHV has been highlighted: the fact of having a clear and measurable criterion is part of the directors' motivation and ability to articulate clear and unifying strategies (Sundaram and Inkpen, 2004b).
4.) **Efficient allocation of residual claims in team production.** Fourth, beyond the relationship between shareholders and executives, the literature has also studied the "team production" (Alchian and Demsetz, 1972). When several individuals take part in the production of the same output, the team functions by putting a monitor in charge of supervising team members' effective contributions and defining their contractual remuneration during negotiations. For the team to be efficient, the monitor needs to have an incentive to perform optimally: hence the principle of a "residual claimant". By having ownership rights on the residual balance ("not of payments to other inputs"), the monitor is incentivized to achieve optimal overall efficiency. In joint stock companies, shareholders delegate this role to the chief executive officers: they remain residual claimants insofar as they can receive dividends only once all the other parties have been remunerated, and are responsible for monitoring the CEO.

The joint welfare of stakeholders

Despite some arguable limits about its representativeness of the collective value creation, generating profit could legitimately be thought to be a source of motivation and evidence of the company's ability to efficiently develop products or services that are useful to society. The SHV criterion, on the other hand, becomes quickly problematic as it influences both strategic choices upstream to generate profit, and the way in which profit is distributed downstream. Critical and counter arguments have been made regarding each of the above factors:

1.) **Aggregation of interests.** If contractual obligations must be mfulfilled and wages paid before any dividend can be paid, there are many reasons to believe that the shareholder value is a factor a misalignement of interests: first, one must keep in mind that any contract can be breached, and employees can be laid off or a factory shut down to increase the company's profits. In this case, shareholder value is derived, without the other parties' interests being met. Second, the shareholder value can be legitimate as a control principle, but not as a corporate purpose (Koslowski, 2000). The results are measured not only in terms of wages or remunerations provided for

contractually; there are numerous impacts, including on parties that do not have a contractual relationship with the corporation. The company is made up of diverse relationships, and is not limited to a nexus of contracts. Considering the variety of impacts the company has on society, stakeholder theory highlights the enormous social and environmental damage induced by strategies steered towards shareholder profitability (Margolis and Walsh, 2003; Scherer and Palazzo, 2007). Therefore, more inclusive criteria of welfare are needed to coordinate stakeholder interests (Evan and E., 1988). Instead of shareholder value, the corporate purpose is to generate sustainable wealth over time (Post, Preston, and Sachs, 2002), and for all its constituencies : it is both the *raison d'être* of the firm and a condition of its lasting existence (Clarkson, 1995; Harrison, Bosse, and Phillips, 2010; Post et al., 2002).

2.) **Managers' accountability.** Second, the agency view focuses on the corporation contract, which binds shareholders to the directors. But the firm is larger than the corporation. And the stakeholder approach is more concerned by the firm, as an organized economic activity, than by its corporate legal structure (Robé, 2011) (Chassagnon, 2014). While the corporate contract asks managers to run the company on behalf of the shareholders, managers must also recognize the stakeholders' multiple investments to make the firm work and they should be accountable to the society as a whole (Deakin, 2005). Besides, the focus on SHV is recognized to have negative influence on performance: it drives managers to make decisions on share prices at the expenses of the long term health of the firm; it focuses on financial performance instead of considering the process of value creation and discourages the building of corporate capabilities (Certo, Dalton, Dalton, and Lester, 2008; Jordi, 2010; Pitelis and Teece, 2009) (Prahalad, 1994). Is a set of indicators richer than the SHV likely to reduce the transparency and accountability required from directors? The criticism is often made that by requiring directors to take all parties' interests into account, stakeholder theory makes it impossible to challenge them: any decision could be justified by its potential impact on at least one stakeholder. "An organization that is answerable to everyone, is actually answerable to no one" (Sternberg, 2000). Boatright argues that the idea of shareholders ultimately being the only ones with the right of scrutiny is a public policy issue (Boatright, 1994). But the law allows for the principle of accountability to be retained, while diassociating the corporation's purpose from that of its directors or shareholders: the corporation is controlled by a board nominated by the shareholders but "insulated" from them (Lipton and Rowe, 2007) (Blair and Stout, 1999). And other "enlightened" criteria can encomposass financial and social obligations of the firm with an emphasis on the long-term sustainability of the firm (Jensen, 2001; Queen, 2014).

3.) **Managers' motivation.** Likewise, the management representation underpinning the SHV criterion is criticized as bearing litte resemblance to reality (Davis *et al.*, 1997; Donaldson and Davis, 1991). Directors have often less self-serving behaviors than pro-organizational ones (Davis *et al.*, 1997). From this perspective, the general welfare can be a more realistic purpose for managers than the shareholder value (Dean, 2001: 94).

4.) **The role of the corporation in the allocation of results in the team production.** Finally, the modeling of team production does not necessarily make shareholders the residual claimants Firstly, other stakeholders bear the risks on gains that are not written in contracts (as proposed by the incomplete contracts theory (Grossman and

Hart, 1986). Furthermore, in the law, shareholders actually own neither the assets, nor the surplus of the firm. And above all, it is legally inaccurate to consider them as executives' principal. Blair and Stout have proposed an alternative model of both team production and the corporate contract. According to them, the different team members are investors but there is no rule to determine how to satisfactorily share joint results. On the one hand, it is difficult to decide on the attribution of profits beforehand, as there is a risk of reducing incentives (resulting in *shirking*). On the other hand, if the rules for sharing are not decided in advance, there is the risk of very expensive *ex post* disputes (resulting in *bargaining*). To agree on a procedure that all consider fair, team members form a public corporation and transfer to this distinct legal entity the ownership of both the assets and the results (Blair and Stout, 1999; (Orts, 2013). Team members thus transfer authority over the allocation of the surpluses to an independent body – a mediating hierarchy in the form of the board of directors (Lan and Heracleous, 2010). Consequently, rather than being in charge of controlling the managers, the board of directors is a third party whose key role is to conduct arbitration between stakeholders and to solve potential conflicts of interests (Hillman and Dalziel, 2003; Lan and Heracleous, 2010). The corporation, with its neutral board, is thus a legal solution to encourage firm-specific investments by the various parties despite the uncertainty and the risks of opportunism.

This latest approach, refered to as the "team production theory of the corporation", challenges the foundations of shareholder value. It also sidesteps the fears usually voiced regarding the "unrealistic" stakeholder theory (Keay, 2010; Sternberg, 2009; Stoney and Winstanley, 2001). And it moves the debates on the purpose of the corporation in the following way: does corporate law offer the possibility to pursue social and environnemental objectives? Or by making sharehdolers the corporation's only contracting parties, does it bind ipso facto companies to shareholder value? In the following section, we analyse the empirical development of new corporate forms to investigate this question.

Profit-with-purpose companies: lessons from the new corporate forms

An empirical movement for legalizing multi-purpose enterprises

In the past years, legislation has been passed to authorize the incorporation of a new form of businesscorporation. In 2012, California was the first state to propose the creation of « Flexible Purpose Corporations » (FPC) or « Benefit Corporations » (BC). Other states had already enacted statutes allowing for the creation of for-profit corporations with a primarily charitable purpose. Today, in the United States alone, the Benefit Corporation has been adopted in 20 States[i] and the Flexible Purpose Corporation (FPC) in two States[ii].

This legal innovations draw upon the movement towards "hybrid organizations" (Battilana and Dorado, 2010), which combine profit-seeking strategies with social welfare objectives (Bromberger, 2011). These organizations bring together in their organizational core social and business goals. For instance, thanks to new organizational forms and new institutional logics, they bring together conventional private equity investors and non-profit organizations around a single project, or they engage in technological research while contributing to the development of local communities. Some authors see in the development of "for-benefit"

enterprises a new era, where stakeholder value will gain ground over shareholder value (Cohen, 2014; Sabeti, 2011).

But the creation of new corporate forms more specifically answers to the institutional, legal and managerial challenges generated by such enterprises (Battilana, Lee, Walker, and Dorsey, 2012). For instance "because the law usually forces a nascent for-benefit to organize as a for-profit or a nonprofit, the enterprise defines itself accordingly" (Sabeti, 2011) 4); and the hybrid nature of for-benefit enterprises also leads to confusion, mistrust, and low credibility among stakeholders. The new laws offer two versions (FPC and BC) of a solution to an identified gap in the corporate laws of many states. For instance, existing law in California permitted formation of for-profit corporations that places interests of shareholders as the primary objective of the. On the contrary, a non-profit corporation in California is mandated to serve public interests and is prohibited from pursuing private gain.

How exactly do the new corporate forms address these challenges ? We first review the main features of BC and FPC before discussing their implications for the purpose of the corporation.

Purpose-driven corporations: main principles

Benefits, as well as Flexible Purpose Corporations, are very similar to classical corporations. Both of the new entities will be taxed the same as for-profit corporations under current tax law. The difference is that the charters or bylaws of these corporations stipulate a purpose different from, and in addition to, profit (Hiller, 2013) (Hemphill and Cullari, 2014; Nass, 2014). This differs from general corporations, which are *allowed* to form for any lawful purpose, but have no explicit purpose requirement.

They resulted from the work of two groups: the proposal of the FPC was written by a group of corporate attorneys from major law firms in California. The proposal of th BC resulted from efforts of B Lab, a non-profit organization that offers certification of corporations as "B corporations" (which B Lab describes as "a new type of corporation which uses the power of business to solve social and environmental purposes"). To simplify and compare these organizations with classical corporations, three distinctive elements characterize profit-with-purpose corporations:

1.) Principle of purpose: the enterprise must first and foremost adopt a particular purpose (or several), whether generic or contingent, in addition to profit. This can be of different types. For instance, the law requires that the special purpose of the FPC be:

> (1) One or more charitable or public purpose activities that a nonprofit public benefit corporation is authorized to carry out; or
> (2) The purpose of promoting positive short-term or long-term effects of, or minimizing adverse short-term or long-term effects of, the flexible purpose corporation's activities upon any of the following:
>> (a) The flexible purpose corporation's employees, suppliers, customers, and creditors;
>> (b) The community and society; or
>> (c) The environment.

In contrast, the mission of the Benefit Corporation is expressed as a "General Public Benefit". More precisely, BCs are *required* to have a purpose of creating "general public benefit" and are *allowed* to identify one or more "specific public benefit" purposes. In California, the general public benefit is defined as a "material positive impact on society and the

environment, taken as a whole, as assessed against a third-party standard, from the business and operations of a benefit corporation." In addition, the law requires that directors take into account the impact of their decisions on the firm's significant stakeholders. A company may also designate a specific public benefit, in addition to its general public benefit purpose. Compared to FPC, a specific public benefit can only come in addition to the commitment to a general public benefit.

2.) ***Mission-lock principle***: Second, profit-with-purpose corporations must adopt a lock-in mechanism for their mission. For instance, both FPCs and Benefit Corporations require a positive vote by two thirds of each class of shares to adopt, change or repeal the Flexible Purpose or Benefit Corporation statute. Once enacted, a flexible purpose is thus a mid- or long-term commitment by the corporation (conversely, statutes may grant rights to shareholders that want to break away from the mission, for example, by ensuring that these shareholders can sell their shares at a fair value when they leave[iii]). Significantly, this commitment also concerns potential buyers of the corporation: for FPCs and BCs, the same supermajority 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.

3.) ***Accountability principles.*** Third, profit-with-purpose corporations can adopt special procedures to evaluate the management of their purpose. To attain the appropriate level of transparency, both Benefit Corporations and FPCs must publish the following results in an annual report made accessible to the public:

- The Benefit Corporation requires a third party evaluation standard. The annual evaluation of the corporation's results regarding its mission must follow that standard.
- FPCs' reports must also include a discussion of the strategies followed during the year, the investments made, and the future strategies to be deployed for the year to come. Additionally, local reports may be required for significant decisions involving a compromise between profit and purpose. The FPC also requires operational objectives to be derived from the special purpose, so that the directors' actions can be evaluated against these objectives.

Discussion: a legal way to unlock the purpose of the corporation?

It is still too early (and beyond the scope of this article) to tell whether these statutes will be appealing and effective in terms of actors' accountability and economic interests. At this stage, very few companies of this nature have been created and it is impossible to tell whether the numbers will increase over coming years. Some weaknesses can already be identified in these reforms: Profit-with-purpose corporations will only ever concern firms whose founder or majority associates are committed to and concerned about their firm's sustainable development. They will therefore not allow for all firms, particularly multinationals, to be made accountable. Moreover, they will only allow for objectives that are clearly desirable and acceptable for the shareholders to be pursued.

It should also be stressed that even if shareholders commit to various objectives, the governance model is still of a "shareholder primacy". While fiduciary duties are relaxed, directors are still appointed by shareowners only and depend on shareholders to adopt or

modify the purposes. Other concerned parties, such as employees or local authorities, are no more able to sue corporate officers than in the case of traditional corporations.

In view of all these issues, there is reason to doubt the actual impact of these new forms of corporations on business practices. Nevertheless, the creation of these new forms critically revisits the debate on corporate purpose.

The "asymmetric" bias in corporation law

The very existence of FPCs and BCs first confirms empircally some biases of the corporate law. In our view, it shows that managers or directors are neither sufficiently « insulated » from shareholder's pressure, nor sufficiently protected against a breach of their fiduciary duties.

Entrepreneurs need FPCs because corporate law does not protect "special purposes" from possible pressure from the board and from shareholders (Gelter, 2009). While team members can form a corporation to pursue various objectives, the structure of corporation is also too imbalanced to protect such objectives (Marens and Wicks, 1999; Yosifon, 2011). As directors are legally accountable to the firm's shareholders (Kaufman and Englander, 2005), the latter are by law given a great power of influence over directors (Greenfield, 2008; Greenwood, 2005; Mayer, 2013): the insulation of "directors" is fragile and political pressures may influence the board's decision making (Millon, 2000). The creation of new corporate forms corroborates the fear that managers can be forced or incentivized to give up social purposes to favor more profitable strategies (Haigh and Hoffman, 2014) or to pursue shareholder interests at the expense of the firm's long-term welfare (Lazonick, 2014), especially in case of takeovers or upon a change of control (Page and Katz, 2010).

Second, the law creates fiduciary obligations for directors with regard to shareholders. Decisions by directors are protected by the "business judgment rule" (BJR)– a legal presumption that a corporate fiduciary has endeavored in good faith to exercise care in pursuing the corporation's interest. The business judgment rule gives directors discretion in deciding how to pursue a corporate objective (Bainbridge, 2004). Normally, it protects directors who take decisions in the interest of the corporation in a broad sense, even when they impact short-term shareholder value. However, the board could still face liability if there is no rational basis for the action in light of the corporation's purpose. To avoid potential liability risks, directors under the traditional corporate model tend to adopt a risk-averse behavior and avoid decisions that could result in mixed benefits to society and shareholders. This may explain why, while nothing legally prevents a company from making SRI investments, in practice these possibilities are limited (Sandberg, 2011). According to the lawyers who designed the FPC :

> "*the business judgment rule does not afford sufficient protection and flexibility to consider social or environmental factors in all decisions*", and "*because the litigation in this area is prevalent, directors and their lawyers tend to apply risk-averse constructions even when judicial guidance favors an expansive interpretation*" (Mac Cormac and Haney, 2012).

The same argument is put forward by the architects of BCs (Clark and Vranka, 2013) :

> "*Many leaders of early and growth-stage mission-driven businesses fear being pressured to change business practices or pursue strategic alternatives to independent growth by investors whose financial interests often diverge over time from the social mission of the company.*

Whatever the letter of the law, these fears, combined with both prevailing business culture and advice of counsel about the risk of litigation on failing to maximize shareholder value, have a chilling effect on corporate behavior as it relates to pursuit of a social mission".

In summary, FPC and BCs confirm former research on the *assymetries of corporate law*: corporate law allows for corporate purpose to differ from shareholder value. But if the shareholders' interests evolve, these corporate purposes are not protected by corporate law.

From generic to local definition of corporate purpose?

Although FPCs and Benefit Corporations differ in their law provisions, they both illustrate a more general purpose-driven model of corporations of "purpose-driven" or mission-locked corporations. In our view, this model successfully resolves the tentsion between board insulation (managerial discreation) and managerial accountability. It thus restores the possibility, for business corporations, to actually pursue objectives that go beyond the shareholder value.

The purpose-driven model first ensures **managerial discretion/safe haven**. The stipulation of one or several purposes has a binding effect on shareholders, as they are committed to giving directors the necessary leeway to achieve the purpose of the corporation. It thus offers a "safe harbor" (Mac Cormac and Haney, 2012) for directors: they are given authority to make decisions within the scope of the purpose. They are also protected against breach of fiduciary duties unless their decisions can be proven to pursue other objectives than those stipulated in the constituent documents. once the purpose is specified it has a binding effect for shareholders, who lose the capacity to sue directors as long as they act towards this purpose. They can no longer file a derivative suit against decisions that do not maximize shareholder value. The directors of the FPC are legally protected for each of their decisions that entails a compromise between profitability and purpose. Likewise, Benefit Corporation shareholders univocally accept that directors take other stakeholders into account while exercising their managerial power. It thus creates a "safe haven" for directors. This is critical for the corporation to pursue objectives that are not directly in line with shareholder value.

The purpose-driven model secondly maintains managerial accountability. The purpose serves as a reference to assess the relevance of managerial decisions and strategic orientations. The discretion granted to directors to act towards the purpose is not blank check for virtually any decision. On the contrary, the specification of a purpose comes with the stipulation of peculiar procedures of control and monitoring. Whether by transparency (as in the case of the FPC) or by *ad hoc* evaluation processes (such as the third-party assessment standard demanded by the Benefit provision), managerial discretion is limited to strategies reasonably advancing the stake of the purposes, and is not open to any decision that would create an hypothetic and unmeasured positive effect on various stakeholders.

In these conditions, the purpose-driven model reliably restores the possibility of various corporate purposes. Since it ensures managerial latitude but maintains accountability, a corporation that defines and embeds particular objectives into its incorporation documents can, if need be, have objectives other than shareholder value.

The purpose-driven model of the corporation thus reappraises the debates between shareholders and stakeholder theorists about the purpose of the corporation. It suggests that

we do not need to specify one single and generic substitute to shareholder value. It may be illusory and even counter-productive to look for a unique definition of corporate purpose. Instead, the purpose-driven model gives the possibility for each company to define its own special purposes: it thus offers a way for the corporation to genuinely become a "multi-functional tool" (Stout, 2013). In this respect, we argue that the purpose-driven model of the corporation deeply revisits the debate on the corporate purpose: instead of trying to beat the shareholder value with another generic criterium, it suggests that the purpose will be better defined and anchored locally. Paradoxically, mission-lock-in could be a way to unlock the rule of sharehoder value.

A purpose-driven model of the corporation: origins and implications

The model of the purpose-driven corporations, as we conceptualize it, consists of the free dimensions we have outlined above :

- **The specification of an explicit purpose**, which replaces or adds to profitability
- **Mission-lock mechanisms** that ensure the commitment of shareholders to the purpose
- **Accountability principles**, which better suit the chosen purpose than financial accounting and control that it is effectively followed.

Although further empirical research is needed to assess the validity and implications of this model in a variery of purpose-driven company cases, we believe that the relevance and general character of this model is supported by two important elements : First, it reconnects with the original model of the "business corporation", as revealed by a historical analysis of the form. Second, it is more consistent with the managerial function and accounts for its innovative role.

Reviving the original model of corporations

A purpose at the heart of the early corporation

The purpose-driven model of the corporation may well not only be found in the newest and latest legal bodies, but also close to the heart of the original model of the corporation. It is indeed now well established in business history that early corporations were fundamentally purpose-driven. Historically, corporations have existed in English law since the 14th century, when Edward III formalized an existing form of association into a legal structure that would be granted a specific royal charter (Fishman, 1985). Corporations were created to unite many individuals into a "*body sharing a common purpose in a common name*" (Trachtenberg, 1982).

The creation of a corporation derived from an act of a sovereign authority; the priviliges stemming from a corporate charter were important for an organization: if incorporated, an organization would survive the death of some of its constituents, as opposed to usual partnerships (Williston, 1888) ; it would have the capacity to hold and grant property, and the capacity to sue and be sued (Kyd, 2006 [1793]). And it would eventually authorize its members to conduct profitable trade within regulated and protected places… Such priviliges and power depended on the specification of a purpose. "*It was assumed, as it still is in nonprofit corporations, that the corporate body earned its charter by serving the public good*"

(Trachtenberg, 1982). Corporations were partly serving private interests, but they were "*conceived as an agency of government, endowed with public attributes, exclusive privileges, and political power, and designed to serve a function of the State*" (Handlin and Handlin, 1945)

The same thinking applied in the chartering of joint-stock companies in the age of exploration and colonization, and later, when they were created mainly to build and operate infrastructures such as roads, canals, and railways. Not only was there no fundamental dichotomy between public interest and private objectives, but the public purpose was also a critical condition for authorizing the creation of new social bodies with extraordinary powers.

The purpose as a control mechanisms

The purpose consenquently served to delineate corporate powers and to control their activites. According to an early 19th century treatise, "*the corporation is confined to the sphere of action limited by the terms and intention of the charter*" (Greenfield, 2001 quoting Angell and Ames). The specific purpose, included in the royal charter, allowed strict scrutiny from the state, and the doctrine of *ultra vires* limited corporations to certain purposes and powers (Greenfield, 2001). Corporations were kept under strict control, which included examination by the crown before a royal charter could be issued for each corporation to operate, a strict overview of the accumulation of property, and a right of visitation, which is the right of specified "proper persons to visit, inquire into and correct all irregularities that arise in such corporations" (Blackstone and Field, 1827 [1765]).

The specification of a purpose also protected shareholders. Greenfield (2001) explains that the *ultra vires* doctrine limited the uses to which shareholders' equity capital could be put and was thus seen as a mechanism for the protection of shareholder interests that was "essential for the protection of the investing public" (Greenfield, 2001: 80). The underlying idea was that shareholders made investment decisions based in part on the scope of permissible business activities in which a corporation could engage. The specific activities listed in the corporate charter were therefore considered to be an important part of the "contract" between shareholders and the firm (and its management). It was assumed that shareholders cared about which activities the firm engaged in, and if it went beyond the activities specified in the corporate charter it was a violation of the firm's contractual duty to the shareholders. The *ultra vires* doctrine thus protected shareholders by ensuring that corporations kept within the bounds of business, as enumerated in the articles of incorporation (*Ibid.* p.81). This limitation on the corporation's activities was enforced even when the unauthorized venture was likely to be profitable (*Ibid.* p.82).

The progressive disappearance of purpose

We have historical evidence that in early corporations qualifying the purpose was key to combining corporate power and corporate control. What has happened since is also well documented: the corporation has progressively been authorized not only for public interest but also for private purposes. The State of New-York, for example, was the first to provide a "general incorporation statute". In 1811 this status was available only to corporations manufacturing textiles, glass, metals and paint. Connecticut (1837) and Iowa (1846) were the first states to sign legislation permitting the formation of a corporation for any lawful,

specified purpose, but general incorporation was common before the end of the nineteenth century. "Allowance by states of general incorporation resulted in explosive growth in corporations for private business purposes and to erosion of state attempts to proscribe their behavior through the *ultra vires* doctrine" (Sundaram and Inkpen, 2004a). Before the end of the 19th century, the *ultra vires* doctrine was dead, at least in state courts (Hovenkamp, 1991). As a result, business companies became incorporated, as did Philip Morris, for instance, *"to transact any lawful business."* This promptly cleared the way for the notion of managing the corporation for shareholders' profits.

Although the *ultra vires* doctrine has essentially disappeared from contemporary corporate law, the corporation is deeply rooted in a purpose-driven model presented above. And we further argue that this model may account for the managerial function much better than the classical view of the corporation

Accounting for the function of the executives

The model of purpose-driven corporation may also be a way to restore in law the managerial function. The figure of director is currently defined in broad terms. As the Deleware Code puts it, "the corporation's business and affaires "shall be managed by or under the direction of a board of directors"; directors have supposed to have fiduciary duties and to be protected by the Business Judgment Rule. But this basic framework leaves room for heterogenous approaches of management: reacting agains "managerialism" and the figure of autocratic managers as goal-setters (Selznick, 1957), shareholder supremacists have modeled managers as "agents" of shareowners, in charge only of executing the plans of their principals. In this view, the managerial authority derives from the delegation of the property rights of the investors. Conversely the team production theory sees managers as "bona fide team members" endowed with distinct managerial competencies (Lan and Heracleous, 2010). Blair and Stout distinguish then the role of the board, with a mediating function, and the role of management.

The purpose-driven model of the corporation invites to take into account another dimension of managerial function: the function of capability building and value creation (Pitelis and Teece, 2009; Prahalad, 1994). Their role is to design new strategies to renew and develop the firm assets and capabilities (Castanias and Helfat, 1991, 2001; Hatchuel, Starkey, Tempest, and Masson, 2010; Segrestin and Hatchuel, 2011). The specification of a purpose introduces the possibility of innovative or "unknown" objective, i.e. objective which push "beyond the known" (Leonard-Barton, 1992), and asks for new and disruptive strategies (Bower and Christensen, 1995). For instance, if the purpose is to foster energy transition, managers will need to generate new strategies). Thus, stipulating a purpose may explicit the role and status of managers in the governance framework:

- Managers are note simple "agents": they are mandated not to execute a plan, but to invent new collective strategies to achieve disruptive objectives. Consequently, their authority comes not only from the delegation of the control right upon some assets, but from their creative capabilities. Knight for instance noted that uncertainty leads to the

  > "tendency of the groups themselves to specialize, finding the individuals with the greatest managerial capacity of the requisite kinds and placing them in charge of the work of the group, submitting the activities of the other members to their direction and control" (Knight, 1921).

  Shareholders nominate managers because they believe that managers are the agents most capable of *inventing* strategies to fulfill the corporate purposes.

- Compared to “experts”, managers are entitled also to invent and implement new strategies with potentially unknown effects. This means that risks bear by team members result less from opportunism than from the managerial decisions. To account for the related risks is crucial in order to have responsible and balance team management.

To summarize, the specification of a mission, especially when it is innovative, makes visible the creative role of managers as opposed to their position of agents. Managerial legitimacy is unseperable to the necessity to engage new collective endeavour and to invent new strategic uses of assets. But it also makes visible the risks induced by management upon stakeholders. In our view, the purpose-driven model of the corporation can ingrains corporate law with a view of management that is more consistent both with the foundations and effects of managerial authority. It can both legitimate but delineate the discretionary power of managers, in the manner as the *ultra vires* tradition.

This view, we assume, could favors the development of innovative capabilities and support the economic efficacy of the firm. As noted earlier, an exclusively profit-oriented firm will tend to favor strategies with rapid and preferably quite probable returns, rather than pure exploratory strategies. It will find extremely difficult to invest in long-term and uncertain research. The specification of a mission can facilitate the collective engagement into uncertain and innovative strategies as conditions are gathered to build trust : the purpose-driven model of the corporation provides guidance and control for managerial action, even with disruptive strategies. Further research is required to test such an hypothesis.

Concluding discussion and avenues for further research

The introduction of new corporate forms, such as FPCs or BCs, pertains to a more global movement of reforms that have been undertaken in several places to counterbalance the asymmetry of corporation law. For instance, the *constituencies statutes* introduced in parts of the United States in the 1980s explicitly allow directors to take into consideration the interests of constituencies other than stockholders (Bainbridge, 1992; Orts, 1992). They extend the range of permissible concern by boards of directors to other parties, including employees, creditors, suppliers, customers, and local communities (Donaldson and Preston, 1995)[1]. The recent UK Company Act of 2006 also requires managers to consider the impact of their decision upon the various constituencies (Sternberg, 2000). The law thus introduced the “duty to promote the success of the company, for the benefit of its members as a whole” (sec. 172(1)(b)) (Keay, 2007). It was beyond the scope of the paper to examine whether the new corporate forms can have more or different impact than former reformative legislation. Neither have we tried to discuss the barriers or the needs to the adoption of such legal frameworks by other legislations. We have focused on the theoretical implications of the legal

[1] A similar statute was adopted by the California State Assembly and Senatein 2008, but later vetoed by the governor. Had this statute been promulgated, directors' duties would have been extended far beyond shareholders’ mere financial interests. The governor’s letter of veto mentioned that such a provision could have "unknown ramifications" for a large number of organizations, and thus created a risk that directors acquire a discretion broad enough to promote their own interests at the expense of both the corporation and its stakeholders.

innovations for corporate law and for governance. But future research will have to study more thoroughly the real developments, limitations and effects of such reforms.

Clearly the stipulation of a purpose in the corporate charter is not a guarantee of good governance. Many examples illustrate the contrary. Were the housing-finance giants Fannie Mae and Freddie Mac not both government-sponsored entities that were purpose-driven? They were designed and government-sponsored to facilitate housing finance. But as Levine has demonstrated, "while facilitating housing is a *raison d'être*", these companies have used their mission and their privileged positions to earn substantial profits with increasingly and excessively risky investments (Levine, 2010). Therefore, a special attention will have to be paid to the actual governance of FPCs and BCs. It is necessary to assess both the weaknesses and the governance principles required to meet the expectations not only from the state's or the shareholders' point of view, but also from that of the different constituencies. To what extent the legal framerwoks sufficient to guide the governance of purpose-driven business? And if additional principles are needed, to what extent are they contingent to the type of purpose?

Another stream of research will be also needed on the purpose-driven model of the corporation: it is, in our view, highly generic as it stretches far beyond the cases of FPCs or Benefit Corporations. In this respect, it is likely to encompass many cases of current or past firms, beyond the formulas sanctioned by the law. Many contemporary cases could be referred to as purpose-driven corporations without being considered as FPCs or Benefits. Most cases of "hybrid organizations", such as commercial micro-finance organizations (Battilana and Dorado, 2010) and others (Cooney, 2006), do not have a specific governance structure and do not meet the specifications of the purpose-driven corporations. Conversely, we can fin different past and contemporary companies have experimented original governance schemes to lock in and protect a specific mission. For instance, the Danish pharmaceutical company Novo Nordisk, founded with a mission "to rid the world of diabetes (…) is a publicly traded operating company that is controlled by a foundation – which prevents hostile takeovers, enables executives to focus on the long term, and allows profits to be used for humanitarian purposes" p. 6 (Sabeti, 2011). Another similar, historical example is the Carl Zeiss Company, well known not only for being a leading pioneer in embracing strong social responsibility very early on (Glatzee, 1913; Weiss, 1949), but also for experimenting with science-based management (Buenstorf and Murmann, 2005; Kogut and Zander, 2000). Interestingly, in the late 19th century, the control of the Carl Zeiss Company was transferred to a foundation (*Stiftung*), whose constitution defines a whole series of rules for administration. These rules, in our view, perfectly exemplify the mission-driven model of the corporation (Segrestin and Hatchuel, 2014), albeit very different from those of FPCs or BCs. The table below details the dimensions of the purpose-driven companies in the case of Carl Zeiss Company according to the incorporation documents of 1896.

Attributes of purpose-driven companies	The Carl Zeiss company
Profit-with-purpose principle	The business, as stipulated in the first article of the foundation's constitution, must be run with the following objective, to "cultivate the branches of precise technical industry" (…) for the "service of scientific and practical interest".
Lock-in principle	The mission is fixed and cannot be revised. Capital is transferred to a single owner, the *Stiftung*, whose mission is anchored in its

	constitution. As a result, this "impersonal ownership" grants the company a very stable orientation
Accountability principle	The constitution explicitly provides significant latitude to managers, who are not revocable. Managers must be competent and work with a collegial group. But the constitution defines detailed rules for controlling them. For instance, it is specified that during the exercise of their mandate, managers shall report to the board of the *Stiftung*, which includes representatives of local government. They should report according to specific criteria, such as the *"Wirtschaftlicher Gesamtertrag"*. This criterion indicates that investment decisions shall not be made only according to their potential financial returns but, more fundamentally, according to their potential learning pay-off.

As the few examples above show, the purpose-driven model can be broken down into many different forms:

- Different types of purpose (generic, specific, with or without authorization) and different procedures to approve/review the purposes (as the sole remit of shareholders or involving the opinion of other parties or the State, etc.)
- Different lock-in procedures (for example with a foundation that is the sole shareholder and is devoted to a specific and non-reviewable mission)
- Different evaluation procedures (with a report produced by the classical board, by management, by a third-party organization or by an expert committee, or entrusting management reporting to employees, as is the case in Germany where the supervisory board includes employee representatives).

Thus far we lack the knowledge and research needed to characterize the relevance and efficiency of the mechanisms. Should lock-in mechanisms depend on the type of purpose? Are there some contingent criteria? What are the best combinations and the contingent risks for each of them? The diversity of cases should be explored both in historical cases and also in the range of further possibilities.

Finally, our research reveals that what we know about management and managerial value-creating functions does not necessarily match the dispositions of corporate law. A careful analysis of the adequacy of management theory and corporate law would certainly be useful to ensure that management is exercised in an efficient and fair way.

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[i] See http://benefitcorp.net/state-by-state-legislative-status
[ii] Counting a variant called Social Purpose Corporation in the State of Washington, as presented in Battilana, "Hybrid Ideal," 53
[iii] It is the principle of the dissenter's rights respected by the Californian legal forms.