GOLDEN SHARES AND SOCIAL ENTERPRISE

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Social enterprises—for-profit companies with public-interest missions—are now ubiquitous, yet few have emerged from the realm of small business. The main obstacle to their growth is a gap in trust between managers and investors, with each side lacking any legal assurance that the other will pursue both profits and purpose. Too often, these misgivings limit businesses' access to capital.

Beyond new legal forms created to accommodate this sector, some social entrepreneurs have adopted inventive organizational structures as part of a growing global movement called steward ownership. Among the first structures in the United States is the golden share model, in which a Delaware public benefit corporation with dual-class stock grants all voting rights to managers, all economic rights to investors, and critical veto rights to an independent foundation.

This Article is the first to address this movement and its potential to advance social enterprise. The golden share model begins to close this sector's trust gap from one side, by assuring managers that investors cannot divert a company from its mission. But from the other side, the gap may widen even further, as investors worry that managers will ignore that mission and abuse their unchecked authority.

To bridge this gap, novel applications of established industry practices and familiar legal concepts, like impact metrics and voting trusts, could vastly improve the model. With these practical proposals, social entrepreneurs could retain independence in pursuing their missions, while attracting the capital needed to achieve them at scale.

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Introduction

One of the nation's most famous social enterprises is Etsy, a "global marketplace for unique and creative goods."[1] From its founding in 2005, the company had a mission "to reimagine commerce in ways that build a more fulfilling and lasting world,"[2] as a conscientious alternative to consumerist juggernauts like Amazon and eBay.[3] Lauded for its commitment to the public interest,[4] Etsy quickly succeeded in establishing a vast network of sellers and buyers of handcrafted goods.[5] In addition, its idealism and thoughtful employee benefits attracted passionate workers who reported remarkable satisfaction rates despite earning lower salaries than they could elsewhere.[6]

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[1] Etsy, *About*, https://www.etsy.com/about (last visited Sept. 17, 2021).

[2] Chad Dickerson, *Etsy's Next Chapter: Reimagining Commerce as a Public Company*, Etsy News (Apr. 16, 2015), https://blog.etsy.com/news/2015/etsys-next-chapter-reimagining-commerce-as-a-public-company.

[3] Adele Peters, *Will Etsy Keep Its Commitment To Social Good After Its Management Shakeup?*, Fast Company (May 4, 2017), https://www.fastcompany.com/?40418325/?will-etsy-keep-its-commitment-to-social-good-after-its-management-shakeup.

[4] Ofer Eldar, *The Role of Social Enterprise and Hybrid Organizations*, 2017 Colum. Bus. L. Rev. 92, 165 (2017).

[5] Taylor Majewski, *A brief history of ETsy on its 10th Anniversary*, Built in NYC (Nov. 5, 2015), https://www.builtinnyc.com/2015/11/04/brief-history-etsy.

[6] Norman D. Bishara, *Hybrid Entities and the Psychological Contract with Employee-Stakeholders*, 22 U. Pa. J. Bus. L. 303, 333–34 (2020); David Gelles, *Inside the Revolution at Etsy*, N.Y. Times (Nov. 25, 2017) (noting that Etsy employees often "turned down higher salaries from other companies").

At the same time, Etsy accepted tens of millions of dollars in venture capital financing, inevitably creating pressure for an initial public offering ("IPO").[7] This finally occurred in 2015,[8] presaging profound changes to the organization. At first, Etsy's leadership insisted that it could continue its commitment to social responsibility as a publicly traded company.[9] Indeed, shortly after its IPO, Etsy earned an exceptionally high score when renewing its B Corp Certification,[10] which is awarded to social enterprises based on a numerical assessment of their "positive impact on [their] workers, community, customers and environment."[11]

But in 2017, in response to investor complaints of poor sales growth, Etsy's board of directors fired its longtime chief executive officer.[12] They replaced him with a former executive of eBay,[13] one of the e-commerce titans from which Etsy had originally sought to distinguish itself. From a financial perspective, Etsy's change of direction has clearly succeeded. After a sustained and precipitous drop following the IPO, its stock price has increased by over 2,100 percent since the new CEO's appointment,[14] compared with only an 87 percent increase in the S&P 500 index,[15] which Etsy joined in 2020.[16]

But in the process, at least to some observers, the distinctive qualities associated with Etsy's social mission have disappeared, leaving the company "barely recognizable."[17] Its original, elaborate mission statement was replaced with the perfunctory phrase, "keep commerce human," and the "Value-Aligned Business" team that oversaw that mission was disbanded.[18] Confronted with management's increasing emphasis on profits, many employees lost enthusiasm for the company and no longer felt encouraged to express their feelings openly.[19] Etsy eventually let its B Corp Certification

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[7] *See* Gelles, *supra* note 6.

[8] *Id.*

[9] Dickerson, *supra* note 2.

[10] Peters, *supra* note 3.

[11] B Lab, *Certification Requirements*, https://bcorporation.net/certification/meet-the-requirements (last visited Sept. 17, 2021). Despite their similar names, a B Corp is different from a benefit corporation; the first is a private certification awarded by a nonprofit organization, and the second is a type of legal entity created by state law. For details about benefit corporations, see *infra* Part I.B.

[12] Gelles, *supra* note 6.

[13] *Id.*

[14] *ETSY Historical Data*, Nasdaq, https://www.nasdaq.com/market-activity/stocks/?etsy/historical (last visited Sept. 17, 2021). Josh Silverman was appointed as President and CEO effective May 3, 2017. Etsy, Inc., Current Report (Form 8-K) (Apr. 30, 2017).

[15] *SPX Historical Data*, Nasdaq, https://www.nasdaq.com/market-activity/index/?spx/historical (last visited Sept. 17, 2021).

[16] Mira Reyes, *Etsy to join S&P 500*, S&P Global Market Intelligence (Sep. 7, 2020), https://www.spglobal.com/marketintelligence/en/news-insights/latest-news-headlines/etsy-to-join-s-p-500-60237643.

[17] Gelles, *supra* note 6.

[18] *Id.*

[19] *Id.*

lapse to avoid a requirement to legally transform into a benefit corporation,[20] which would have mandated that directors consider the company's social mission in their decisions.[21] Moreover, the company "generated significant controversy when it" engaged in "aggressive techniques to avoid paying taxes," which appeared to contradict its commitment to the public good.[22] Beyond legal issues, perhaps Etsy's most fundamental change was to its core business; though it started as a haven for handmade items by individual sellers, users began complaining that the site had become "flooded" with "mass-produced goods."[23]

Through these developments, Etsy went from a darling of the social enterprise sector to "a cautionary tale for social entrepreneurs,"[24] a parable of "mission drift,"[25] and "a case study in how the short-term pressures of the stock market can transform even the most idealistic of companies."[26] Some attribute this alleged failure to Etsy's "corporate structure."[27] By granting control to outside investors through venture capital financings and then a public offering, managers could no longer steer the company toward the public-interest mission that they had originally envisioned. As in many social enterprises, they faced "a fundamental tension between the need . . . to achieve liquidity for themselves and investors and the desire to maintain their companies' missions and values."[28]

To prevent the perceived fate of wayward social enterprises like Etsy from befalling the multitude of less famous mission-driven entrepreneurs, a growing global movement is advocating "steward ownership."[29] Rather than one approach, steward ownership consists of several different organizational structures and policies intended to "secure a company's mission and integrate independence into its legal DNA."[30] Applicable structures vary across countries, and one of the first in the United States is called the golden share model.[31] Starting with a Delaware public benefit corporation ("PBC"), this

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[20] Elizabeth Schmidt, *New Legal Structures for Social Enterprises: Designed for One Role but Playing Another*, 43 Vt. L. Rev. 675, 717–18 (2019).

[21] *See infra* text accompanying note 67.

[22] Brett H. McDonnell, *Benefit Corporations and Public Markets: First Experiments and Next Steps*, 40 Seattle U. L. Rev. 717, 729 (2017).

[23] Gelles, *supra* note 6.

[24] Bishara, *supra* note 6, at 333.

[25] Juho Makkonen, *How to build companies that are a force for social good, in* Purpose Foundation, Steward-Ownership: Rethinking ownership in the 21st century 59 (Josh Raisher ed., n.d.), https://purpose-economy.org/file/364.

[26] Gelles, *supra* note 6.

[27] Makkonen, *supra* note 25, at 59.

[28] Purpose Foundation & RSF Social Finance, State of Alternative Ownership in the US: Emerging Trends in Steward-ownership and Alternative Financing 12 (2019), https://perma.cc/W2JK-JLWA.

[29] Brown et al., Mapping the State of Social Enterprise and the Law 2018–2019, at 21 (2019), https://socentlawtracker.org/wp-content/uploads/2019/05/Grunin-Tepper-Report_5_30_B.pdf.

[30] Makkonen, *supra* note 25, at 59.

[31] Purpose Foundation, Steward-Ownership: Rethinking ownership in the 21st century 17 (Josh Raisher ed., n.d.), https://purpose-economy.org/file/364.

approach divides equity into multiple classes, vesting all control rights in management and all economic rights in investors, while empowering an independent "golden shareholder" to veto sales of the company, changes in its social mission, and certain other transformations that could undermine that mission.[32] Thus insulated from outside investors' pressure to focus on profitability and provide a lucrative "exit," social entrepreneurs could supposedly remain committed to the public interest.

In recent years, social enterprise has been among the most prevalent topics in business law scholarship, with many authors proposing various legislative changes to overcome this sector's continued challenges.[33] But some of the same commentators acknowledge that the potential for state lawmakers to enact their proposals is "dishearteningly small."[34] Without new legislation, private ordering by social entrepreneurs and investors would constitute a far more realistic solution to their problems.[35]

Steward ownership and the golden share model purport to provide just such an answer, based entirely on existing laws. These arrangements implicate not only the literature on social enterprise but also several other areas of close scholarly attention, from dual-class stock structures and nonvoting shares to bankruptcy laws and impact investment contracts. Yet to date, no academic publication has analyzed steward ownership or its potential to advance the field of social enterprise. If the emerging golden share model can legally and practically overcome the central challenges of social enterprise, then both scholars and practicing attorneys should consider its potential to

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[32] For more details regarding the golden share model's capital structure, see *infra* Part I.D.

[33] See, *e.g.,* Dana Brakman Reiser & Steven A. Dean, Social Enterprise Law: Trust, Public Benefit, and Capital Markets 25–51 (2017) (proposing the "mission-protected hybrid" as "an ideal legal form for social enterprises"); Dana Brakman Reiser & Steven A. Dean, *SE(c)(3): A Catalyst for Social Enterprise Crowdfunding*, 90 Ind. L.J. 1091, 1093 (2015) (proposing "a tax regime designed to comfortably accommodate a double bottom line"); Ofer Eldar, *Designing Business Forms to Pursue Social Goals*, 106 Va. L. Rev. 937, 937 (2020) (proposing "a social enterprise legal form that draws on the legal regime for community development financial institutions (CDFIs) and European legal forms for work-integration social enterprises (WISEs)"); Michael A. Hacker, *Profit, People, Planet Perverted: Holding Benefit Corporations Accountable to Intended Beneficiaries*, 57 B.C. L. Rev. 1747, 1747 (2016) (proposing to "amend[ ] benefit corporation legislation to allow state attorneys general to oversee the creation of public benefits"); Brent J. Horton, *Rising to Their Full Potential: How a Uniform Disclosure Regime Will Empower Benefit Corporations*, 9 Harv. Bus. L. Rev. 101, 101 (2019) (proposing "a uniform disclosure regime that will apply to all benefit corporations"); Lloyd Hitoshi Mayer & Joseph R. Ganahl, *Taxing Social Enterprise*, 66 Stan. L. Rev. 387, 439 (2014) (proposing "several modest tax accommodations that could be offered specifically for" social enterprises); Brett H. McDonnell, *From Duty and Disclosure to Power and Participation in Social Enterprise*, 70 Ala. L. Rev. 77, 84 (2018) (proposing "legal reforms that could further encourage representation mechanisms for stakeholders" in social enterprises).

[34] Brakman Reiser & Dean (2017), *supra* note 33, at 51.

[35] For a common example of private ordering in corporate governance, see D. Gordon Smith et al., *Private Ordering with Shareholder Bylaws*, 80 Fordham L. Rev. 125, 127–28 (2011) ("Shareholders in closely held corporations routinely use private ordering in the form of shareholder agreements and other contractual arrangements to impose order on the business of the corporation and to regulate the conduct of its affairs.").

advance a field in great need of innovation. Therefore, a legal assessment of this structure is both timely and valuable.

This Article fills this need as the first to examine steward ownership generally or the golden share model specifically. It identifies the problems currently impeding the expansion of social enterprise and assesses the extent to which this model addresses, ignores, or exacerbates them. To resolve these problems further, this Article proposes substantial, realistic improvements that would ensure a company's commitment to its mission while assuaging outside investors' concerns of mismanagement. Like the existing model, but unlike many scholars' suggestions for facilitating social enterprise, this Article's proposals do not depend on improbable legislative changes but can be implemented immediately based on current laws.

Together, these contributions advance the increasingly prominent discussion of social enterprise in corporate law literature, by clarifying this sector's fundamental obstacles, illuminating a promising way forward, and providing direction for further scholarship. Just as importantly, this Article offers practical guidance to social entrepreneurs and their attorneys in organizing businesses to achieve and sustain public-interest missions in the long term.

Part I begins this discussion by identifying the central challenge of social enterprise: to promote trust between managers and investors so that these companies access sufficient capital to grow beyond the realm of small business. This Part also describes the current state of legal structures intended to accommodate social enterprise, with a focus on the leading form, the Delaware PBC. Despite this form's achievements, it leaves open the trust gap impeding this sector's growth, creating an opportunity for private ordering to close it further.

To explore that possibility, Part I then introduces the concept of steward ownership in general, the golden share model in particular, and their relationships to social enterprise. Based on the corporate filings of existing golden share companies ("GSCs"), it explains this model's complex stratification of rights and obligations across different classes of stock.

Given these detailed and unusual arrangements, Part II assesses the golden share model's achievements, beginning with a fundamental inquiry into its legality in Delaware, the model's intended state of incorporation. Although some of the default model's aspects risk unenforceability, they could readily be adjusted to withstand judicial scrutiny more reliably. Therefore, the model, or at least a modified version of it, passes this essential test of a new organizational structure.

Part II proceeds to identify the golden share model's advantages for social enterprises, beyond the standard Delaware PBC's existing contributions. In terms of the trust gap between managers and investors, this new model offers many assurances to managers that investors will not interfere with the company's direction, including its pursuit of a social mission.

On the other side of that gap, however, Part III explains that the golden share model would not alleviate investors' misgivings of managers' intentions and actions. In fact, it may exacerbate them, primarily by failing to require managers to prioritize the company's social mission and by offering them unchecked opportunities to retain control and extract private benefits. As a result, this model could deter outside investors and threaten to further deprive social entrepreneurs of access to capital. Indeed, these expectations are not merely theoretical, as at least one GSC has reported that its esoteric structure has created significant challenges in obtaining financing.[36]

To address these limitations, Part IV proposes specific improvements to the model, based on novel applications of familiar concepts in corporate law and established practices in impact investment. Most importantly, GSCs could integrate curated impact metrics into their organizational documents to conditionally enable investors to steer a wayward social enterprise back toward its intended public benefit. Mission-driven businesses can readily implement this proposal and others in this Article to retain independence in pursuing social goals, while attracting the capital that they need to achieve those goals at scale. With these advances, an improved golden share model could realize the aspirations of social enterprise and steward ownership more successfully than any existing legal entity alone.

I. Social Enterprise and Steward Ownership

A. *The Challenge of Social Enterprise*

In any venture, an outside investment requires trust between managers and investors.[37] Without that mutual trust, each side may worry that the other will use the money or control flowing from the investment to benefit themselves privately rather than the firm, and these concerns could thwart a deal.[38] Mitigating investors' misgivings, general corporate law imposes fiduciary duties of care and loyalty that require managers to pursue the corporation's interests instead of their own.[39] For additional oversight and control, large investors frequently contract for representation on early-stage compa-

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[36] Brown et al., *supra* note 29, at 30 (reporting that Marleen Vogelaar, founder and CEO of Ziel, said, "it took a lot of time and energy to find investors who would be willing to fund a [GSC]. Many investors were reluctant to agree to a deal structure in which they did not have any voting rights. Investors were also concerned about making a return on their investment.").

[37] For concision, this Article uses the term "manager" to include both directors and officers.

[38] Brakman Reiser & Dean (2017), *supra* note 33, at 11.

[39] *Id.* at 14; Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1280 (Del. 1989) ("[T]he directors owe fiduciary duties of care and loyalty to the corporation and its shareholders.").

nies' governing boards.[40] In turn, incumbent directors can legally employ various contractual and governance mechanisms, such as poison pills and other takeover defenses, to avoid losing control to investors unintentionally.[41] Therefore, even in the absence of mutual trust between managers and investors, legal safeguards may alleviate each side's concerns and encourage outside investment nonetheless.

Unfortunately, these protections do not fully apply to social enterprises.[42] No principle of conventional corporate law requires managers to pursue both a stated social mission and financial returns. In addition, no legal requirement prevents investors who care about that mission from transferring their equity to acquirers who would cause the enterprise to deviate from it. Even takeover defenses would not deter "a sufficiently determined suitor" faced with willing sellers but a resistant board.[43]

Despite corporate law's assurances that managers will not simply use investment proceeds to enrich themselves through self-dealing, investors of all kinds may worry that managers will not pursue both mission and profit in running the company. On one hand, "profit-seeking investors may fear that the firm will forego profits in order to pursue some unverifiable social mission."[44] On the other hand, "impact" investors—those who intend "to generate positive, measurable social and environmental impact alongside a financial return"[45]—often worry about "impact washing," when a company "makes impact-focused claims in bad faith without truly having any demonstrable positive social or environmental impact."[46] For their part, managers

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[40] Constance E. Bagley & Craig E. Dauchy, The Entrepreneur's Guide to Law and Strategy 477 (5th ed. 2018) ("Generally, the lead venture capitalist in a [financing] round will expect a board seat.").

[41] Brakman Reiser & Dean (2017), *supra* note 33, at 14–15. For a more thorough discussion of takeover defenses, see *Defending Against Hostile Takeovers*, Thomson Reuters Prac. L., https://us.practicallaw.thomsonreuters.com/9-386-7206 (last visited Sept. 17, 2021).

[42] This Article uses the term "social enterprise" to refer to a for-profit business that pursues a "defined social mission[ ], whether or not that pursuit increases profits." McDonnell (2018), *supra* note 33, at 79. This usage is consistent with most of the literature on this sector, except that it expressly excludes nonprofit organizations, which some common formulations may include. *E.g.,* Dana Brakman Reiser, *Theorizing Forms for Social Enterprise*, 62 Emory L.J. 681, 681 (2013) (using "social enterprise" to refer to any "organization formed to achieve social goals using business methods"). *See also* Marya Besharov et al., *The Many Roads to Revenue Generation*, Stan. Soc. Innovation Rev., Fall 2019, at 35 (explaining that nonprofits often engage in commercial activities to pursue their missions). Because nonprofits do not have capital stock (e.g., in Delaware they are called "nonstock corporations"), they cannot be GSCs and are outside this Article's scope. Del. Code Ann. tit. 8 § 114.

[43] Brakman Reiser & Dean (2017), *supra* note 33, at 16.

[44] Eldar (2017), *supra* note 4, at 172. *See also* McDonnell (2017), *supra* note 22, at 721 ("Because [social enterprises] may choose to prioritize their social mission over profits if the two conflict, investors may fear that social enterprises will earn lower returns, lowering the return on their investments.").

[45] Global Impact Investing Network, *What You Need to Know About Impact Investing*, https://thegiin.org/impact-investing/need-to-know (last visited Sept. 17, 2021).

[46] Peter O'Flynn and Grace Lyn Higdon, *Is participatory impact investing the antidote to "impact washing"?*, Inst. Dev. Stud. (Sept. 19, 2019), https://www.ids.ac.uk/?opinions/is-participatory-impact-investing-the-antidote-to-impact-washing; *accord* Dean Hand et al.,

may worry that any investor will abandon the company's mission under financial pressure when receiving an attractive purchase offer in the future. These situations could lead to "mission drift," when "social enterprises . . . los[e] sight of their social missions in their efforts to generate revenue."[47]

Therefore, in contrast to traditional businesses, which can raise investment from strangers thanks to legal assurances, social enterprises cannot rely on corporate law alone to facilitate access to outside capital. As a result, one of this sector's central challenges is to promote trust between managers and investors. Before giving money to such a business, investors would like assurances of managers' commitment both to its mission and to profit. In turn, before accepting that money, managers would like assurances that investors will remain committed to that mission and will not cause the enterprise to abandon it to maximize monetary gain.

Without those assurances from each side, social enterprises will have limited access to capital, "consigned to the strategy of limiting ownership."[48] Without the growth that additional capital can promote, those enterprises will struggle to achieve their missions at scale. Unfortunately, mutual trust between managers and investors is still elusive. This may explain why, with a few prominent exceptions,[49] most social enterprises in the United States have remained relatively small, closely held businesses.[50]

B. Legal Structures for Social Enterprise

Scholars and courts have long debated "whether and to what extent for-profit corporations, and their directors, must pursue value maximization for shareholders."[51] The traditional "shareholder primacy" view, enshrined by the Michigan Supreme Court over a century ago, is that "a business corporation is organized and carried on primarily for the profit of the stockholders."[52] About 50 years later, in a landmark essay,[53] the economist Milton

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GLOBAL IMPACT INVESTING NETWORK, 2020 ANN. IMP. INV. SUR. 9 (10th ed. 2020) (reporting the results of a worldwide survey of impact investors, which rated impact washing as by far the biggest challenge facing the impact investment market).

[47] Alnoor Ebrahima et al., *The governance of social enterprises: Mission drift and accountability challenges in hybrid organizations*, 34 RSCH. ORG. BEHAV. 81, 82 (2014).

[48] BRAKMAN REISER & DEAN (2017), *supra* note 33, at 16–17.

[49] Christopher Marquis, *The B Corp Movement Goes Big*, STAN. SOC. INNOVATION REV., Fall 2020 (recounting how the large multinational companies Danone, Laureate Education, and Natura, or their subsidiaries, recently became Certified B Corps).

[50] Eldar (2020), *supra* note 33, at 953 ("[F]irms that are dedicated to the pursuit of social missions are typically closely held firms."); McDonnell (2017), *supra* note 23, at 717 ("Most . . . social enterprises to date, are new, small, and closely held businesses."); Marquis, *supra* note 49, at 25 (citing Cassie Werber, *Danone Is Showing Multinationals the Way to a Less Destructive Form of Capitalism*, QUARTZ (Dec. 9, 2019)) ("95 percent of Certified B Corps are small- and medium-sized companies that have fewer than 250 employees.").

[51] BRAKMAN REISER & DEAN (2017), *supra* note 33, at 28.

[52] Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919).

[53] Milton Friedman, *The Social Responsibility of Business Is to Increase Its Profits*, N.Y. TIMES MAG., Sept. 13, 1970, at 32, 33.

Friedman helped to spread this understanding of corporations beyond that famous case into popular public perception, especially among the business-people subject to its supposed mandate.[54] Until this century, even many legal scholars practically took for granted the maxim that corporations must maximize stockholder value.[55]

Since then, other scholars have challenged this established view, arguing that the business judgment rule permits directors of traditional Delaware corporations to consider social missions and other non-stockholder interests in day-to-day business decisions.[56] Though initially provocative, this perspective has since been widely adopted, up to the nation's highest court.[57]

But even if directors can legally consider non-stockholder interests in routine decisions, they may struggle to exercise that discretion in practice, because only stockholders are legally authorized to elect directors and to enforce their fiduciary duties.[58] Further hindering the more expansive view

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[54] *Greed Is Good. Except When It's Bad*, N.Y. Times: Dealbook Newsletter (Sept 13, 2020), http://www.nytimes.com/2020/09/13/business/dealbook/milton-friedman-essay-anniversary/html. ("It was the essay heard round the world. Milton Friedman's 'The Social Responsibility of Business Is to Increase Its Profits' laid out arguably the most consequential economic idea of the latter half of the 20th century. The essay . . . was a call to arms for free market capitalism that influenced a generation of executives and political leaders."); Taylor Tepper, *Milton Friedman On The Social Responsibility of Business, 50 Years Later*, Forbes Advisor (Sept. 16, 2020), https://www.forbes.com/advisor/investing/milton-friedman-social-responsibility-of-business ("[Friedman's] signature achievement was the near universal acceptance—in the world of business, anyways—of the idea that a public company must maximize profits and shareholder value, above all other goals."); Grant M. Hayden & Matthew T. Bodie, *The Corporation Reborn: From Shareholder Primacy to Shared Governance*, 61 B.C. L. Rev. 2419, 2428–29 (2020) ("By the mid-2000s, the shareholder primacy norm oriented not only academic theory but also boardroom practice."); Lynn A. Stout, *The Toxic Side Effects of Shareholder Primacy*, 161 U. Pa. L. Rev. 2003, 2004 (2013) ("Many, and possibly most, public companies now embrace a shareholder-centered vision of good corporate governance that emphasizes 'maximizing shareholder value' (typically measured by share price) over all other corporate goals.").

[55] *E.g.,* Henry Hansmann & Reinier Kraakman, *The End of History for Corporate Law*, 89 Geo. L.J. 439, 439 (2001) ("There is no longer any serious competitor to the view that corporate law should principally strive to increase long-term shareholder value."); Henry T. C. Hu, *New Financial Products, the Modern Process of Financial Innovation, and the Puzzle of Shareholder Welfare*, 69 Tex. L. Rev. 1273, 1278 (1991) ("The most basic principle of corporate law is that a corporation is to be primarily run for the pecuniary benefit of its shareholders. Apart from the impact of non-stockholder constituency statutes and notions of social responsibility generally, few would disagree with this principle as a general matter.").

[56] *E.g.,* Lynn A. Stout, The Shareholder Value Myth: How Putting Shareholders First Harms Investors, Corporations, and the Public 31 (2012) (explaining that, except "when a public corporation is about to stop being a public corporation" pursuant to a merger or acquisition, the business judgment rule grants directors "a remarkably wide range of autonomy in deciding what to do with the corporation's earnings and assets . . . even if the result is to decrease—not increase—shareholder value").

[57] *See* Burwell v. Hobby Lobby Stores, Inc., 573 U.S. 682, 711 (2014) ("[M]odern corporate law does not require for-profit corporations to pursue profit at the expense of everything else, and many do not do so.").

[58] Hayden & Bodie, *supra* note 54, at 2436 ("[T]here are no governance structures in place to ensure that actual directors . . . manage the firm for all constituents. . . . [T]he ultimate check on the board is left in the hands of the shareholders alone."); Leo E. Strine, Jr., *Making It Easier for Directors to "Do the Right Thing"?*, 4 Harv. Bus. L. Rev. 235, 237–41

of corporate purposes, certain language in recent Delaware Court of Chancery opinions may suggest, at least when taken out of context, that corporations must prioritize stockholder interests.[59] Some of these statements are arguably dicta that are incidental to the courts' rulings and do not bind future decisions.[60] In addition, they could be read to apply only to defensive actions taken against minority stockholders, not to more general business decisions.[61]

Of course, these nuanced legal arguments may not comfort a corporate director worried about stockholder derivative suits. Nevertheless, after decades of believing and preaching the gospel of shareholder primacy,[62] the leaders of the country's largest businesses now finally acknowledge that corporations are permitted, perhaps even obligated, to pursue goals other than maximizing stockholder value.[63]

Responding to these developments in legal scholarship, jurisprudence, and business administration, most state legislatures in the United States have recently created "hybrid" business entities of various kinds intended to promote social enterprise.[64] By far the most popular are benefit corporations,

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(2014) (claiming that, even if "those who manage public corporations may, outside of the corporate sales process, treat the best interests of other corporate constituencies as an end equal to the best interests of stockholders, . . . American corporate law makes corporate managers accountable to only one constituency—stockholders").

[59] eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1, 34 (Del. Ch. 2010) ("The corporate form . . . is not an appropriate vehicle for purely philanthropic ends, at least not when there are other stockholders interested in realizing a return on their investment. . . Having chosen a for-profit corporate form, the . . . directors are bound by the fiduciary duties and standards that accompany that form. Those standards include acting to promote the value of the corporation for the benefit of its stockholders."); Virtus Capital L.P. v. Eastman Chem. Co., No. CV 9808-VCL, 2015 WL 580553, at *16 (Del. Ch. Feb. 11, 2015) ("The directors of a Delaware corporation . . . owe fiduciary duties of loyalty and care to the corporation, which require that the directors exercise their managerial authority on an informed basis in the good faith pursuit of maximizing the value of the corporation for the benefit of its residual claimants, *viz*., the stockholders.") (citations omitted).

[60] David A. Wishnick, *Corporate Purposes in a Free Enterprise System: A Comment on eBay v. Newmark*, 121 YALE L.J. 2405, 2417 (2012) ("Future interpreters should read *Newmark*'s 'mandatory' language as dicta because the opinion offers two grounds for rescission of the poison pill that do not require inquiry into the definition of 'proper corporate purposes.' ").

[61] BRAKMAN REISER & DEAN (2017), *supra* note 33, at 30 ("Like *Dodge*, *eBay* can be read as staking out protections for minority shareholders rather than imposing generally applicable rules on the proper objectives for a for-profit corporation.").

[62] *See supra* note 54 and accompanying text; Business Roundtable Redefines the Purpose of a Corporation to Promote 'An Economy That Serves All Americans,' BUS. ROUNDTABLE (Aug. 19, 2019), https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans ("Since 1978, Business Roundtable has periodically issued Principles of Corporate Governance that include language on the purpose of a corporation. Each version of that document issued since 1997 has stated that corporations exist principally to serve their shareholders.").

[63] Business Roundtable, *supra* note 62 (stating that "[w]hile each of our individual companies serves its own corporate purpose, we share a fundamental commitment to all of our stakeholders," including "customers," "employees," "suppliers," "the communities in which we work," and lastly "shareholders," and "commit[ing] to deliver value to all of them, for the future success of our companies, our communities and our country.").

[64] SOCIAL ENTERPRISE LAW TRACKER, https://socentlawtracker.org (last visited Sept. 17, 2021).

with the Delaware PBC becoming the predominant variety.[65] Even for those who believe that traditional corporations can legally pursue public-interest initiatives, the PBC legislation does make a difference. In contrast to general corporate law, this legislation's main contribution is to *require*, not simply to *permit*, directors to consider a social mission in their business decisions.[66] More specifically, directors must "[balance] the pecuniary interests of the stockholders, the best interests of those materially affected by the corporation's conduct, and the specific public benefit or public benefits identified in its certificate of incorporation."[67] At least biennially, the corporation must report to stockholders regarding its promotion of those interests and benefits.[68] In addition, to enforce directors' balancing obligation, the holders of at least two percent of a corporation's shares may bring a derivative lawsuit against the directors on the corporation's behalf.[69]

Despite these additions to general corporate law, the PBC statute does not solve the central challenge in social enterprise of promoting trust between managers and investors. On one hand, directors must only *consider* public benefits, not prioritize them.[70] Mere consideration does not assure investors that management will ever really act toward achieving those benefits,

[65] Brakman Reiser & Dean (2017), *supra* note 33, at 65 (stating that, among the available legal structures for social enterprise, "[a] betting person . . . would wager on Delaware's public benefit corporation"); David Nows & Jeff Thomas, *Delaware's Public Benefit Corporation: The Traditional VC-Backed Company's Mission-Driven Twin*, 88 UMKC L. Rev. 873, 874 (2020) (stating that, among "new hybrid entities," the Delaware PBC "is quickly becoming *the* standard"); Jen Barnette, *So You Want to be a "B Corp" – What Does that Mean?*, Cooley Go, https://www.cooleygo.com/b-corp-what-does-that-mean (last visited Sept. 17, 2021) ("While some version of the benefit corporation has been adopted in 30 states and the District of Columbia, the Delaware Public Benefit Corporation, or PBC, is quickly becoming the gold standard given the integration into the Delaware corporate code."). For salience and concision, this Article addresses only the Delaware model as a representative example. Although Delaware PBCs and other states' analogs differ in many respects, most of this Article's analysis applies to all these forms regardless of those distinctions. For a comparison between the Delaware PBC and other states' models, see Nows & Thomas, *supra*, at 882–884.

[66] Hayden & Bodie, *supra* note 54, at 2438 ("The signal change from corporation to benefit corporation is its rejection of the shareholder primacy norm for a more socially-beneficial corporate purpose."); McDonnell (2017), *supra* note 22, at 734 ("The central legal innovation of benefit corporations is the statutory formulation of fiduciary duties to explicitly require that directors and officers consider not just the financial interests of shareholders, but also the interests of a wide range of corporate stakeholders."); Strine, *supra* note 58, at 243 (explaining that various provisions of the Delaware PBC statute "create a mandatory, enforceable duty on the part of directors to consider the best interests of corporate constituencies and those affected by the corporation's conduct when they make decisions").

[67] Del. Code Ann. tit. 8 § 365(a).

[68] *Id.* at § 366(b).

[69] *Id.* at § 367. Regarding stockholder derivative actions more generally, *see id.* at § 327.

[70] Brakman Reiser & Dean (2017), *supra* note 33, at 68–69 ("[P]ublic benefit must be an ever-present factor in directors' decision-making—one they could not forsake at every turn. But so too with shareholders' pecuniary interests and the mysterious 'interests of those materially affected by the corporation's conduct.' The statute plainly does not give public benefit precedence.").

beyond simply discussing those goals in board meetings.[71] Moreover, the prospect of a derivative lawsuit would not ameliorate these concerns, given the high costs and limited remedies associated with these actions.[72] The biennial reporting requirement offers little solace; in fact, facing an expensive compliance burden and no practical consequence for noncompliance, most PBCs do not even produce the required reports.[73] On the other hand, if profiteering investors eventually hold—individually or collectively—a majority of voting shares, then managers may worry that those investors will cause the enterprise either to neutralize the specific public benefit stated in its charter or to abandon the PBC form altogether.[74] With or without such a formal transformation, each side may worry that others will eventually sell their shares to outsiders who will cause the company to sacrifice that mission by pursuing profit alone.

Therefore, though intentional, the PBC form's flexibility may impede the successful union of like-minded social entrepreneurs and impact investors.[75] To address this deficiency, various scholars have called for changes to this legal form or the creation of entirely new ones.[76] Unfortunately, the prospect of legislative action toward these ends seems "impossibly out of reach."[77] But when the government will not solve a fundamental problem

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[71] Eldar (2020), *supra* note 33, at 966 ("Wide managerial discretion to pursue social missions enables managers to promote their own interests. Without adequate monitoring, there is little reason to believe that managers would be dedicated to pursuit of public benefits.").

[72] Brakman Reiser & Dean (2017), *supra* note 33, at 74 ("[I]nvestors facing the time and monetary outlays required to litigate failures to prioritize mission will rarely take up the fight. . . [S]tatutory elimination of liability for such lapses makes injunctive relief the only possible vision of success, further limiting the appeal of shareholder litigation as a remedy. . . . [S]erious collective action problems and changing preferences will stymie shareholder enforcement."); Eldar (2020), *supra* note 33, at 966 ("[I]t is doubtful that shareholders will undertake costly lawsuits to enforce public benefits."); McDonnell (2017), *supra* note 23, at 734 ("[M]any commentators fear that the statutes build in so many limits to potential lawsuits for violation of [PBC directors' fiduciary] duties that the new duties are basically toothless.").

[73] Brakman Reiser & Dean (2017), *supra* note 33, at 72–73 ("A recent study found just 8 percent of benefit corporations produced the statutorily required benefit report.") (citing J. Haskell Murray, *An Early Report on Benefit Reports*, 118 W. Va. L. Rev. 25, 35 (2015)).

[74] *Id.* at 71 ("[B]oard approval and voting requirements allow investors to cast off the organization's social mission over a founder's objection. It simply comes down to numbers. If investors control enough shares to shift the board to their viewpoint and win a supermajority in the shareholder voting process, they can remove the organization's dual mission."). *But see* Michael R. Littenberg et al., *Delaware Public Benefit Corporations—Recent Developments*, Harv. L. Sch. F. Corp. Gov. (Aug. 31, 2020), https://corpgov.law. .edu////public-benefit-corporations-recent-developments (explaining that Del. Code Ann. tit. 8 § 363(c) previously required the approval of two-thirds of voting shares to convert a PBC to a conventional corporation, but that in 2020 this provision was eliminated from the statute).

[75] Eldar (2017), *supra* note 4, at 183 ("Gaining access to . . . capital is a particular problem for for-profit social enterprises because they lack a standardized commitment device (such as the non-distribution constraint [applicable to tax-exempt organizations]) to assure their investors, customers, and the government that they utilize subsidies effectively, and there is an obvious risk that those who control an organization will expropriate the subsidies it receives.").

[76] *See supra* note 33 and accompanying text.

[77] Brakman Reiser & Dean (2017), *supra* note 33, at 76.

like a lack of mutual trust, then creative private ordering may bridge the gap.[78]

C. Steward Ownership's History and Goals

Rather than just one type of private ordering, steward ownership encompasses an array of different organizational structures in different countries, all intended to keep a company "independent, purpose-driven, and value-led over the long term."[79] Its primary proponent is Purpose, an international conglomerate of various legal entities.[80] The most relevant to this Article is Purpose Stiftung, CH, a Swiss foundation established in 2015 (the "Purpose Foundation"),[81] which serves as a golden shareholder to GSCs.[82]

Although this Article focuses on a very recent iteration of steward ownership in the United States, Purpose traces this movement's history back much further and around the world, as far as 1846, when Carl Zeiss founded his eponymous optics company in Germany.[83] After his death in 1888, the Carl Zeiss Foundation was created and "has owned the company ever since," ensuring that "the company cannot be sold, and that profits are either reinvested or donated to the common good."[84] Other famous examples of steward ownership, which may employ similar "foundation-based structures" or "different legal frameworks," "include the German electronics company Bosch, [the] Danish pharmaceutical company Novo Nordisk, [the] British department store chain John Lewis, and the American internet pioneer Mozilla."[85]

Regardless of the legal structure involved, steward ownership is intended to "commit companies to two key principles."[86] First, "profits serve purpose"; they are "a means to an end, not an end in and of themselves."[87] However, this principle seems more rhetorical than effectual, as profits are still "reinvested in the business, used to repay investors, shared with stake-

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[78] *See supra* note 35 and accompanying text.

[79] Purpose Foundation, *supra* note 31, at 9.

[80] *See* Purpose Foundation, *Who we are*, https://purpose-economy.org/en/who-we-are (last visited Sept. 17, 2021) ("In order to meet the specific challenges of our mission, Purpose consists of different legal entities: Purpose Foundation, Purpose Ventures Coop, Purpose Foundation GmbH and Purpose Evergreen Capital GmbH & Co. KGaA. All Purpose entities are steward-owned through a veto held by the charitable Purpose Foundation.").

[81] Stiftung Schwiz, *Purpose Stiftung*, https://stiftungen.stiftungschweiz.ch//stiftung (last visited Sept.17, 2021).

[82] Purpose Foundation, *supra* note 31, at 18.

[83] *See id.* at 10.

[84] Purpose Foundation, Steward-Ownership: Ownership and Finance Solutions for Mission-Driven Businesses 14 (Jason Wiener, et. al., eds., 2019), https://purpose-economy.org/content/uploads/expowest_purpose_digital_020419.pdf; Wolfgang Mühlfriedel & Edith Hellmuth, *The Company's History of ZEISS – At a Glance* (1996), https://www.zeiss.com/content/dam/corporate-new/about-zeiss/history/downloads/the_companys_history_of_zeiss-at_a_glance.pdf.

[85] Purpose Foundation, *supra* note 31, at 10.

[86] *Id.* at 11.

[87] *Id.*

holders, or donated to charity,"[88] just as in any other corporation. In contrast, the second key principle, "self-governance," is more distinctive in practice: steward-owned companies "keep control with the people who are actively engaged in or connected to the business," as opposed to outside investors.[89]

One of the main benefits attributed to steward ownership is the long-term preservation of "a company's mission and values," which arises largely from restrictions on any sale of the company.[90] In addition, Purpose claims that steward ownership leads to better "governance and management," increased "employee productivity and retention," and "long-term customer loyalty."[91]

In terms of mission and values, although all "steward-owned companies serve a purpose," each defines its own unique purpose.[92] This could take the form of a social or environmental mission, a particular product or service, or a specific method of doing business.[93] Despite these various possibilities, most of the companies highlighted on Purpose's website, including all the American ones, claim to have social or environmental missions of some kind.[94] Evidently, social enterprise is steward ownership's primary focus, at least in the United States.

D. The Golden Share Model of Steward Ownership

Though many steward ownership structures, especially in foreign countries, require the creation of foundations and trusts,[95] the golden share model in the United States is based entirely in corporate law. Starting with a Delaware PBC, this model employs a capital structure with multiple classes of stock, intended to separate stockholders' voting and economic rights and to grant certain veto powers to an unaffiliated foundation.

To date, two GSCs exist in the United States: Zielwear and Creative Action Network.[96] These are Delaware PBCs with the legal names Ziel, Inc. PBC and Creative Action Network, Inc.[97]

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[88] *Id.*

[89] *Id.*

[90] *Id.* at 13.

[91] *Id.* at 13–14.

[92] *Id.* at 9.

[93] *Id.*

[94] Purpose, *Companies*, https://purpose-economy.org/en/companies (last visited Sept. 17, 2021) (listing three steward-owned companies based in the United States: Creative Action Network, Organically Grown Company, and Ziel).

[95] Purpose Foundation, *supra* note 31, at 20–24 (describing structures known as "Single Foundation," "Trust Foundation," "Trust Partnership," and "Perpetual Purpose Trust").

[96] *See supra* note 94; Purpose Foundation, *supra* note 31, at 17 (listing Creative Action Network and Zielwear as examples of the golden share model); *id.* at 24 (listing Organically Grown Company as an example of a "Perpetual Purpose Trust").

[97] Ziel, Inc. PBC Amended and Restated Certificate of Incorporation, Article I (Aug. 31, 2018) [hereinafter "Ziel Charter"] (on file with author); Amended and Restated Certificate of Incorporation of Creative Action Network, Inc., Article I (Jun. 25, 2018) [hereinafter "CAN Charter"] (on file with author).

Ziel is an "on-demand apparel manufacturing platform."[98] Among its principles, the company seeks to "eliminate overproduction" and the corresponding waste of resources, to "create local jobs" in the United States, "to minimize the pollution and energy cost of shipping overseas," and to "support sustainable [production] practices and equal opportunity."[99] Accordingly, Ziel's charter states that its specific public benefit is "to support fair trade and sustainable clothing production; furthermore, in order to advance the best interests of those materially affected by the Corporation's conduct, it is intended that the business and operations of the Corporation create a material positive impact on society and the environment, taken as a whole."[100]

Creative Action Network describes itself as "a community of artists and advocates making art with purpose."[101] They "run crowdsourced campaigns around causes, inviting anyone and everyone to contribute their own meaningful designs," and "then develop those designs into a range of physical goods, from posters to apparel to home goods, which [they] sell online, and in retailers all over the country, supporting artists and causes with every purchase."[102] As the specific public benefit identified in its charter, Creative Action Network "shall foster a global community of artists making art with purpose, supporting both independent artists and nonprofit partners through the dissemination of meaningful work."[103]

Aside from their specific public benefits and certain stockholder rights, Ziel and Creative Action Network each employ substantially similar versions of the golden share model, using only nominally different language in their charters. As the only GSCs in the United States so far, they constitute this model's prototype, which the following subsections describe based on these two companies' charters.

1. Common Stock

Common stock is issued only to specific types of insiders, which may include any combination of founders, directors, employees, other service providers, customers, and suppliers.[104] This stock can be transferred only to other members of those groups or to the corporation, not to outsiders.[105] If a common share is transferred in violation of these restrictions or if its holder

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[98] Ziel, *Our Story*, https://www.zielwear.com/our-story (last visited Sept. 17, 2021).
[99] *Id.*
[100] Ziel Charter, *supra* note 97, at III.C.
[101] *About*, Creative Action Network, https://creativeaction.network/pages/about (last visited Sept. 17, 2021).
[102] *Id.*
[103] CAN Charter, *supra* note 97, at 3.3.
[104] Ziel Charter, *supra* note 97, at V.C.1; CAN Charter, *supra* note 97, at 4.2.3.1.
[105] Ziel Charter, *supra* note 97, at V.C.1; CAN Charter, *supra* note 97, at 4.2.3.1.

ceases to be a member of one of those groups, then the corporation must redeem (that is, repurchase) that share for an amount equal to its par value.[106]

The charters of Ziel and Creative Action Network do not directly address the succession of founders or other managers. According to Purpose, however, GSCs can specify how the common stock of these "stewards" is transferred when they depart.[107] For instance, successors could be selected by the previous stewards (perhaps subject to another body's approval), by the corporation itself, or by an outside actor like the golden shareholder (as described in Part I.D.3 below).[108]

To control the proportion of voting and economic rights that eligible common stockholders receive over time, common stock is further divided into multiple classes. Class A common stock is the only class entitled to vote at stockholder meetings, but it is generally not eligible for dividends or redemption.[109] Separately, Class B common stock can be used as a form of equity incentive compensation for directors, employees, and other service providers. This class bears no voting rights, but its holders are eligible to receive dividends up to a certain percentage (e.g., 10%) of the corporation's earnings and profits since incorporation, if holders of preferred stock also receive proportional dividends.[110] The percentage limitation is intended to prevent managers from extracting excessive value from the corporation. In addition, the charter could state that, following a specified date (e.g., the fifth anniversary of incorporation), the corporation may redeem shares of this class with the approval of the golden shareholder and any preferred stockholders.[111]

Although the charter's rules apply only to common stock, a GSC may also issue stock options and other forms of equity incentive compensation to employees and service providers. In corporations more generally, "as [a] company matures and the value of its stock increases, employee stock options are used extensively" instead of common stock awards.[112] After exercising options in a GSC, however, an optionee would receive shares of common stock subject to the charter's applicable rules.

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[106] Ziel Charter, *supra* note 97, at V.C.1; CAN Charter, *supra* note 97, at 4.2.3.1. Regarding par value, see *infra* text accompanying note 168.

[107] Purpose Foundation, *supra* note 31, at 18.

[108] *See id.*

[109] Ziel Charter, *supra* note 97, at V.B.1, V.B.2.1.1, V.B.3; CAN Charter, *supra* note 97, at 4.2.1, 4.2.2. Confusingly, the charters of Ziel and Creative Action Network apply opposite labels to voting and nonvoting common stock. In addition, Ziel imposes transfer restrictions on all common stock, whereas Creative Action Network does so only on voting common stock. For simplicity, this Part I.D presents the Ziel charter's nomenclature and rules with respect to common stock.

[110] Ziel Charter, *supra* note 98, at V.B.1, V.B.2.1.2, V.B.3.2; CAN Charter, *supra* note 98, at 4.1.1.2, 4.1.2, 4.4.2.3.2.

[111] *E.g.,* Ziel Charter, *supra* note 98, at V.B.2.1.2.

[112] Bagley & Dauchy, *supra* note 41, at 105.

2. Nonvoting Preferred Stock

To investors, a GSC can issue preferred stock with no ordinary voting rights.[113] However, as in many companies financed by venture capital,[114] the charter may contain "protective provisions" that prevent the corporation from taking certain extraordinary actions without preferred stockholders' approval.[115] These enumerated actions may include business combination transactions, public offerings of stock, liquidations, changes to the charter or bylaws, dividends to other stockholders, changes in the number of directors, and related-party transactions.[116]

In contrast, subject to rules and schedules stated in the charter, preferred stock is eligible for dividends and for redemption. Regarding the first of these entitlements, a charter could allot to preferred stockholders a pro rata share of any dividends declared by the board of directors.[117] Alternatively, it could provide that, if the corporation achieves a certain annual revenue milestone, then preferred stockholders must receive dividends equal to a certain percentage of post-tax earnings until a certain date and up to a certain monetary cap.[118]

Furthermore, a corporation could specify various rules regarding redemption. It could repurchase each preferred stockholder's shares any time after a certain date (e.g., the fifth anniversary of incorporation), either upon that stockholder's request or according to a predetermined schedule.[119] The redemption price for each share of preferred stock would equal a specified multiple (e.g., five times) of that share's original issue price.[120] Then, the corporation would apply to redemption payments a certain percentage (e.g., 30%) of its post-tax earnings.[121] This payment schedule could proceed indefinitely until all of a stockholder's shares are redeemed.[122] Alternatively, those limited payments could continue only until a certain date (e.g., the tenth anniversary of incorporation), after which the corporation would apply to redemption payments *all* its post-tax earnings, as long as that stockholder retains any shares.[123] This second approach would accelerate investors' receipt of returns.

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[113] Ziel Charter, *supra* note 97, at V.B.3.3; CAN Charter, *supra* note 97, at 4.4.6.1.
[114] Bagley & Dauchy, *supra* note 40, at 475.
[115] Ziel Charter, *supra* note 97, at V.B.4; CAN Charter, *supra* note 97, at 4.4.4.
[116] Ziel Charter, *supra* note 97, at V.B.4; CAN Charter, *supra* note 97, at 4.4.4.
[117] Ziel Charter, *supra* note 97, at V.B.1.
[118] CAN Charter, *supra* note 97, at 4.4.1.2, 4.4.2.2, 4.4.2.3.
[119] Ziel Charter, *supra* note 97, at V.B.2.3.1; CAN Charter, *supra* note 97, at 4.4.1.8, 4.4.5.2.
[120] Ziel Charter, *supra* note 97, at V.B.2.3.1; CAN Charter, *supra* note 97, at 4.4.1.8, 4.4.5.2.
[121] Ziel Charter, *supra* note 97, at V.B.2.3.3(a); CAN Charter, *supra* note 97, at 4.4.1.6, 4.4.5.2.
[122] CAN Charter, *supra* note 97, at 4.4.5.2.
[123] Ziel Charter, *supra* note 97, at V.B.2.3.3(b).

As in the preferred stock arrangements typical of venture capital financing,[124] this class has a preference over other classes of stock upon any sale or liquidation, permitting preferred stockholders to receive a specified multiple of the purchase price before other stockholders receive any proceeds.[125] In addition, unlike other classes of equity, preferred stock is not subject to any transfer restrictions in the charter.[126]

3. Golden Share

As a final class of stock, a golden share is issued to a "veto service" foundation.[127] This class has no ordinary voting or economic rights, but it holds certain approval rights. Most importantly, this includes the right to veto (a) any sale or liquidation of the corporation or its assets and (b) certain charter amendments, including any (i) change to the specific public benefit required of all Delaware PBCs, (ii) change to rights and restrictions on capital stock, or (iii) grant of either voting rights to outsiders or economic rights to voting stock.[128]

The golden share's ownership is strictly limited. It can be held by or transferred to only "a trust, foundation, or tax-exempt entity established to hold [golden] shares . . . that is required by its constitutional documents to exercise the powers of [the golden share] in order to further the principles of steward ownership and create a material positive impact on society and the environment, taken as a whole."[129] This organization cannot "have any economic beneficiaries, and the decision makers with respect to the [organization's] assets may not be permitted to benefit from any action or inaction of [that organization] under [its charter]."[130]

The Purpose Foundation serves as a veto service provider for GSCs.[131] Its own charter obligates it "to veto any changes to [a company's] structure that would undermine the separation of voting and dividend rights or an attempted sale,"[132] satisfying a golden shareholder's typical criteria.

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[124] BAGLEY & DAUCHY, *supra* note 40, at 96 ("[V]enture capital investors usually acquire preferred, not common, stock . . . [T]he venture investors can reduce their risk by purchasing preferred stock that includes a liquidation preference over the common stock. A *liquidation preference* gives the preferred shareholders first claim on the company's assets in the event that the company is dissolved or is sold.").

[125] Ziel Charter, *supra* note 97, at V.B.7.1; CAN Charter, *supra* note 97, at 4.4.3.1.

[126] Ziel Charter, *supra* note 97, at V.C; CAN Charter, *supra* note 97, at 4.2.3, 4.3.3, 4.4.

[127] PURPOSE FOUNDATION, *supra* note 31, at 18.

[128] Ziel Charter, *supra* note 97, at V.B.6; CAN Charter, *supra* note 97, at 4.3.2. Regarding the specific public benefit, see *supra* text accompanying note 67.

[129] Ziel Charter, *supra* note 97, at IV, V.C.3; CAN Charter, *supra* note 97, at 4.3.3.

[130] Ziel Charter, *supra* note 97, at IV.

[131] *See* PURPOSE FOUNDATION, *supra* note 31, at 18.

[132] Ernst Schütz, *Why we need new solutions for succession: family business 2.0*, *in* PURPOSE FOUNDATION, STEWARD-OWNERSHIP: RETHINKING OWNERSHIP IN THE 21ST CENTURY 75 (Josh Raisher ed., n.d.), https://purpose-economy.org/file/364.

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Together, these arrangements have interesting implications for the relationships among managers, investors, the golden shareholder, and the corporation itself, which the remainder of this Article proceeds to explore.

II. The Golden Share Model's Achievements

A. Legality

As a threshold matter, any novel legal structure must comply with applicable law. As a whole, the golden share model has not yet been tested in court. But in Delaware, the state in which the underlying PBC would typically be organized, this model's individual features appear to be legal either in their current iterations or after straightforward adjustments.

1. Separation of Economic and Voting Rights

First, a central aspect of the golden share model is the separation of economic and voting rights through designations of different classes of stock.[133] Delaware corporations are expressly permitted to authorize multiple classes of stock with different rights and limitations, including voting rights.[134] Indeed, dual-class share structures have become increasingly common in publicly traded corporations.[135] Unlike the golden share model, which vests all economic rights in one class and all voting rights in another, most dual-class share structures take a less extreme approach. Instead, they typically provide all classes with some voting rights but offer "low-voting stock for public investors to buy, keeping the high-voting shares (which typically have ten times as many votes as the low-voting shares) in the possession of the company's insiders."[136]

A notable exception is Snap, the maker of the Snapchat mobile application. In its initial public offering in 2017, this Delaware corporation offered

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[133] *See supra* text accompanying notes 109–10, 113.

[134] Del. Code Ann. tit. 8 § 151 ("Every corporation may issue 1 or more classes of stock . . . which classes . . . may have such voting powers, full or limited, or no voting powers."); *id.* § 212(a) (contemplating situations in which "the certificate of incorporation provides for more or less than 1 vote for any share"); Providence & Worcester Co. v. Baker, 378 A.2d 121, 123 (Del. 1977) ("Under [Del. Code Ann. tit. 8] § 212(a), voting rights of stockholders may be varied from the 'one share-one vote' standard by the certificate of incorporation.").

[135] Albert H. Choi, *Concentrated Ownership and Long-Term Shareholder Value*, 8 Harv. Bus. L. Rev. 53, 55 (2018) (reporting that, "by 2015, about 14 percent of all companies that went public have done so with a dual class structure"); Dhruv Aggarwal et al., *The Rise of Dual-Class Stock IPOs* 1 (NBER Working Paper No. 28609, 2021) (reporting that "almost 30 percent of initial public offerings (IPOs) in 2017–2019 had dual-class structures").

[136] Dorothy S. Lund, *Nonvoting Shares and Efficient Corporate Governance*, 71 Stan. L. Rev. 687, 689 (2019).

to investors shares with no votes, allowing the two founders to retain complete voting control.[137] This approach is like the golden share model without the golden share, and with nonvoting common stock instead of nonvoting preferred stock. Although this separation of rights may be more extreme than a typical dual-class structure, Delaware's relevant statutes and case law provide no reason to believe that it is unlawful.[138] Indeed, Snap's structure has not been challenged in court despite the company's high profile, and "other companies included nonvoting stock in their public offerings in the months following Snap's IPO."[139]

Given the statutory authority for these structures and their widespread use, the golden share model's similar separation of economic and voting rights appears legal in Delaware.

2. Stock Transfer Restrictions

Another indispensable feature of this model is its broad restrictions on the transfer of common stock and the golden share.[140] Delaware corporations may impose stock transfer restrictions subject to certain conditions, which are primarily codified in Section 202 of the Delaware General Corporation Law. First, the transfer restrictions must comply with some straightforward ministerial requirements, which a company can easily satisfy through appropriate language in its charter and stock certificate legends or equivalent notices.[141] Second, only the following types of stock transfer restrictions are permissible: (a) rights of first refusal or offer and tag-along rights; (b) obligations of the corporation or stockholders to purchase stock; (c) rights of the corporation or stockholders to approve any proposed transfer; (d) obligations of stockholders to sell restricted stock to the corporation or any other person (including through drag-along rights), and automatic sale provisions to any of those effects; and (e) restrictions on stock's transfer to or ownership by designated people, if the "designation is not manifestly unreasonable."[142] Regarding the last category, a transfer restriction is "conclusively presumed to be for a reasonable purpose" if it is intended to maintain a tax, statutory, or regulatory advantage or to comply with an applicable law or regulation.[143]

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[137] Snap Inc., Registration Statement (Form S-1) 4 (Feb. 2, 2017).

[138] *See supra* note 134 and accompanying text.

[139] Lund, *supra* note 136, at 707.

[140] *See supra* text accompanying notes 105, 129.

[141] Del. Code Ann. tit. 8 § 202(a) (requiring that transfer restrictions be "noted conspicuously" on each relevant stock certificate or the equivalent notice that must accompany uncertificated stock, or that the transferring stockholder have "actual knowledge of the restriction"); *id.* § 202(b) (requiring that transfer restrictions be imposed by the corporation's charter or bylaws or by an agreement with the transferring stockholder).

[142] *Id.* § 202(c).

[143] *Id.* § 202(d).

More generally, a transfer restriction must be "reasonable to achieve a legitimate corporate purpose."[144] However, when such a restriction's validity is contested, "Delaware courts have been reluctant to invalidate stock restrictions because they are unreasonable."[145] Instead, since Section 202's adoption in 1967, those "courts have been broadly deferential to the decisions of market participants when they decide to place restrictions on stocks."[146]

In contrast, before 1967, the Delaware Supreme Court invalidated certain stock transfer restrictions in *Tracey v. Franklin*, when it found "no specification of any particular purpose, so far as the restraints in question are concerned, to benefit the corporation, or other stockholders of the same class, or to do otherwise than to solidify ownership in the parties themselves."[147] Similarly, in *Greene v. E.H. Rollins & Sons*, the Delaware Chancery Court refused to enforce a charter provision permitting the corporation to repurchase stock at any time without a stockholder's consent.[148] In that case, the only apparent justification for this right was that "the corporation ought at all times to have a body of stockholders among whom there should never be any whom the directors find not agreeable."[149] Finding this goal illegitimate, the court concluded that the charter provision was not "reasonably necessary to advance the corporation's welfare and promote business success."[150]

One might presume that Section 202 supplanted these prior rulings, but to the contrary, Delaware courts have since viewed that provision as mere "codification" of earlier case law,[151] which they have continued to cite long after that statute's adoption.[152] Therefore, despite their general deference to

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[144] Capital Group Companies, Inc. v. Armour, No. Civ.A 422-N, 2005 WL 678564, at *9 (Del. Ch., 2005).

[145] *Id.* at *8.

[146] *Id.*; *accord* Jesse A. Finkelstein, *Stock Transfer Restrictions Upon Alien Ownership Under Section 202 of the Delaware General Corporation Law*, 38 Bus. Law. 573, 586-89 (1983) (discussing Delaware law's "substantive requirement that a transfer restriction be reasonably necessary to the corporation"); Edward B. Rock, *Shareholder Eugenics in the Public Corporation*, 97 Cornell L. Rev. 849, 888–90 (2012) (discussing the ability of public corporations to use stock transfer restrictions to exclude undesirable shareholders).

[147] Tracey v. Franklin, 67 A.2d 56, 60 (Del. 1949).

[148] *See* Greene v. E.H. Rollins & Sons, 2 A.2d 249 (Del. Ch. 1938).

[149] *Id.* at 252.

[150] *Id.*

[151] Grynberg v. Burke, 378 A.2d 139, 142–43 (Del. Ch. 1977) (rejecting an argument "that the *Lawson-Greene-Tracey* trilogy no longer provides the only standard for measuring the validity of restrictions on the transferability of corporate stock," and concluding instead that "the express authorization of § 202(c)(3) . . . is no more than a modern codification of the principle adopted in *Lawson v. Household Finance Corp.*, namely, that a restraint on the free transferability of corporate stock . . . is permissible under our law provided it bears some reasonably necessary relation to the best interests of the corporation").

[152] Capital Group Companies, Inc. v. Armour, *supra* note 144, at 6 ("The decision in *Grynberg* has been cited approvingly and applied in several cases in this court."). *E.g.*, eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1, n. 159 (Del. Ch. 2010) (citing *Grynberg* to support the statement that a transfer restriction must "bear[ ] some reasonably necessary relation to the corporation's best interests").

corporate decisions, those courts may still invalidate transfer restrictions that are intended solely to perpetuate existing stockholders' ownership, as in *Tracey* and *Greene*.[153]

Faced with a novel request to invalidate the golden share model's typical restrictions, which prohibit all transfers of common stock to outsiders and require the corporation to redeem any improperly transferred shares at par value,[154] how would a Delaware court rule? These provisions fit the fifth category of Section 202c's permitted restrictions, as they "[p]rohibit[ ] or restrict[ ] the transfer of the restricted securities to, or the ownership of restricted securities by, designated persons or classes of persons or groups of persons."[155] Such a restriction is permissible only if it is "not manifestly unreasonable."[156] In assessing these transfer restrictions' validity, a court would have to determine whether they are "reasonable to achieve a legitimate corporate purpose."[157]

As a defendant, a GSC would presumably cite the goals of steward ownership, such as perpetual commitment to a social mission. Because the underlying entity would be a PBC rather than a traditional corporation, it seems more likely that a court would agree that a social mission could constitute a "legitimate corporate purpose."[158] In such a proceeding, a GSC might also cite Purpose's claims of this model's "proven benefits" to business performance, such as heightened "employee productivity and retention" and "customer loyalty."[159] These claims would distinguish the situation from those of the seminal cases of *Greene* and *Tracey*, in which the courts invalidated restrictions that benefitted only insiders rather than the corporation itself.[160]

If these goals of steward ownership suffice to constitute a "legitimate corporate purpose," then the court would have to assess whether the transfer restrictions are "reasonable to achieve" it.[161] In some respects, the restrictions are extreme. They are perpetual and limit transfers only to certain insiders, which could constitute a prohibitively small group in many closely held companies. In some cases, they may effectively constitute "absolute restraints on transfer," which "are often deemed unreasonable and unenforceable."[162] If so, a court might consider whether the corporation could

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[153] *Stockholders Agreement (Multi-Party; General Form) (DE)*, at § 3.01, Thomson Reuters Prac. L., https://us.practicallaw. .com/W-020-1836 (last visited Sept. 17, 2021) ("[A]bsolute restraints on transfer, such as blanket prohibitions on transfer for an indefinite or an unduly long period, are often deemed unreasonable and unenforceable by Delaware courts.").

[154] *See supra* text accompanying notes 105–06.

[155] Del. Code Ann. tit. 8 § 202(c)(5).

[156] *Id.*

[157] *See supra* text accompanying note 144.

[158] *See supra* text accompanying notes 66–67.

[159] *See supra* text accompanying note 91.

[160] *See supra* text accompanying notes 147–49.

[161] *See supra* text accompanying note 157.

[162] *Stockholders Agreement (Multi-Party; General Form) (DE)*, *supra* note 153, at § 3.01.

achieve the same purpose with a less extreme restriction. For example, to limit outside stockholders, the charter could grant to the corporation a right of first refusal ("ROFR") with respect to any proposed stock sale to any buyer outside the permitted groups. Section 202 expressly permits ROFRs,[163] and they are common in privately held companies.[164] As a disadvantage of this approach, the corporation would have to pay the proposed purchase price for the stock,[165] which could be high depending on the company's valuation. But theoretically, perhaps this is the appropriate cost that one should incur when seeking to restrict stockholders' property rights. If a court adopts this reasoning, then it may conclude that, given the relatively fair alternatives, the typical golden share model's more complete restrictions on transfer are unreasonable and therefore unenforceable, no matter how legitimate the alleged purpose may be. Fortunately, GSCs could readily mitigate the risk of invalidation by imposing less extreme restraints, such as a ROFR, if they are willing to bear the potential costs.

Therefore, though it is unclear whether the typical golden share model's transfer restrictions are valid under Delaware law, they could be easily modified to ensure enforceability.

3. Requirements to Redeem Transferred Stock

Coupled with these transfer restrictions are provisions that require the corporation to redeem, for par value, any share that is purportedly transferred in violation of those restrictions.[166] In general, Delaware law broadly permits corporate charters to provide that the corporation will redeem stock at either its or the stockholder's option (pursuant to a call or a put right, respectively) or upon a certain event,[167] subject to a few limitations. First, in general, a corporation may redeem stock only if the required funds do not exceed the difference of net assets (i.e., total assets minus total liabilities) minus the par value of its issued stock.[168] Second, "it is improper to cause the corporation to repurchase its stock for the sole or primary purpose of

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[163] *See supra* text accompanying note 142.

[164] Bagley & Dauchy, *supra* note 40, at 116–17 ("It is common for privately held companies to impose certain restrictions on the transfer of both unvested and vested shares. . . The most common form of transfer restriction imposed on shareholders of a newly formed company is a right of first refusal.").

[165] *Rights of First Negotiation, Offer, and Refusal*, Thomson Reuters Prac. L., https://.practicallaw.thomsonreuters.com/6-534-6258 (last visited Sept. 17, 2021) ("A typical ROFR clause . . . [a]llows the holder to accept the material terms of the third-party offer and enter into the covered transaction with the grantor on these terms.").

[166] *See supra* text accompanying note 106.

[167] Del. Code Ann. tit. 8 § 151(b).

[168] Del. Code Ann. tit. 8, §§ 154, 160(a); SV Inv. Partners, LLC v. ThoughtWorks, Inc., 37 A.3d 205, 210 (Del. 2011) (citing Klang v. Smith's Food & Drug Ctrs., Inc., 702 A.2d 150, 153 (Del. 1997)) ("Capital is impaired if the funds used in the repurchase exceed the amount of the corporation's surplus, defined by 8 Del. C. § 154 to mean the excess of net assets over the par value of the corporation's issued stock.") (internal quotation marks omitted).

maintaining the board or management in control; in such a case the purchase is deemed unlawful even if the purchase price is fair."[169]

The typical golden share charter provides for redemption at par value.[170] In corporations generally, par value is ordinarily set at a nominal level, like a fraction of a cent per share.[171] Accordingly, the funds required by such a redemption would typically be minimal and exceed the statutory limit only when a corporation's net assets are negative. Therefore, contrary to their charters, GSCs whose liabilities exceed their assets could not legally redeem improperly transferred common stock. But sales of shares in companies in that financial situation seem uncommon, so this restriction may not often matter in practice.

The second limitation on redemptions may be more problematic. One of the main objectives of steward ownership in general is to maintain existing management's control.[172] Accordingly, many of the golden share model's mechanisms are intended to prevent outsiders from obtaining voting stock. However, redemptions made solely or even primarily for these purposes could be considered illegal.[173] Therefore, if a stockholder were to challenge such a redemption's validity in Delaware court, a GSC would have to convince the court that its actions had other objectives. As with stock transfer restrictions, perhaps it could argue that it redeemed the stock for a purpose other than maintaining control, such as long-term commitment to a social mission or certain indirect business advantages.[174] Delaware case law does not provide enough guidance to predict how a court would receive such an argument, so the validity of the golden share model's redemption provisions is unclear.

However, a challenge to these provisions seems unlikely to arise in the context of an actual redemption, which would occur only after stock is transferred. But a prospective stock purchaser that learns of the corresponding charter provisions would ordinarily not proceed with the purchase, because the newly acquired shares would be immediately lost for their mere par value, which would usually amount to a small fraction of the purchase price.[175] Therefore, the redemption requirement is more significant for its chilling effect on potential transfers than for the effects of its actual exercise.

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[169] Strassburger v. Earley, 752 A.2d 557, 572–73 (Del. Ch. 2000) (citing Bennett v. Propp, 187 A.2d 405, 411 (Del. 1962)).

[170] *See supra* text accompanying note 106.

[171] Irina Fox, *Protecting All Corporate Stakeholders: Fraudulent Transfer Law as a Check on Corporate Distributions*, 44 Del. J. Corp. L. 81, 91 (2020) ("Most modern corporations will limit share par value to a nominal amount, typically a fraction of a dollar or sometimes even a penny.").

[172] Purpose Foundation, *supra* note 31, at 11 (stating that one of the two "key principles" of "[s]teward-ownership structures" is to "keep control with the people who are actively engaged in or connected to the business.").

[173] *See supra* text accompanying note 168.

[174] *See supra* text accompanying note 159.

[175] *See supra* text accompanying note 169.

In that sense, it effectively operates as an additional transfer restraint beyond the charter's explicit restrictions.

As a result, the redemption provisions would likely be challenged only by an existing stockholder seeking to disarm the corporation's stock transfer restrictions before selling shares. In that context, a court may construe the redemption provisions as a permissible type of transfer restriction within the accepted categories identified in Section 202.[176] But to insulate itself from even this kind of challenge, a GSC could simply replace both the transfer restrictions and the mandatory redemption provision with a ROFR in the corporation's favor, as suggested in Section II.A.2 above.

Therefore, even if the redemption provisions' enforceability is questionable, a GSC could prevent this issue with relatively simple changes to its charter.

4. Golden Shareholder Rights

Of course, the most distinctive aspect of the golden share model is the golden share itself. But the concept of a golden share is not unique to steward ownership. It first arose "in the 1980s during the global wave of privatizations of state-owned companies," when European governments would often retain "disproportionate voting power with respect to the election of the company's directors and various strategic decisions affecting the operation of the company."[177]

In the United States, however, golden shares appear primarily in the context of private debt financing. With such a mechanism, which can take various forms, "the creditor's vote is required to authorize the debtor's bankruptcy filing."[178] Accordingly, in the United States the only case law relevant to golden shares relates to bankruptcy. In some circumstances, federal courts have invalidated these veto rights as unenforceable waivers of the right to file for bankruptcy, in violation of public policy.[179]

But this reasoning does not apply to the kinds of rights granted to veto service providers in the golden share model of steward ownership. No acknowledged public policy grants stockholders an inalienable right to sell a corporation or to amend its charter, and these are the only actions that a golden shareholder can normally block.[180] Therefore, as long as the golden share does not also confer a veto right regarding bankruptcy filings, the risk

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[176] Del. Code Ann. tit. 8 § 202(c)(4) (permitting a transfer restriction that "[o]bligates the holder of the restricted securities to sell or transfer an amount of restricted securities to the corporation").

[177] Saule T. Omarova, *Bank Governance and Systemic Stability: The Golden Share Approach*, 68 Ala. L. Rev. 1029, 1043–44 (2017).

[178] Yiming Sun, *The Golden Share: Attaching Fiduciary Duties to Bankruptcy Veto Rights*, 87 U. Chi. L. Rev. 1109, 1120 (2020).

[179] *Id*. at 1124–25, 1127–30 (describing three cases with this outcome).

[180] *See supra* text accompanying note 128.

that courts would invalidate this device on public policy grounds appears minimal.

Even if golden shares are not invalid, this model of steward ownership could be less effective if the institutions holding these shares could not exercise their veto rights freely. Notably, if a golden shareholder is considered a "controlling" stockholder, then it owes certain fiduciary duties to the corporation and to other stockholders. In cases of "self-dealing," where a controller "appears to benefit at the expense of the controlled corporation (for example, when the controller disparately gains from contract terms or the enforcement of those terms where the two parties are on opposite sides)," the controller must "prov[e] that the terms of the transaction were intrinsically fair."[181]

In the bankruptcy context, "no court has held that golden shareholders owe fiduciary duties to the debtor by virtue of their inherent ability to control the debtor's bankruptcy decision."[182] Outside that context, under Delaware law, a stockholder is considered "controlling" if it has either "majority control of the entity's voting stock" or "a combination of potent voting power and management control such that the stockholder could be deemed to have effective control of the board without actually owning a majority of stock."[183] The second test is met only when stockholders "have such formidable voting and managerial power that they, as a practical matter, are no differently situated than if they had majority voting control."[184]

With veto rights only in the context of certain charter amendments and major transactions, and no voting rights or other involvement in any other decisions, golden shareholders do not possess the kind of "voting power" or "management control" that would render them controlling stockholders. Moreover, a controller's duties arise when a transaction is approved, not when it is blocked. In practice, by consistently performing its task of blocking transactions rather than approving them, a golden shareholder would not breach any fiduciary duty that a controlling stockholder would have. Therefore, no such duties would typically limit a golden shareholder in properly performing its assigned task.

Of course, a golden shareholder could shirk this responsibility by approving a transaction in which it has an interest, even though this would not only violate the charter but also adversely impact its reputation in the veto service business. In that unlikely situation, one might speculate that a Delaware court could deem the golden shareholder a controller with fiduciary duties with respect to that transaction, because its voting power regarding that transaction indeed bestows "effective control" over the decision of

[181] Ronald J. Gilson & Jeffrey N. Gordon, *Controlling Controlling Shareholders*, 152 U. Pa. L. Rev. 785, 791 (2003) (citing Sinclair Oil Corp. v. Levien, 280 A.2d 717 (Del. 1971)).

[182] Sun, *supra* note 178, at 1127.

[183] Corwin v. KKR Fin. Holdings LLC, 125 A.3d 304, 307 (Del. 2015) (en banc) (footnotes omitted).

[184] In re PNB Holding Co. S'holders Litig., 2006 WL 2403999, at *9 (Del. Ch. 2006).

whether to enter it.[185] This conclusion would be unprecedented for a stockholder with such a small interest in the corporation,[186] but perhaps that is only because Delaware courts have not faced sufficiently similar facts. Even if this outcome is possible, the prospect would advance, not impede, steward ownership's goals by incentivizing the golden shareholder to perform its task properly even when its own interests might lead it astray.

Therefore, Delaware courts are unlikely to either invalidate a golden shareholder's veto rights or limit their exercise in a manner that contravenes the golden share model's purposes. Overall, this aspect of the model appears legally sound.

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In summary, the golden share model's most central features—its separation of voting and economic rights through dual-class stock and the veto rights assigned to the golden share—do not present any apparent legal issues in Delaware. In contrast, the model's stock transfer restrictions and redemption requirements are of less certain enforceability, given the lack of case law that addresses the arguments that a GSC would have to make in defending those rules. Fortunately, to withstand judicial scrutiny more confidently, a GSC could replace those rules with standard ROFRs, at the potential cost of additional payments to stockholders upon exercise.

B. Advantages for Social Enterprises

The previous section established that the golden share model is legal, possibly with some straightforward variations. This section proceeds to explore the model's laudable achievements. Although the purported benefits of steward ownership in general are not limited to social enterprises, this appears to be the primary focus and audience for this approach to business organization.[187] Accordingly, this Article assesses the golden share model only for its potential value for social enterprises, not for all its possible benefits for other types of businesses.

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[185] *See supra* text accompanying note 183.

[186] *See* Purpose Foundation, *supra* note 31, at 17 ("Golden Share represents 1% of voting rights"); *In re Crimson Expl. Inc. Stockholder Litig.*, 2014 WL 5449419, at *10 (Del. Ch. 2014) (surveying nine Delaware cases considering controller status for minority stockholders with share percentages ranging from 27.7% to 49% and finding 35% to be the lowest to result in that status); *Calesa Assocs., L.P. v. Am. Capital, Ltd.*, 2016 WL 770251 (Del. Ch. 2016) (finding that a stockholder with 26% of a corporation's shares could be controlling).

[187] *See supra* text accompanying note 94.

1. Mission Protection

Most importantly, this model helps to protect a company's mission in the long term, consistent with the central aims of steward ownership. At least temporarily, dual-class structures alone could allow social entrepreneurs to pursue public-interest missions without other stockholders' interference. But if founders have a change of heart or are succeeded by managers with different priorities, then the company could eventually abandon its social goals even without investor pressure. With the addition of the golden shareholder, however, a dual-class company could prevent the most egregious departures from its mission, regardless of changes in management.

In particular, social entrepreneurs and impact investors often express deep concerns about the risk of the eventual sale of a mission-driven business to a larger, profiteering acquirer that will discontinue that mission.[188] By preventing any such sale without the golden shareholder's consent, the model could assuage these concerns and remove one large obstacle to trust between managers and investors. With this potentially destructive exit option off the table for both groups, they can have more confidence that the company will not abandon its mission following an acquisition.

In addition to M&A transactions, one of the most aspirational exits for investors in startup companies is an initial public offering.[189] Based on prominent examples like Etsy, many social entrepreneurs fear that an IPO driven by investor pressure will inevitably divert the company from its mission.[190] In a standard IPO, a corporation issues new common shares to outside investors.[191] But a GSC can issue common stock only to insiders, and the golden shareholder would have the authority and obligation to veto any change to this restriction.[192] Therefore, an IPO of common stock would be impossible in a GSC. Although Purpose suggests that GSCs could make public offerings of nonvoting preferred stock,[193] entrepreneurs should find this prospect less threatening than a standard IPO, because public stockholders without voting rights cannot control the company's direction.

Another common concern in all PBCs, including the typical GSC, is that the organization will convert to a traditional corporation.[194] This process would erase both the social mission's description from the corporation's charter and directors' obligations to balance public benefits against other interests. Instead, a PBC could retain its organizational form and simply amend the charter's description of the social mission to something that falls

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[188] Brakman Reiser & Dean, *supra* note 33, at 15–17.
[189] Bagley & Dauchy, *supra* note 40, at 616.
[190] *See supra* text accompanying notes 24–26.
[191] James D. Cox & Melvin Aron Eisenberg, Business Organizations, Cases and Materials 347 (12th ed. 2019).
[192] *See supra* text accompanying notes 104–06, 128.
[193] Purpose Foundation, *supra* note 31, at 37.
[194] Brakman Reiser & Dean (2017), *supra* note 33, at 70–71.

short of a manager's or investor's earlier aspirations. In a normal PBC, either of these processes would require the affirmative vote of a simple majority of voting shares.[195]

In a GSC, however, the golden shareholder's veto rights would block any such entity conversion or charter amendment.[196] This should instill confidence that the corporation will remain dedicated to its stated mission, at least on paper, and that directors will continue to have balancing obligations with respect to that mission, even if those obligations are only weakly enforceable.[197]

However, all these potential benefits arising from veto rights require managers and investors to trust the golden shareholder to exercise those rights reliably. As discussed in Part III.E below, some may hesitate to delegate these critical responsibilities to an unknown veto service foundation.

2. Management Protection

Social enterprise founders often fear that investors with enough voting power or other control will eventually elect new directors to replace them, directly or indirectly.[198] By denying investors any role in stockholder voting, including in board elections, the golden share model assures managers that investors cannot simply oust them in this manner. Therefore, managers may feel more comfortable issuing equity to investors in a GSC than in a standard PBC. Like other dual-class stock structures, the model provides "a way of bringing [investors] on board while limiting their influence."[199]

Of course, the extent to which this attribute advances social enterprise's broader goals, beyond just reducing managers' mistrust, depends on business leaders' genuine and continued commitment to the company's social mission. As discussed in Part III.A below, the golden share model does not actually guarantee this commitment. Further, Part III.B considers how investors' inability to replace directors could impede that mission rather than advance it.

3. Positive Signaling

Even if the golden shareholder does exercise its veto rights consistently, this mechanism prevents only major changes in a company, like an acquisition or corporate transformation. As discussed in Part III.A below, these veto rights have limited effectiveness in preventing other kinds of mission drift

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[195] *See supra* note 74.
[196] *See supra* text accompanying note 128.
[197] *See supra* text accompanying notes 67, 72.
[198] Brakman Reiser & Dean (2017), *supra* note 33, at 13 ("Parting with a significant equity stake in a double- bottom-line venture means parting with an equal measure of control over its future. For the founder of an incorporated social enterprise, yielding a majority stake means ceding the ability to elect directors that share his vision of a balance of a profit and mission.") (citations omitted).
[199] McDonnell (2017), *supra* note 22, at 737.

arising from day-to-day business decisions. Therefore, even investors with faith in the golden shareholder may question whether managers will prioritize the social mission when making those decisions.

However, a business's very choice of the golden share model could alleviate these deeper concerns by sending positive signals to prospective investors. After all, the PBC form's advocates claim that one of its main advantages is "the opportunity to make a very public declaration that you care about more than profit" with "a signal to your investors."[200] This signal should be even stronger with the golden share model, which demonstrates greater devotion to a mission than the standard PBC structure does.

Essentially, by granting veto rights to a golden shareholder, a GSC founder gives up the right to sell their company or to change its PBC status or specific public benefit. Except to the extent that they grant themselves common stock with economic rights, they also forego the other financial returns normally associated with stock ownership, like dividends.[201]

If founders elect a corporate form that denies them several economic rights and exit options that they would normally possess, then the signal to investors may resemble those of the even more restrictive non-distribution constraint that applies to tax-exempt organizations.[202] Like donors to nonprofits, investors in GSCs may perceive this apparent sacrifice as evidence of true dedication to the social mission. This could alleviate any concern that managers would eventually deviate from that mission in ways that are not subject to veto rights but remain within their discretion. Accordingly, impact investors may place more trust in founders of GSCs than they would in those of ordinary PBCs.

4. Negative Signaling

Exemplifying "mission drift"[203] are parables of famous companies that began with limited means and public-interest missions but abandoned them under pressure from rapacious venture capital funds and other institutional investors that forced them to pursue profit over purpose.[204] Wary of repeating these moral failures, social entrepreneurs often seek to avoid these greedy investors.

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[200] Karim Abouelnaga, *5 Reasons to Become a Benefit Corporation*, ENTREPRENEUR (May 24, 2017), https://www.entrepreneur.com/article/294213.

[201] *See supra* text accompanying notes 109–10.

[202] *See* Eldar (2020), *supra* note 33, at 948 ("By mitigating the controllers' incentives to pursue profits, [the non-distribution constraint creates] a higher likelihood that firms will (i) act fairly towards their stakeholders, including their consumers and employees, and/or (ii) contribute some of their revenues to the community.").

[203] *See supra* text accompanying note 47.

[204] *E.g.,* Makkonen, *supra* note 25, at 59–60 (recounting the stories of Etsy, Airbnb, and Lyft as examples of "companies [that] can't escape the profit-maximizing paradigm imposed by venture capitalists and the stock market.").

Through signaling, the golden share model may equip those entrepreneurs to achieve this goal. Just as it may attract like-minded investors by sending positive signals to those who prioritize the public interest,[205] this model may deter adverse investors by sending negative signals to those who seek only to maximize profits. If a founder chooses a corporate structure that apparently deprives them of the greatest opportunities for personal financial gain, then profit-maximizing investors will anticipate misalignment with management and refrain from funding the company. After all, those investors should easily find more lucrative opportunities among more traditional business organizations.

Of course, one might question whether a scheme as elaborate as the golden share model is necessary to avoid financiers of this sort. It may seem that, if social entrepreneurs really do not want to do business with venture capitalists, then the former could simply refuse the latter's money even in an ordinary PBC, with far less cost and complexity.

These doubts may be valid to an extent, but the clear and irreversible commitment inherent to the golden share model could offer some additional benefits. First, to adopt this model could effectively "tie oneself to the mast," when an initially mission-driven founder fears that the siren song of venture capital will eventually lure them to wreck their public-interest dreams on the jagged rocks of EBITDA. To a GSC, that song is likely inaudible, as profiteering investors lose any interest upon reviewing the corporate structure and recognizing its relatively paltry pecuniary promise.[206] Second, intentions may not always be apparent when managers and investors first meet. The founder of an ordinary PBC may think that an investor shares their commitment to a social mission because of a productive conversation and a good track record with other social enterprises. But after acquiring equity and perhaps a board seat, that investor may begin to lead the company astray from its mission, especially once the tradeoffs between profits and purpose become apparent. In contrast, no one with those intentions would bother to invest in a GSC in the first place.

In these ways, a GSC may deter adverse investors more easily than an ordinary PBC would. If so, this should result in greater trust between managers and those investors who care enough about the company's social mission to finance the venture despite its limited financial returns.

III. The Golden Share Model's Limitations

While achieving many important goals, the golden share model also presents several inherent limitations in meeting the challenges of social enterprise. In general, this model would appear to eliminate most of managers' typical reasons for mistrusting investors, but from investors' perspective,

[205] *See supra* Part II.B.3.
[206] *See infra* Part III.D.

many concerns should remain. Overall, the golden share model does not effectively close, but may in fact widen, the trust gap that inhibits social enterprises' growth.

A. No Mission Commitment

Most critically, although the model may guarantee that a particular mission remains enshrined in a PBC's charter,[207] it does not ensure that management will prioritize or advance that mission. A company's achievement of social goals depends largely on day-to-day business decisions, not on the M&A transactions and charter amendments that are subject to the golden shareholder's veto or a stockholder vote.

For instance, a common form of social enterprise is a manufacturer that uses environmentally sustainable materials and production practices even though they are relatively expensive and may thereby reduce profits. A well-known example is Patagonia, a California benefit corporation that manufactures outdoor clothing using eco-friendly materials like organic cotton, despite decreased profit margins.[208]

If a manufacturer with this kind of business model were a Delaware PBC, it may describe in its charter that its specific public benefit is to manufacture products "in an ethical and environmentally sound manner" or simply "to promote environmental sustainability."[209] If the managers eventually decide to adopt cheaper, dirtier manufacturing practices, then stockholders with at least two percent of the corporation's shares could bring a derivative lawsuit to enforce directors' obligation to consider in their decisions the specific public benefit identified in the charter.[210] But these plaintiffs would face substantial obstacles, because specific public benefits are usually stated vaguely[211] and directors have broad discretion in balancing their obligations.[212] Even when it could succeed, high costs and limited remedies would make stockholder litigation so unlikely as to have little, if any, deterrent or corrective effect on management's actions.[213]

If this business were not only a PBC but also a GSC, then the situation would not improve. The golden shareholder's veto rights are typically lim-

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[207] *See supra* text accompanying note 197.

[208] Eldar (2017), *supra* note 4, at 167.

[209] B Lab, *Delaware Public Benefit Corporations: Choosing a Specific Benefit*, *Appendix A*, https://perma.cc/FZZ7-D9MN (last visited Sept. 17, 2021).

[210] *See supra* text accompanying note 69.

[211] When stating their specific public benefit, PBCs are advised "to refer to [a] generic but specific purpose, rather than articulating the specific means by which the company currently achieves that purpose since, as the company scales and evolves, its method for [achieving that purpose] may also change." B Lab, *Delaware Public Benefit Corporations: Choosing a Specific Benefit*, https://perma.cc/484W-MRKL (last visited Sept. 17, 2021). For an example of a vaguely stated specific public benefit in a GSC's charter, see Ziel's language at *supra* text accompanying note 100.

[212] *See supra* note 71 and accompanying text.

[213] *See supra* note 72 and accompanying text.

ited to proposed charter amendments and sales of the company.[214] But neither of these actions or any broader stockholder approval would be necessary for management to change the company's production processes to reduce costs rather than sustain the environment. Instead, that change could simply take the form of day-to-day business decisions—like a substitution of suppliers, equipment, or inputs—which typically do not require a stockholder vote.[215] Therefore, even a GSC could effectively, if not nominally, abandon its stated social mission without any check from concerned investors or the golden shareholder.

Other aspects of the golden share model, such as the limitation on dividend payments to common stockholders, may seem to cap managers' personal gains from profit-maximizing decisions, thereby discouraging them from this path. However, as discussed in Part III.C below, these measures have limited impact and leave managers with other means of extracting private benefits from a corporation. Therefore, a GSC's managers could still have incentives to prioritize profits over purpose.

Moreover, a social mission's abandonment could be driven not just by personal greed but by other, less nefarious motives. For instance, during an economic downturn, businesses of all kinds may struggle to generate enough revenue to continue paying employees. Accordingly, to maintain their workforces, they may seek to cut costs wherever possible. To the extent that a social mission increases a business's costs, like in our example of an environmentally sustainable manufacturer, that mission's continued pursuit may lead indirectly to layoffs. In these dire circumstances, managers may justifiably give the mission less priority than their employees' livelihoods.

As in any PBC, directors of GSCs have full discretion to make these decisions if their deliberations merely "balance" competing interests between stockholders, other stakeholders, and general and specific public benefits.[216] Beyond the PBC form's limited assurances, the golden share model provides no guarantee that managers will prioritize the last of these concerns in their routine business decisions.

B. Entrenchment of Managers

A related concern regarding management arises from the golden share model's resemblance to an extreme form of dual-class stock structure.[217] In most public corporations with these structures, outside investors receive shares with one vote each, whereas managers receive shares with many

[214] *See supra* text accompanying note 128.

[215] *See* Richard D. Freer, The Law of Corporations in a Nutshell 105–06 (8th ed. 2020) ("The shareholders in the traditional statutory scheme . . . have limited power to participate in management and control. . . . The model contemplates that shareholders have decision-making authority only in discrete areas.").

[216] *See supra* text accompanying note 67.

[217] *See supra* Part II.A.1.

votes each, allowing the latter to control stockholder votes even when they hold a minority of outstanding shares.[218] The golden share model takes the dual-class structure almost to its outer limit, providing investors with no votes at all and vesting complete control in management, except with respect to the golden shareholder's limited veto rights and any common shares granted to other employees and service providers.

Therefore, certain lessons from thoroughly studied dual-class structures may apply even more strongly to the relatively new golden share variant. Scholars have demonstrated that, "as time passes, the potential costs of a dual-class structure tend to increase while the potential benefits tend to erode" and "that controllers have strong incentives to retain a dual-class structure even when that structure becomes inefficient over time."[219] These structures are "often justified on the grounds that the founder of a company going public has skills, abilities, or vision that makes her uniquely fit to be at the helm. Many years later, however, the founder's superiority as the company's leader, and with it the expected value of having the founder retain a lock on control, could erode or disappear altogether."[220] These concerns "are further aggravated when the dual-class structure enables a transfer of the founder's lock on control to an heir who might be unfit to lead the company."[221] Dual-class structures' potential costs apply not only to financial performance but also, more generally, to any misalignment between controllers' incentives and investors' preferences, whatever those preferences may be.[222]

Similarly, the golden share model could entrench initial managers who may turn out not to be the best people to run a social enterprise in the future.[223] This problem could perpetuate if their successors are appointed not for their competence but for their relationship with the incumbents.[224] Whether founders or successors, entrenched managers could underperform by both financial and social measures.

Without voting shares, investors would have no way to elect new directors to drive wayward companies back on course. Despite many social entre-

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[218] *See supra* text accompanying note 136.

[219] Lucian A. Bebchuk & Kobi Kastiel, *The Untenable Case for Perpetual Dual-Class Stock*, 103 VA. L. REV. 585, 590 (2017).

[220] *Id.* at 592.

[221] *Id.*

[222] *Id.* at 602 ("[C]ontrollers' incentives regarding certain issues may become distorted and misaligned with the preferences of public investors.") (citing Lucian Arye Bebchuk et al., *Stock Pyramids, Cross-Ownership, and Dual Class Equity: The Mechanisms and Agency Costs of Separating Control from Cash-Flow Rights*, *in* CONCENTRATED CORPORATE OWNERSHIP 295, 298–301 (Randall K. Morck ed., 2000)).

[223] In fact, this tendency may reinforce a more general problem in which businesses that engage in social activism permit underperforming managers to remain in power. *See* Giovanni Cespa & Giacinta Cestone, *Corporate Social Responsibility and Managerial Entrenchment*, 16 J. ECON. & MGMT. STRATEGY 741 (2007).

[224] Purpose expressly contemplates such arrangements. PURPOSE FOUNDATION, *supra* note 31, at 18 ("In some companies . . . , stewards select their successors, who are then confirmed or vetoed by a workers council.").

preneurs' fears regarding investors' intentions, active stockholder engagement in traditional corporations can have many benefits, like improved corporate governance practices.[225] To the extent that impact investors want a company to preserve its social mission, they could normally use their votes to ensure that directors continue working toward it. By depriving investors of this ability, the golden share model eliminates an important source of course correction.

Investors have often been willing to accept the lack of control arising from dual-class structures in the context of highly successful companies that are going public with household names and famed entrepreneurs at the helm.[226] In a publicly traded company, stockholders receive abundant required disclosures and can easily sell their shares if they dislike the company's direction. But social enterprises almost never resemble the famous corporations that manage to get away with these schemes, and GSCs may be even less likely than others to engage in public offerings.[227] Therefore, it is questionable whether enough investors would take similar risks on these types of businesses if they adopt dual-class structures through the golden share model.

C. *Opportunities to Extract Private Benefits*

The concentration of control in management, a primary purpose of steward ownership,[228] could have other negative consequences. The golden share model employs various mechanisms to limit the amount of private financial gain that managers can extract from the company, presumably so that money can remain devoted to the mission.[229] But these mechanisms are limited to restrictions on dividends, redemptions, transfers, and issuances of stock. In fact, insiders could employ alternative means of extracting wealth

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[225] Kosmas Papadopoulos, *The Long View: The Role of Shareholder Proposals in Shaping U.S. Corporate Governance (2000-2018)*, HARV. L. SCH. F. CORP. GOV. (Feb. 6, 2019), https://corpgov.law.harvard.edu/2019/02/06/the-long-view-the-role-of-shareholder-proposals-in-shaping-u-s-corporate-governance-2000-2018 ("Over the past three decades, shareholder proposals have transformed the corporate landscape in the U.S. by spurring the adoption of governance best practices. Annual director elections, majority vote rules for director elections, shareholder approval for poison pills, and proxy access bylaws are some of the critical governance practices that have become common practice thanks to investor support for shareholder proposal campaigns led by a wide variety of investors—some large; others small.").

[226] Choi, *supra* note 135, at 55 (mentioning Facebook, Fitbit, Google, Groupon, LinkedIn, Shake Shack, Snap, and Yelp as well-known examples of public companies with dual-class structures); Aggarwal et al., *supra* note 135, at 3 ("When founders have greater bargaining power . . . they are more likely to be able to negotiate for greater control rights at the time of IPO, and thus, the firm is more likely to adopt a dual-class structure."); *id.* at 4 (showing that "dual-class structures tend to be determined at the IPO stage," with those structures "created prior to the IPO negotiation process in about 80 percent of these firms").

[227] BRAKMAN REISER & DEAN (2017), *supra* note 33, at 101 ("Most social enterprises, like most businesses, simply won't ever be large enough to qualify for an IPO, or to have the wherewithal to pay its price of admission."); *supra* text accompanying note 192.

[228] *See supra* text accompanying note 89.

[229] *See supra* text accompanying notes 109–11.

and other "private benefits of control" from the corporation without implicating any of these restrictions.[230]

Notably, when insiders constitute a majority of the board, as is expected in the golden share model, they can increase officers' and other employees' salaries, bonuses, and other cash compensation. Unlike dividends, which must be paid proportionately to all stockholders of a class,[231] these compensation decisions could be targeted only at managers themselves or at certain other employees that they want to enrich.[232] That way, in the aggregate, these targeted compensation payments would be smaller than equivalent dividend payments, leaving more money in the corporation for business activities. Therefore, depending on certain tax considerations,[233] even directors and officers who are loyal to the corporation may have incentives to use compensation rather than dividends to pay themselves. Because dividends are one of the primary ways in which investors can receive financial returns from stock in a GSC,[234] this misalignment of incentives could trouble them.

Managers could probably get away with this tactic in many situations. First, Delaware corporations are not legally required to declare dividends, and courts will not compel them to do so absent "an oppressive or fraudulent abuse of discretion."[235] Second, unlike tax-exempt nonprofit organizations,

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[230] For a summary of the theory of private benefits of control, see Mark J. Roe, *Rents and Their Corporate Consequences*, 53 Stan. L. Rev. 1463, 1487 (2001) (defining this benefit as "the value that controlling stockholders can divert to themselves in related-party contracts that legal institutions fail to eliminate, in excess salaries or in a better life").

[231] Ziel Charter, *supra* note 97, V.B.1.

[232] For a more general concern regarding unequal distribution of corporate resources, see Choi, *supra* note 135, at 58 ("[A] controlling shareholder can influence how the fruits of enhancing the firm's performance are divided among shareholders. Rather than making a pro rata distribution to all shareholders, she can divert that cash flow through various means, such as transactions with a controlled company or investments in pet projects.").

[233] *See* Menard, Inc. v. Comm'r, 560 F.3d 620, 621–22 (7th Cir. 2009) ("A dividend, like salary, is taxable to the recipient, but unlike salary is not deductible from the corporation's taxable income. . . . As a result of a change in law in 2003, dividends are now taxed at a lower maximum rate than salaries—15 percent, versus 35 percent for salary. 26 U.S.C. § 1(h)(11). This makes the tradeoff more complex; although the corporation avoids tax by treating the dividend as a salary, which is deductible, the employee pays a higher tax. But depending on its tax bracket, the corporation may still save more in tax than the employee pays, and in that event, if the employee owns stock in the corporation, he may, depending on how much of the stock he owns, prefer dividends to be treated as salary.") An additional consideration is that salary payments, unlike dividends, are subject to federal (and possibly state and local) employment taxes, including those for social security and Medicare. Stephen Schwarz & Daniel J. Lathrope, Fundamentals of Corporate Taxation 725–26 (10th ed. 2019).

[234] *See infra* text accompanying notes 249–54.

[235] Buckley Fam. Tr. v. McCleary, 2020 WL 1522549, at *5 (Del. Ch. 2020) (quoting Gabelli & Co., Inc. v. Liggett Grp., 479 A.2d 276, 280 (Del. 1984)). Findings of oppression are exceedingly rare in Delaware. In one of the only cases, the directors withheld dividends to pressure a minority stockholder to sell his shares to them at a discount. Due to the corporation's Subchapter S election, the stockholder had to pay taxes on the corporation's income even without receiving distributions. *See* Buckley, 2020 WL 1522549, at *6 (citing Litle v. Waters, 1992 WL 25758 (Del. Ch. 1992)). In addition, Delaware courts would not typically order a corporation to repurchase an aggrieved minority stockholder's shares instead of declaring dividends. *See* Blaustein v. Lord Baltimore Cap. Corp., 2013 WL 1810956 at *16 (Del. Ch. 2013), aff'd, 84 A.3d 954 (Del. 2014) ("[U]nder Delaware law the directors of a corporation (or

PBCs are not subject to limits or penalties regarding executive compensation.[236] Third, Delaware's conflict-of-interest rules may have little practical effect in limiting executive compensation in a GSC. Normally, when challenged in court, directors' decisions regarding their own compensation are subject to the heightened "entire fairness" standard of review, under which the directors must prove that the compensation is "entirely fair to the corporation,"[237] a significant hurdle. However, if ratified by "a majority of fully informed, uncoerced, and disinterested stockholders," those decisions are subject instead to the more "deferential business judgment standard."[238] In that case, "directors can take self-interested action secure in the knowledge that the stockholders have expressed their approval."[239]

In a GSC, investors cannot vote at stockholder meetings,[240] so they would be excluded from the ratification process.[241] Instead, approval by only a majority of the common shares, held entirely by managers and perhaps other employees and service providers, would suffice to insulate a board compensation decision from heightened scrutiny. Therefore, if each director's compensation package is submitted to a stockholder vote which excludes any shares held by that director, then the directors could together set their own pay in compliance with Delaware law, without any check from investors. They would have even more freedom to set non-directors' compensation, which, absent a separate conflict of interest, would be limited only by the doctrine of corporate waste.[242] Claims based on waste are exceedingly difficult to prove and are sustained only in the most extreme situations,[243] so this doctrine is unlikely to provide much deterrent or corrective effect on directors' actions.

controlling stockholders) do not have a special fiduciary duty to minority stockholders or a general duty to buy them out.") (citing Nixon v. Blackwell, 626 A.2d 1366, 1379–80 (Del. 1993)).

[236] Payments of excess compensation by a tax-exempt organization could result in excise taxes on the organization and on its employees. 26 U.S.C. §§ 4960, 4968.

[237] In re Investors Bancorp, Inc. Stockholder Litig., 177 A.3d 1208, 1211 (Del. 2017).

[238] *Id.*

[239] *Id.*

[240] *See supra* text accompanying note 113.

[241] *See* Steven M. Haas & Charles L. Brewer, *Nonvoting Common Stock: A Legal Overview*, HARV. L. SCH. F. CORP. GOV. (Nov. 30, 2017), https://corpgov.law.harvard.edu///30/nonvoting-common-stock-a-legal-overview ("Delaware's interested directors statute . . . appears to provide that the only stockholders who can cleanse an interested transaction under the safe harbor are the voting stockholders.") (citing DEL. CODE ANN. tit. 8 § 144(a)(2)).

[242] Brehm v. Eisner, 746 A.2d 244, 262 n.56 (Del. 2000) ("To be sure, directors have the power, authority and wide discretion to make decisions on executive compensation. *See* [DEL. CODE ANN. tit. 8] § 122(5). As the often-cited Court of Chancery decision by Chancellor Seitz in *Saxe v. Brady* warns, there is an outer limit to that discretion, at which point a decision of the directors on executive compensation is so disproportionately large as to be unconscionable and constitute waste.") (citing 184 A.2d 602, 610 (Del. Ch. 1962)).

[243] *Id.* at 263 ("Roughly, a waste entails an exchange of corporate assets for consideration so disproportionately small as to lie beyond the range at which any reasonable person might be willing to trade. Most often the claim is associated with a transfer of corporate assets that serves no corporate purpose; or for which no consideration at all is received. Such a transfer is in effect a gift. If, however, there is *any substantial* consideration received by the corporation,

Finally, compensation decisions are not the only potential source of opportunism by controlling stockholders. Instead, they can also extract "non-pecuniary benefits" of corporate control, such as "carrying on a family legacy, acquiring political clout by running a large enterprise, building a conglomerate empire, and pursuing pet projects."[244] Moreover, this "[p]rivate benefit extraction is done primarily through operation and management of the corporation" on a day-to-day basis, as opposed to "sale of control transactions and freeze-outs" (i.e., purchases of minority stockholders' shares).[245] Even in an ordinary corporation, these routine activities are not subject to stockholder approval, and in a GSC, the golden shareholder could not veto them either.[246] Therefore, directors would have even more freedom to extract non-pecuniary benefits than pecuniary ones, in many cases without even informing investors, let alone seeking their approval.

Of course, if managers run a company as just a tool for extracting private benefits, then current investors will suffer, but in the future, prospective investors who perform even a modicum of due diligence are unlikely to fund the company further. In addition, excessive extraction of these benefits could lead the company to underperformance or even insolvency. Absent legal constraints, these reputational and financial incentives could limit managerial abuse to a certain extent, but they apply in all corporations and are no different in a GSC. For managers who underappreciate those incentives, the golden share model makes it easier to exploit current investors by depriving them of any ability to block extractive decisions or replace the directors who make them.

D. Lower Financial Returns for Investors

Even without managerial maneuvers to avoid payments to investors, the golden share model may limit social enterprises' access to capital by promising lower financial returns than traditional corporate structures. One could portray this as a "feature" of the model rather than a "bug"—that is, a desirable sorting mechanism that deters investors who are too focused on profits and attracts those who put mission first. But social enterprises are not charities, and they are supposed to pursue financial returns along with public

and if there is a *good faith judgment* that in the circumstances the transaction is worthwhile, there should be no finding of waste, even if the fact finder would conclude *ex post* that the transaction was unreasonably risky.") (citing Lewis v. Vogelstein, 699 A.2d 327, 336 (Del. Ch. 1997)) (emphasis added).

[244] Choi, *supra* note 135, at 58 n.17.

[245] *Id.* at 80.

[246] *See supra* text accompanying note 128.

benefits.[247] It is not clear that the golden share model strikes the optimal balance in the deal that it offers investors.[248]

In this model, preferred stockholders can receive financial returns on their investments through dividends, share redemptions, and private stock sales.[249] As to the first of these categories, GSCs can structure dividends in different ways.

Most simply, as in a typical corporation, directors could declare dividends in their own discretion.[250] For several reasons, however, investors should not count on discretionary dividends as a reliable source of financial return. First, unlike in a typical corporation, investors in a GSC cannot use their votes to incent directors to pay dividends. Second, closely held corporations and startup companies rarely pay dividends,[251] so no industry standard would encourage early-stage GSCs to do so either. Third, directors may not have personal incentives to declare dividends, because they can instead pay themselves through compensation without sharing any returns with investors.[252]

Alternatively, the charter could provide for automatic dividend payments of a preset amount after the corporation achieves a certain financial milestone.[253] Under this approach, investors do not have to rely on directors' discretionary generosity to receive dividends. However, even these automatic payments are ordinarily subject to limits in time and money. For instance, with respect to each share of preferred stock, Creative Action Network's charter provides for dividends until the charter's fifth anniversary or until the stockholder has received five times that share's original issuance price, whichever is earlier.[254] This cap sharply restricts preferred stockholders' potential returns, in contrast to an ordinary corporation, which imposes no aggregate limits on dividends.

[247] Brakman Reiser & Dean (2017), *supra* note 33, at 10 ("Social entrepreneurs and investors . . . do not aspire to be charities. They want to generate profits, to sustain their businesses, and to more than merely make a living."); McDonnell (2017), *supra* note 22, at 722 (noting that "founders and investors of benefit corporations do seek profit (or else they could form as nonprofits and gain tax advantages)").

[248] *See infra,* note 262 and accompanying text (arguing that different investors have different preferences in the balance between financial and social returns. From a company's perspective, the "optimal balance" would be the one that attracts the greatest amount of investment from the most desirable investors).

[249] *See supra* Part I.D.2.

[250] *See supra* text accompanying note 117.

[251] Schwarz & Lathrope, *supra* note 233, at 153 ("Closely held companies, influenced by the federal tax law, typically resist paying dividends and expend considerable energy to avoid the sting of the double tax."); Joshua Brustein, *Kickstarter Just Did Something Tech Startups Never Do: It Paid a Dividend*, Bloomberg (June 17, 2016), https://www.bloomberg.com/news/articles/2016-06-17/kickstarter-just-did-something-tech-startups-never-do-it-paid-a-dividend ("People who follow the venture capital industry were hard-pressed to come up with a single example of a VC-backed startup that has ever paid regular dividends.").

[252] *See supra* text accompanying notes 231–34.

[253] *See supra* text accompanying note 118.

[254] CAN Charter, *supra* note 97, at 4.4.1.2, 4.4.1.8, 4.4.2.3.

In contrast to dividends, preferred stockholders may have some control over share redemptions, if the charter permits them to request these anytime after a specified date.[255] In that case, they receive at most a fixed multiple of their purchase price for each share, depending on the corporation's earnings over the ensuing years.[256] As with the capped approach to dividends described above, stockholders' potential return on investment through redemptions is precisely limited.

With little promise from dividends and redemptions, investors should consider the potential for stock sales to provide adequate financial returns. Indeed, unlike other classes of stock, preferred stock in a GSC is freely transferrable. However, this model's capped returns on dividends and redemptions would likely depress the resale value of that stock, as prospective buyers discount its expected financial returns accordingly.

This downward effect on prices would apply not just to secondary sales but also in other contexts. For instance, as potential sources of liquidity for investors in a steward-owned company, Purpose suggests public offerings of nonvoting stock and a sale of the company to another steward-owned company with "a common purpose and operating philosophy."[257] In an ordinary startup, initial public offerings and M&A transactions are typically the most desired "exits" for investors.[258] With a GSC, however, the limited financial returns of preferred stock under this model would discount the price that buyers would be willing to pay for each share in any offering. Moreover, the suggestion of a sale of the company seems to conflict with the golden shareholder's apparent obligation to veto any such transaction.[259] Therefore, in no context should investors count on stock sales to public investors or acquirers as a lucrative source of financial return from a GSC.

These considerations raise interesting implications for potential investments in these organizations. Two advantages of equity over debt are an indefinite potential for financial returns and the right to vote as a stockholder. But preferred equity in a GSC bears neither of these benefits. Its upside is precisely limited, with caps on dividends and redemptions, which in turn would depress its resale value. Nor does it afford any voting rights, aside from protective provisions applicable to certain extraordinary events.[260]

These limitations may deter investors. In companies other than GSCs, impact investors tend to prefer equity over debt,[261] and they are sometimes

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[255] *See supra* text accompanying note 119.
[256] *See supra* text accompanying note 120.
[257] PURPOSE FOUNDATION, *supra* note 31, at 36.
[258] *See supra* note 189 and accompanying text.
[259] *See supra* text accompanying note 128.
[260] *See supra* text accompanying notes 113-16.
[261] Christopher Geczy et al., *Contracts with (Social) benefits: The implementation of impact investing*, J. FIN. ECON. (forthcoming 2021), at 17 (reporting that impact funds have a "preference for equity" over debt investments).

willing to accept below-market returns.[262] But they may be less likely to accept the golden share model's defined limits on those returns, especially when that model does not assure preferred stockholders that managers will reliably pursue both profit and purpose.[263] Absent an external reason to trust a social entrepreneur, such as a personal relationship or record of successful ventures, investors may find preferred stock's substandard economic and control rights to constitute too little reward for the attendant risks of mission drift and financial failure.

Indeed, Ziel's founder had previously cofounded Shapeways, which eventually became the world's leading 3D printing service and marketplace, raising nearly $50 million in equity investment from some of the leading venture capital firms during her leadership.[264] But even she had great difficulty in "find[ing] investors who would be willing to fund a [GSC]. Many investors were reluctant to [forego] voting rights [and] were also concerned about making a return on their investment."[265] To address these concerns, Ziel "created a deal structure similar to an equity loan where in five years Ziel would use 30 percent of its cash flows to pay back its investors."[266] Even then, the company appears to have found only three investors willing to participate in this structure over the past five years.[267]

If even an established entrepreneur with a highly successful record had so much difficulty in convincing investors to purchase preferred stock in a GSC, other founders should expect similar or greater challenges. As with Ziel, impact investors may choose to fund the company, if at all, using secured debt instruments. If they are interested in the standard repayment schedule associated with the golden share model, a debt investment could

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[262] *Id*. at 2 (contrasting impact "funds targeting market returns (market-rate-seeking, or MRS, funds) and those with lower financial targets (nonmarket-rate-seeking, or NMRS, funds), where the NMRS group's willingness to forgo higher financial returns implicitly elevates the impact objective"); Global Impact Investing Network, *supra* note 45 ("Impact investments target financial returns that range from below market (sometimes called concessionary) to risk-adjusted market rate."); Eldar (2020), *supra* note 33, at 954 (noting that some impact investors "claim to pursue social impact at the expense of profits").

[263] *See supra* Part III.A.

[264] Crunchbase, *Marleen Vogelaar*, https://www.crunchbase.com/person/marleen-vogelaar (last visited Sept. 17, 2021) (showing that Marleen Vogelaar was COO and CFO at Shapeways from January 2008 to July 2014); Crunchbase, *Shapeways – Financials*, https:// .crunchbase.com/organization/shapeways/company_financials (last visited Sept. 17, 2021) (showing that, during this period, Shapeways raised $46.3 million from equity financings from eight investors, including Andreesen Horowitz and Union Square Ventures); *The Top 20 Venture Capital Investors Worldwide*, N.Y. TIMES (Mar. 13, 2016) (listing the founders of Andreesen Horowitz and Union Square Ventures among the top 20 venture capitalists in the world based on factors like "connectedness" and "exits").

[265] BROWN ET AL., *supra* note 29, at 30.

[266] *Id.*

[267] Crunchbase, *Ziel*, https://www.crunchbase.com/organization/ziel (last visited Sept. 17, 2021) (showing that, since 2017, Ziel has raised equity financing from Borski Fund, Hatzimemos / Libby, and Newark Venture Partners).

follow a revenue-based financing model like Ziel did.[268] This would similarly permit the company to repay the funding amount as a percentage of its revenue over time.[269] In contrast to equity, however, secured debt would offer valuable benefits to investors in the form of restrictions under loan agreements, security interests in corporate assets, and priority in liquidations.[270] This last point may be particularly important in the context of social enterprises, which tend to be small businesses that are more likely to fail without sufficient resources to pay all creditors and stockholders.[271] Under last year's Small Business Reorganization Act, security interests are now more essential than ever for investors in small businesses.[272] In addition, GSCs should expect impact investors to request a guaranteed board seat as part of any substantial investment.[273]

Of course, grants of security interests, control rights, and directorships would undermine the golden share model's promise of managerial independence, so many adherents of steward ownership will resist these concessions. If founders adamantly maintain these principles, they will likely face difficulty in securing investment.

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[268] Regarding revenue-based financing ("RBF"), see J. Brad Bernthal, *The Evolution of Entrepreneurial Finance: A New Typology*, 2018 B.Y.U. L. Rev. 773, 792–93 (2018) ("RBF agreements have two significant economic terms. One, a debtor company pays back the loan as a percentage (typically in the 4-5% range) of its top line monthly cash receipts. . . . The startup's revenue-based payments continue, acting as a lien on future revenues, until the investment is repaid up to an agreed-upon multiple, such as three times the original investment. Two, RBF caps an investor's upside (i.e., profits) associated with the investment. Once a debtor startup pays back three times the loan to [the lender], for example, then the loan is repaid.") (citations omitted).

[269] *See supra* text accompanying notes 121–123.

[270] *See* Bernthal, *supra* note 268, at 793–94 ("From a control perspective, RBF structures investment as a loan secured against the company's assets. As a lender, the RBF investor has a priority over shareholders in case of liquidation of the company. . . The lender does not take a governance role in the startup. Instead, the debtor startup agrees to a restrictive covenant that restricts how loan proceeds will be used and, further, limits the company's ability to incur additional indebtedness absent lender consent.") (citations omitted).

[271] *See* sources cited *supra* note 37. *See also* Christopher G. Bradley, *The New Small Business Bankruptcy Game: Strategies for Creditors under the Small Business Reorganization Act*, 28 Am. Bankr. Inst. L. Rev. 251, 258 (2020) ("Often, small businesses have a primary creditor that has financed much of the debtor's operations and that attains a senior secured position, but that by the time of the bankruptcy has collateral worth far less than the amount of its claim. Such a creditor has not only a security interest in substantially all of the debtor's assets but also a substantial unsecured deficiency claim, often larger than all other unsecured claims combined.").

[272] Bradley, *supra* note 271, at 284 ("Subchapter V [of chapter 11 of the Bankruptcy Code] is unlikely to dampen the influence of powerful creditors, such as senior secured creditors with large deficiency claims. They will retain significant leverage. Subchapter V will likely redistribute power primarily from the other creditors—junior secured and unsecured creditors—to the debtor.").

[273] *See* Geczy et al., *supra* note 261, at 12 (reporting that "impact funds and [market-rate seeking] funds in particular frequently contract for guaranteed [portfolio company] board seats").

E. Dependence on the Golden Shareholder

Trust between managers and investors is essential for all kinds of social enterprises to access the capital that they need to grow beyond the realm of small business.[274] Moreover, for the golden share model in particular to function as intended, managers and investors must not only trust each other to adhere to the public-interest mission, but also trust the golden shareholder to indefinitely and reliably exercise its rights under the charter. Any doubts about that organization could, in turn, undermine its benefits in promoting trust between managers and investors.

Dependence on the golden shareholder may be less problematic when its rights involve no discretion but simply unequivocal directives, such as rejecting any proposed sale of the company or amendment to certain charter provisions. Under that arrangement, because the golden shareholder must be, like the Purpose Foundation, a nonprofit organization that is devoid of economic owners and obligated by its organizational documents to veto any such action,[275] managers and investors can rest easy to an extent.

Of course, no private organization can be expected to last forever or to maintain the same policies perpetually. If the veto service provider dissolves or changes its policies so that it no longer meets the charter's strict criteria for a golden shareholder, then the organization's GSCs would have to find alternative providers that meet those criteria. If no eligible organizations are readily available, then each GSC may have to redeem its golden share,[276] rendering its charter and the golden share model unworkable.

In addition, veto services are not free. Even if fees are affordable at first, a veto service provider could subsequently raise them knowing that the corporation cannot easily find an alternative, leaving the corporation at a monopolist's mercy.

Therefore, before forming or investing in a GSC, one must have faith in the golden shareholder to last at least as long as the company and for its relevant policies and pricing to remain materially the same for the entire duration. Alternatively, one would have to hope that the golden share model spreads widely enough that other veto service providers emerge and can substitute for the initial choice if necessary. The entire model depends on the reputation of the chosen veto service provider or on the expansion of a very small niche.

Furthermore, a corporation could grant the golden shareholder more authority than just rights to mechanically block certain actions. Indeed, some companies provide that the golden shareholder appoints or approves successors to the managers.[277] To the extent that the golden shareholder exercises

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[274] *See supra* Part II.A.
[275] *See supra* text accompanying notes 129–132.
[276] Ziel Charter, *supra* note 97, at V.C.3; CAN Charter, *supra* note 97, at 4.3.3.
[277] *See supra* text accompanying note 108.

any discretion, especially in decisions as important as the company's leadership, it must employ independent and informed judgment consistent with the company's mission. Unlike veto services, this ability over time cannot be assured by provisions in the organization's constitutional documents. A mere change in the golden shareholder's staff could compromise its fitness to make these decisions and, ultimately, lead to undesirable actions. Therefore, even if founders initially trust the veto service provider's representatives enough to delegate critical discretionary authority to them, managers and investors alike should consider whether the golden shareholder can be expected to perform it well in the long term.

* * *

To its credit, the golden share model succeeds in enshrining a company's mission more indelibly in its charter than does the PBC form alone, in which a majority of stockholders can erase or alter it at any time.[278] In addition, by preventing a sale of the company to an acquirer that would strip away its mission, this model addresses one of the most outsized concerns in the social enterprise sector.[279]

But in its present form, this approach does not bridge the trust gap between managers and investors that inhibits this sector's growth. Most critically, no matter how precise a charter's statement of the corporation's specific public benefit, the pursuit of that benefit depends on day-to-day decisions that are not subject to the golden shareholder's veto. Moreover, those decisions evade even indirect oversight by investors, which cannot vote to replace wayward directors as they could in an ordinary corporation. And as in any PBC, the default legal recourse for failure to pursue that benefit is a stockholder derivative lawsuit, which is too expensive and ineffective to assuage rational impact investors' concerns of mission drift.[280]

Instead, the default golden share model may actually exacerbate these concerns, by entrenching managers who may turn out to be inept and enabling them to extract private benefits from the corporation, without any check from investors. Given the sharply limited economic returns offered by this model to preferred stockholders, impact investors may find equity in a GSC too financially unpalatable to warrant the potential for impact washing and other, even worse managerial abuses.[281]

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[278] *See supra* text accompanying note 74.
[279] *See supra* text accompanying note 188.
[280] *See supra* note 72 and accompanying text.
[281] Regarding impact washing, see *supra* note 46 and accompanying text.

IV. Proposed Improvements to the Golden Share Model

Despite these obstacles, to incent investors to accept the limited financial returns and lack of control that the golden share model offers them, a business could make various changes to further promote trust with investors and raise capital. To enhance this model, a GSC could adopt each of this Part IV's three proposals either alone or in combination with the others.

A. *Impact Metrics*

First, to address the golden share model's lack of mission prioritization,[282] a company could employ impact metrics to assure investors of its commitment to certain social objectives. These metrics take many forms and can be implemented in various ways.

"Impact measurement and management" has always been "integral" to impact investing.[283] Over the past decade, investors in this sector have shifted dramatically from primarily using "proprietary measurement systems to measure their impact" to overwhelmingly adopting standardized systems.[284] They use different standards for different purposes.

For "shaping impact targets and processes," "[i]mpact investors most commonly rely on the United Nations' Sustainable Development Goals (SDGs)."[285] These are a set of seventeen broad goals intended "to achieve a better and more sustainable future for all. They address the global challenges we face, including poverty, inequality, climate change, environmental degradation, peace and justice."[286] For example, the goals most directly relevant to environmental concerns are "Clean Water and Sanitation," "Affordable and Clean Energy," "Sustainable Cities and Communities," "Responsible Consumption and Production," "Climate Action," "Life Below Water," and "Life on Land."[287] Impact investors can use these categories to identify which goals they want to pursue.

Once those goals are identified, "IRIS+ is the generally accepted system to measure, manage, and optimize impact."[288] Maintained by the Global Impact Investing Network, this system includes a vast catalog of "numerical measures used in calculations or qualitative values to account for the social, environmental and financial performance of an investment."[289] These metrics should be chosen and analyzed carefully with respect to a given mission.

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[282] *See supra* Part IV.A.
[283] Hand et al., *supra* note 47, at 48.
[284] *Id.*
[285] *Id.*
[286] United Nations, *Sustainable Development Goals*, United Nations, https://sdgs.un.org (last visited Sept. 17, 2021).
[287] *Id.*
[288] Global Impact Investing Network, *IRIS + System | Standards*, https://iris.thegiin.org/ (last visited Sept. 17, 2021).
[289] *Id.*

To continue a previous example,[290] a manufacturer that uses sustainable materials and production practices could choose a suite of IRIS+ metrics specific to those practices, like the one entitled "Biodegradable Materials (OI5101)," which measures the "[a]mount of biodegradable materials used in the organization's products (including packaging) during [each] reporting period."[291]

These metrics' wide variety permits targeted assessments of a company's impact and progress toward a specific mission. But if that progress is measured only by the company, then investors may worry about opportunities for manipulation.[292] Accordingly, a fair evaluation of an enterprise's success or failure in meeting these standards would require regular monitoring and reporting by an independent outside expert.[293] Unfortunately, this may raise transaction costs to the point that they exceed perceived benefits.[294] In addition, despite the metrics' diversity, some companies may not find any that would accurately measure success in their missions.

If businesses and investors find the IRIS+ metrics too inaccurate or their implementation too costly, then they can rely on various alternatives instead. They could choose a much broader measure, like the "balance of expenditures made in pursuit of profit and those made in pursuit of social good."[295] This would require preparation and review of financial reports, but these practices are common in investment relationships anyway, so they may not increase costs as much as the use of more targeted impact metrics. A bigger problem with this approach may arise from its vagueness; investors could easily disagree with the company's classification of expenditures in the broad categories of "profit" and "social good."[296]

Alternatively, to avoid these potential disputes, the parties could choose more specific goals separate from the IRIS+ metrics, as when the founder of the White Dog Café in Philadelphia licensed its name and required the licen-

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[290] *See supra* text accompanying note 208.

[291] Global Investing Network, *Biodegradable Materials (OI5101)*, Global Impact Investing Network, https://iris.thegiin.org/metric/5.2/Ol5101 (last visited Sept. 17, 2021).

[292] Deborah Burand, *Contracting for Impact: Embedding Social and Environmental Impact Goals into Loan Agreements*, 13 N.Y.U. J.L. & Bus. 775, 809 (2017) ("While an impact-seeking lender may try to choose [key performance indicators] whose achievement are within the borrower's control, . . . today's control can morph into tomorrow's manipulation.").

[293] *Id.* at 809–10 ("Where there is a risk that the borrower will try to manipulate attainment of the [key performance indicator], it may be wise to use an external validator to measure performance of the [indicator].").

[294] *Id.* at 811 ("[F]inding an appropriate external validator and then securing sufficient financial resources to pay for such an external validator's services could overwhelm the size of the transaction at hand.").

[295] Brakman Reiser & Dean (2017), *supra* note 33, at 37 (using this test in the proposed "mission-protected hybrid" form).

[296] Regarding the potential for vague "standards," as opposed to precise "rules," to lead to disputes, see Cathy Hwang & Matthew Jennejohn, *Deal Structure*, 113 Nw. U. L. Rev. 279, 288 (2018) ("[D]rafting a standard is relatively low-cost ex ante, but opens the door to misunderstanding and expensive litigation ex post. Standards also open the door to greater judicial error costs.").

see "to use renewable energy, purchase fair-trade ingredients, and meet a range of other sustainable sourcing, green production, and local ownership commitments."[297] These more precise rules could be more difficult to formulate and agree on in the first place but may be less open to disagreement later.[298]

If companies choose to employ social impact metrics, whether from an established database like IRIS+ or a customized variety, then they could implement them through several means. First, impact investment contracts frequently incorporate these metrics into various provisions, often as a way "to align (or reinforce an alignment of) [a business's] financial and social interests."[299] For example, the company's satisfaction of a certain set of metrics could be a condition to an investor's obligation to pay successive tranches.[300] Contracts may also "provide interest rate relief (or increases) depending on the progress made toward agreed-upon impact objectives"[301] or "relax or delay repayments of loans if specified [indicators] are achieved."[302] More punitively, the company's failure to meet certain metrics could be an event of default, permitting the investor to accelerate repayment obligations and terminate the contract.[303] In a convertible debt instrument, metrics could trigger the lender's right to convert the outstanding loan into equity or could affect the price at which that conversion occurs.[304] Through either encouragement or deterrence, each of these provisions could incent companies to pursue their missions.

Though common, these contractual approaches have drawbacks in the context of a social enterprise that seeks to promote trust with investors more generally, beyond the confines of a single investment agreement. First, different investors could insist on different metrics, imposing conflicting or confusing obligations on the company.[305] Second, only sophisticated investors would have the means to identify and negotiate for these metrics' inclusion, which could inhibit the enterprise's ability to appeal to retail investors, as through equity crowdfunding or public offerings of nonvoting stock.[306]

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[297] Brakman Reiser & Dean (2017), *supra* note 33, at 159.

[298] *See* Hwang & Jennejohn, *supra* note 296, at 287–88 ("[U]sing a [precise] rule—which costs more to draft up front—reduces enforcement costs down the line, because rules reduce the probability of misunderstanding, dispute, and the time spent on litigation when disputes do arise.").

[299] Burand, *supra* note 292, at 795.

[300] *Id*. at 799 ("[T]he lenders may decide to disburse additional loan amounts to a borrower only if and when certain agreed-upon [key performance indicators] are achieved.").

[301] *Id*.

[302] *Id.* at 803.

[303] *Id*. at 800–01.

[304] *Id*. at 805–07.

[305] *Id*. at 792–93 ("[T]he costs (financial, time, or otherwise) of collecting and reporting on the [key performance indicators] are high. These costs can be compounded if the borrower has different reporting requirements imposed by its lenders and other stakeholders (such as other investors, donors, and government regulators).").

[306] *See* Brakman Reiser & Dean (2017), *supra* note 33, at 104–09 (explaining equity crowdfunding and analyzing its potential benefits to social enterprises); Eldar (2020), *supra*

Similarly, negotiating different contracts with different investors could be costly for the company as well. Finally, a contractual approach may be more appropriate in debt financings, which typically involve negotiated loan agreements and promissory notes,[307] than in the preferred equity financings contemplated by the golden share model. Indeed, the most common ways to incorporate impact metrics into loan agreements are specific to debt, focusing on disbursements, interest, repayment, and conversion. None of these provisions would make sense in a stock purchase agreement.

Instead of relying on individual contracts, a GSC could implement social impact metrics in a completely novel way, by intertwining them into its charter and bylaws. Indeed, Delaware law requires a corporation with multiple classes of stock to specify in its charter the rights that apply to each class.[308] In this case, if metrics are to trigger rights of preferred stockholders, then they should be included in the charter, not just in a contract.

Metrics could be integrated into the organizational documents in different ways. For example, the charter could provide that a failure to satisfy a set of metrics over a given period could enable preferred stockholders to demand redemption. To avoid disputes with investors and assuage fears of manipulation, the company could require an independent outside expert to determine whether a metric is satisfied, if the costs are affordable. In addition, to prevent individual investors from exiting after a single failure, the company could condition the redemption right on majority approval by preferred stockholders.[309] In any event, this right should be structured so that its exercise would not automatically imperil the corporation's finances. For instance, upon such a demand, redemption might occur not all at once, but over a more accelerated timeframe than the charter's normal redemption schedule.[310] To avoid these increased payments, managers would have a financial incentive to satisfy the specified metrics.

Alternatively, or in addition, the corporation's bylaws could provide that a failure to satisfy certain metrics could permit preferred stockholders to participate in the next annual election of directors by nominating and voting for candidates.[311] Any such procedure would need to be consistent with the

note 33, at 952 ("While control and contractual devices may work well for investors who have a significant stake in a particular social enterprise, they are generally ineffective in reassuring a large segment of subsidy providers: dispersed investors or consumers who wish to contribute small amounts to social enterprises."); *supra* text accompanying note 193.

[307] *See generally* Burand, *supra* note 292 (exploring the use of impact metrics in loan agreements).

[308] Del. Code Ann. tit. 8, § 151.

[309] This provision would be analogous to other common investment arrangements, such as a provision in a convertible promissory note that requires, upon the note's maturity, the election of a majority in interest of all noteholders before any note converts into equity. *E.g., Convertible Note Purchase Agreement with Short-Form Note (Seed-Stage Startup)*, at §§ 1.13, 4.3, Thomson Reuters Prac. L., https://. . .com/-6699 (last visited Sept. 17, 2021).

[310] Regarding a normal redemption schedule, see *supra* text accompanying notes 119–23.

[311] Provisions regarding director election procedures typically appear in a corporation's bylaws rather than its charter. *See Forming and Organizing a Corporation*, Thomson Reuters Prac. L., https://us.practicallaw.thomsonreuters.?com/7-381-9674 (last visited Sept. 17, 2021).

company's succession policy, which is an essential part of steward ownership.[312] In a typical golden share corporation, only certain common stock is ordinarily permitted to vote at stockholder meetings, including those at which directors are elected.[313] Because only managers and perhaps other employees and service providers hold that stock, only these insiders choose the directors. This arrangement could easily lead to a self-perpetuating board. However, if preferred stockholders are temporarily enfranchised due to a metric failure and collectively hold enough shares to outvote common stockholders in an election, then incumbent directors could face the prospect of replacement. This could provide such a company's managers with a powerful incentive to pursue the social mission in their day-to-day business decisions, which the default golden share model does not provide.[314]

A potential obstacle to this proposal is that in many companies, especially those at the earliest stages, shareholding is so concentrated in management that they would retain majority voting control even when investors can participate. For instance, the founders may hold ten million shares of voting common stock, and investors may hold two million shares of nonvoting preferred stock. In that case, temporarily enfranchised investors holding only a minority of voting shares would not suddenly gain the power to elect new directors. Their one-time votes would be ineffectual and would not provide the desired incentive to satisfy the metrics. With proper planning, however, this situation can be avoided.

First, with a typical par value of a fraction of a cent,[315] shares of common stock can be issued to founders in greater or lesser numbers with little financial consequence. In the preceding example, it would make practically no difference to issue one million shares instead of ten million to the founders. To retain the same relative voting power with respect to common stock, they would simply have to issue ten times fewer common shares to employees and service providers. But this change could increase the relative voting power of preferred stock in a contested election, thus creating this proposal's intended incentive for management.

Second, preferred stock and common stock are priced separately to reflect the different rights associated with each class.[316] Consequently, almost regardless of the common stock's fair market value, investors could negotiate for a greater number of preferred shares for the same aggregate purchase

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[312] *See supra* text accompanying notes 107–08.

[313] *See supra* text accompanying notes 109-10, 113, 128. Protective provisions for preferred stockholders do not grant the right to vote in director elections. *See supra* text accompanying notes 115-16.

[314] *See supra* Part III.A.

[315] *See supra* note 171 and accompanying text.

[316] Bagley & Dauchy, *supra* note 40, at 97 ("[B]y issuing venture investors stock that has preferential rights over the common stock, the company can properly value the common stock issued to founders and other service providers at a discount from the price paid by the venture investors for their preferred stock. By issuing preferred stock to investors, the company can justify a lower fair market value for the common stock.").

price, which would reduce the price per share. With more shares, they would have more votes and a greater impact in contested director elections. To the same effect, the price and number of shares could stay the same, but the charter could assign to each preferred share multiple votes in those elections, such that the investor vote would rival the manager vote.

Of course, founders may not like any approach that could threaten their positions under certain circumstances. But if investors care enough about incenting management to pursue a mission, then they could use the leverage afforded by their capital to insist on adjusting the number or voting power of their preferred shares to make their votes count.

Even without these maneuvers, the corporation could still create an incentive for management under any equity distribution. The organizational documents could provide that, upon a metric failure, investors receive not only voting rights in the next director election but also, as suggested above, the right to demand redemption at a fair price, which could strain the business's resources. This way, even if investors hold too few votes to affect an election's outcome, they could place financial pressure on management to achieve the chosen objectives.

These novel proposals to enshrine impact metrics into a corporation's organizational documents could resolve several issues with the default golden share model and thereby promote trust between managers and investors. Most importantly, that model prevents managers only from formally abandoning or changing the specific public benefit stated in its charter, but it does not commit them to prioritize that benefit in their day-to-day business decisions.[317] But if a failure to achieve appropriate impact metrics permits investors to redeem their preferred stock on an accelerated schedule or to potentially replace incumbent directors, then managers have strong financial and personal incentives to achieve those metrics. To the extent that the chosen metrics accurately reflect progress toward the company's mission, these incentives would encourage managers to pursue that mission by their deeds, not just by practically unenforceable words in their charters and promotional materials. Importantly, these proposals do not allow investors to force out social entrepreneurs for insufficient financial returns, as founders often fear based on prominent examples like Etsy.[318] Instead, they empower investors only to steer a wayward company back toward its social mission, not away from it.

In addition, the entrenchment of managers arising from dual-class stock structures like the golden share model becomes a problem when those managers are no longer fit to lead the company.[319] To the extent that metrics gauge managerial performance along the axis of social impact, a failure to satisfy them would, under this proposal, allow investors to potentially re-

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[317] *See supra* Part III.A

[318] *See supra* text accompanying notes 24–26.

[319] *See supra* text accompanying notes 220–21.

place underperforming managers, either directly if those managers are directors or indirectly if they are officers appointed by the board.

Relatedly, under the default golden share model, managers have nearly unfettered opportunities to extract pecuniary and non-pecuniary private benefits from the corporation.[320] If taken too far, these activities can diminish the corporation's value to investors and other stakeholders, by advancing only insiders' interests rather than everybody else's.[321] To the extent that it impedes progress toward social goals, private benefit extraction would prevent the corporation from satisfying the metrics, granting investors financial and control rights to managers' potential detriment. This possibility should encourage managers to limit their extractive activities and redirect their efforts toward the corporation's mission instead.

For investors, another disadvantage of the golden share model is the limited financial returns relative to more traditional organizational forms.[322] Although the proposed integration of impact metrics would not improve these returns, it would, with respect to the other "bottom line," increase the probability that a corporation would achieve its mission. This could lead an impact investor to accept the lower return on investment in exchange for the greater promise of social impact and greater control in certain circumstances. In other words, it may alter a rational investor's cost-benefit analysis enough for them to fund the company, when the default golden share model's weak assurances would appear to offer a losing bet.

Of course, no proposal is without its drawbacks, but many of this one's apparent problems may be resolved quite readily. First, some may fear that profiteering investors could abuse their contingent voting rights by installing directors who do not prioritize mission at all. But if the chosen metrics are reliable indicators of the company's mission, then the old directors may not have been prioritizing that mission in the first place. Moreover, the company's succession rules could protect against potential abuse, by permitting stockholders to nominate only certain individuals to stand in a contested election. Depending on those rules, nominees could be limited to individuals chosen by a workers' council or through another mechanism outside investors' control.[323]

If poorly chosen, the metrics could falsely indicate a lack of commitment to mission. However, the failure to meet metrics during a single period would not result in any director's automatic replacement. Instead, a vote of all voting common stock and preferred stock would determine the outcome.

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[320] *See supra* Part III.C.

[321] *See* Choi, *supra* note 135, at 56 ("Controlling shareholders are known to abuse their power and extract 'private benefits of control' to the detriment of the minority shareholders. Examples include entering into conflicts-of-interest transactions, misusing corporate resources for personal ends, expropriating corporate opportunities, pursuing pet projects, and building conglomerate empires.").

[322] *See supra* Part III.D.

[323] *See supra* text accompanying note 108.

This would set a high bar, depending on the distribution of shares and any adjustments to those numbers for which investors negotiate. Even if a minority investor would like to replace directors, it may not have the votes to do that without other investors' active participation.

As a second potential problem, the proposed implementation of metrics could restrict the company from changing its mission over time to adapt to new circumstances, because mission-specific criteria would be enshrined in the charter, bylaws, or both. These metrics would typically be narrower than the "specific public benefit" that Delaware law requires any PBC charter to include, which is usually stated broadly.[324] But one could address this concern through rules regarding amendments. For instance, the relevant organizational documents could state that the corporation may change the metrics only with majority approval by voting common stockholders and preferred stockholders.[325]

Finally, advocates of steward ownership may object that this proposal falls short of their ideals of managerial independence by granting too much control to outside financiers. This may be true for some. But social entrepreneurs who want to promote trust with investors to gain broader access to capital may need to sacrifice some of the absolute control inherent to the default golden share model. The proposed reliance on metrics would help provide those assurances by elevating purpose, not profits, while relinquishing managerial authority only in limited circumstances, subject to strong protections against abuse.

B. Consent Rights for Investors

Though perhaps the most promising avenue toward improving the golden share model, impact metrics are not the only potential enhancement. Another may be to grant certain separate rights to investors.

Although one of the main purposes of steward ownership is to grant managers independence from outside investors' influence,[326] in fact, GSCs do grant to preferred stockholders certain consent rights through protective provisions. Typically, these are limited to a few major decisions, such as liquidation events, amendments to the charter or bylaws, and debt incurrences above a certain dollar amount.[327] The charter restricts the corporation from taking any of these actions without the consent of the holders of a majority of outstanding preferred stock.

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[324] *See supra* note 211 and accompanying text.

[325] One might think to require the golden shareholder's consent too, but a veto service provider's organizational documents may obligate it to reject any proposed amendment without consideration. Even without such an obligation, granting a golden shareholder discretionary authority over the business's direction may be imprudent. *See supra* text accompanying notes 129, 132, 277.

[326] *See supra* text accompanying note 89.

[327] *See supra* text accompanying note 115-16.

To further limit the risk of private benefit extraction by managers,[328] a business could simply add executive compensation decisions to this list of protective provisions. Of course, to require investor consent for routine business decisions like these would limit managers' freedom, contrary to key principles of steward ownership. Consequently, some adopters of the golden share model may consider these investor rights to diverge unacceptably from their vision, but others may find it an easy way to assuage predictable concerns about abuse of power.

C. Voting Trusts

This Article's final proposal to improve the golden share model addresses potential misgivings regarding the golden shareholder's reliability.[329] Despite that entity's nominal centrality to the model, a business could, in fact, achieve the same goals without entering an unusual and untested arrangement with an unknown overseas foundation. Instead, the novel application of a familiar and accepted device in corporate law—the voting trust—could provide a more comfortable and equally effective alternative, while avoiding some of the risks posed by a veto service provider.

"A voting trust is a device by which [stockholders] separate the voting rights in, and the legal title to, their shares from the beneficial ownership of the shares."[330] Through a written trust agreement, participating stockholders "confer[ ] the voting rights and the legal title on one or more voting trustees, while retaining the ultimate right to distributions and appreciation."[331] "Voting trusts are usually used to pool voting power for the election of directors,"[332] but Delaware law does not limit their use to that purpose; stockholders can direct trustees to vote on any matter.[333]

"Like any trustee, the voting trustee is a fiduciary [and] must vote the shares as instructed by the equitable owners. This arrangement is effective, because the voting trustee is required to act as instructed; a court can compel her to do so."[334] In addition, the separation of the shares' voting and economic rights "survives transfers by the beneficial owners, since they can transfer only their retained equitable interests."[335] Although some states impose "a maximum time period (usually ten years)" on voting trusts,[336] Dela-

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[328] *See supra* Part III.C.
[329] *See supra* Part III.E.
[330] Cox & Eisenberg, *supra* note 191, at 532.
[331] *Id.*
[332] Freer, *supra* note 215, at 144.
[333] Del. Code Ann. tit. 8 § 218 (permitting stockholders to vest in "any person" "or entity" "the right to vote" on their stock, without any restriction on the matters subject to the vote).
[334] Freer, *supra* note 215, at 143.
[335] Cox & Eisenberg, *supra* note 191, at 532.
[336] *Id.* at 533.

ware dispensed with such a requirement in 1994 and no longer limits trusts' duration.[337]

With these characteristics, a voting trust could readily replace the golden shareholder in performing its most essential tasks: vetoing proposed sales and liquidations of the company and charter amendments that would change the social mission or stockholders' rights and obligations.[338] To this end, a GSC could maintain the charter's veto rights for the golden share but eliminate the requirement that this share be held only by an organization that fits the Purpose Foundation's description. Instead, the golden share could be issued to a founder, who would immediately confer its voting rights and legal title to a voting trustee through a written trust agreement. (The founder's beneficial ownership of the golden share would be illusory, because that share bears no economic rights.[339])

To maintain this structure's long-term effectiveness, the trust agreement should contain several specific provisions. First, most basically, are instructions that the trustee reject any of the amendments or transactions subject to veto rights in the charter, leaving the trustee with no discretion in its voting. Second are clear declarations that the trust is perpetual and irrevocable, which would prevent founders or future beneficial owners of the golden share from unraveling the arrangement. Third, the company itself should be a party to the agreement, in addition to the founder and the trustee, and should be obligated to appoint, through its board of directors, a successor if any trustee becomes unavailable. This would ensure that the trust remains effective even after a trustee's death, disability, or other disqualification. Fourth, and perhaps most unique in this context, is a statement that each of the company's stockholders at any time is a third-party beneficiary entitled to specifically enforce the trustee's obligations to vote and the company's obligation to appoint successors.[340] With this provision, as long as even one stockholder continues to prioritize the GSC's social mission, it could legally prevent antithetical corporate changes. Finally, to ensure the agreement's enforceability against any trustee, each party should irrevocably submit to Delaware courts' exclusive jurisdiction.

This use of a voting trust would harness a golden share's power while overcoming a golden shareholder's most significant limitations. In the default model, that role's criteria are so strict that perhaps only the Purpose Foundation currently meets them.[341] If this organization undergoes disqualifying changes in its constitutional documents or simply dissolves, and no

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[337] C. Stephen Bigler, *Delaware Update—Note These Changes to Delaware' Corporation Law*, 4 Bus. L. Today 24, 25 (1995) ("Section 218 has been amended to eliminate the 10-year limit previously applicable to voting trusts . . . The statute now places no time limits on voting trusts . . . The amendment became effective on July 1, 1994.").

[338] *See supra* text accompanying note 128.

[339] *See supra* text accompanying note 128.

[340] Regarding the rules governing third-party beneficiaries and specific enforcement, see Restatement (Second) of Conts. §§ 302, 304, 307, 357 (Am. L. Inst. 1981).

[341] *See supra* text accompanying notes 129–30.

competing veto service foundation has yet emerged to replace it, then the golden share model could immediately disintegrate. In contrast, Delaware law permits any person or entity to serve as a voting trustee,[342] so they could be replaced easily if necessary. Moreover, the trust agreement itself, which trustees cannot unilaterally amend, would impose the judicially enforceable obligation to veto undesired changes. As long as the trustee is subject to Delaware courts' jurisdiction, its identity and internal policies would be irrelevant to its dependable performance of its sole function. Therefore, the company would not have to count on the perpetuation of a specific organization or its constitutional documents.

With this arrangement, founders who are understandably concerned about a veto service provider's long-term reliability could procure the same services using more readily available resources instead.

Conclusion

Forms of social enterprise can be envisioned along a continuum between commitment to a social mission and flexibility in business decisions. On the latter end of the spectrum lies the traditional Delaware corporation, which arguably permits directors to consider social missions but does not require them to do so. A step away from that end is the relatively new PBC, which requires them to consider a mission but not to prioritize or even to pursue it. As other scholars have noted, these shortcomings leave open a gap in trust between managers and investors, limiting social enterprises' access to capital and potential for growth.

The golden share model takes another step away from flexibility and toward commitment, by preventing conversions from the PBC form, amendments to the specific public benefit stated in the charter, sales of the company, and certain opportunities for insiders to extract wealth. In its existing form, however, this model does not assure investors that managers will actually prioritize or pursue that public benefit. In fact, it may widen the trust gap by holding insiders unaccountable for not only mission drift but also entrenchment and various kinds of private benefit extraction. In addition, the idea of indefinitely entrusting a company's governance to a relatively new foundation in Switzerland may give pause to founders and investors alike.

To address these limitations, this Article's proposed improvements to the golden share model take another large step toward commitment, through novel applications of familiar legal concepts and established business practices. Unlike most other proposals for advancing the social enterprise sector, these approaches are viable today, without any further legislation. They may not suit all social entrepreneurs, especially those who idealize managerial independence from investor influence in all circumstances. But for mission-driven founders who want to close the trust gap that continues to impede the

[342] *See supra* note 333.

expansion of social enterprise, this Article's concrete proposals provide effective and practical solutions. And for the many scholars focused on this sector, this Article's exposition and enhancement of a new corporate structure should encourage additional solutions based on private ordering.