2014

What is a “Social” Business and Why Does the Answer Matter?

Justin Blount
Stephen F Austin State University, blountjr@sfasu.edu

Patricia Nunley
Baylor University

Brooklyn Journal of Corporate, Financial & Commercial Law

Volume 8 | Issue 2 Article 2

2014

What is a "Social" Business and Why Does the Answer Matter?

Justin Blount

Patricia Nunley

WHAT IS A "SOCIAL" BUSINESS AND WHY DOES THE ANSWER MATTER?

Justin Blount[*] *& Patricia Nunley*[**]

ABSTRACT

The concepts of "social entrepreneurship" and "social enterprise" continue to gain traction both in business and academia. However, definitions of these concepts remain inconsistent and fractured. This Article discusses and analyzes the attributes of common definitions of these terms, arguing that these definitions suffer from the common problems of defining these terms tautologically by using the word "social" in the definition without defining it and creating a false dichotomy between the social and economic functions of business organizations. Largely based on these flawed definitions, many commentators argue that new hybrid business entity forms are necessary to accommodate social enterprise. We argue that a more principled definition of "social enterprise" is found in a value-creation-based theory of social enterprise from business ethics literature, and that by understanding social enterprise through this theory, we can better evaluate whether new business entity forms, or other changes to corporate law, are in fact necessary to further the growth of the social enterprise movement.

INTRODUCTION

In recent years, the concepts of "social entrepreneurship" and "social enterprise" have become increasingly prevalent and been widely embraced in both the business and legal communities. While the popularity of these terms has grown, as a concept they have remained ill-defined.[1] These terms are generally used to describe organizations that blend aspects of for-profit business with some type of mission benefitting society that is more typically associated with non-profit organizations.[2] Many proponents of the

---

* Justin Blount is an Assistant Professor of Business Law in the Rusche College of Business at Stephen F. Austin State University in Nacogdoches, Texas. B.B.A. in Finance, Southwestern Oklahoma State University; J.D., Baylor Law School; M.B.A., University of Texas at Austin, McCombs School of Business.

** Patricia Nunley is an Associate Professor in the Hankamer School of Business at Baylor University in Waco, Texas. B.B.A., Baylor University; J.D., Baylor Law School.

1. *See, e.g.*, S. Bacq & F. Janssen, *The Multiple Faces of Social Entrepreneurship: A Review of Definitional Issues Based on Geographical and Thematic Criteria*, 23 ENTREPRENEURSHIP & REGIONAL DEV. 373, 374 (2011); Peter A. Dacin et al., *Social Entrepreneurship: Why We Don't Need a New Theory and How We Move Forward from Here*, 24 ACAD. MGMT. REV. PERSP. 37, 39–41 (2010); Raymond Dart, *The Legitimacy of Social Enterprise*, 14 NONPROFIT MGMT. & LEADERSHIP 411, 414 (2004).

2. *See, e.g.*, THOMAS J. BILLITTERI, MIXING MISSION AND BUSINESS: DOES SOCIAL ENTERPRISE NEED A NEW LEGAL APPROACH? 2 (2007), *available at* http://www.aspeninstitute.org/sites/default/files/content/docs/pubs/New_Legal_Forms_Report_FINAL.pdf ("Now, some of the leading thinkers in the business and nonprofit worlds believe they

social enterprise movement have attempted to provide more precise definitions of "social entrepreneur" or "social enterprise." However, definitions in this area remain hopelessly fractured, often conflicting, and almost always tautologically utilize the term "social." Despite this lack of thorough definition, social entrepreneurship has been advocated as a "new Enlightenment" in solving societal problems[3] and has been described as a new "Fourth Sector" of society.[4] Furthermore, many legal commentators have proposed that the social business movement, whatever it may be, requires the development of new *hybrid* entity structures designed to accommodate the needs of social enterprises and expand this new fourth sector.[5]

This Article turns a critical eye towards this trend by analyzing and evaluating current definitions of what makes an organization a social enterprise, and what (if anything) distinguishes social enterprises from existing business or non-profit entities at the organizational level. In Part I, this Article provides examples of organizations that self-identify, and have been identified by independent third-party organizations, as social enterprises. Part II discusses the most common definitions used in this area proffered by business practitioners, as well as legal and business academics. This Article then provides a critique of these existing definitions in Part III and argues that they are problematic because they typically rely on self-referentially using the term "social" within the definition and are based on a false dichotomy between the social and economic aspects of organizations. Thus, these definitions provide no principled basis for distinguishing a social enterprise from a traditional business or non-profit entity at the organizational level. In Part IV, this Article discusses a positive theory of

---

see an evolutionary step in that decades-old model. They point to an emerging 'Fourth Sector' of social enterprise organizations that combine charitable missions, corporate methods, and social and environmental consciousness in ways that transcend traditional business and philanthropy.").

3. David Bornstein, *The Rise of the Social Entrepreneur*, N.Y. TIMES OPINIONATOR BLOG (Nov. 13, 2012, 9:30 PM), http://opinionator.blogs.nytimes.com/2012/11/13/the-rise-of-social-entrepreneur/.

4. *See* HEERAD SABETI & THE FOURTH SECTOR NETWORK CONCEPT WORKING GRP., THE EMERGING FOURTH SECTOR: EXECUTIVE SUMMARY 2–3 (2009), *available at* http://www.aspeninstitute.org/sites/default/files/content/docs/pubs/4th%20sector%20paper%20-%20exec%20summary%20FINAL.pdf (describing the current three organization sectors of society as business, government, and non-profit and stating that hybrid organizations acting as social enterprises are the new fourth sector).

5. *See, e.g.*, SABETI & THE FOURTH SECTOR NETWORK CONCEPT WORKING GRP., *supra* note 4 (advocating certain core characteristics of an archetypal "For-Benefit" organization); William H. Clark, Jr. & Elizabeth K. Babson, *How Benefit Corporations Are Redefining the Purpose of Business Corporations*, 38 WM. MITCHELL L. REV. 817, 818 (2012) (noting that at the time of its publication, seven states had passed legislation allowing the formation of "benefit corporations," and five other states had introduced legislation to do so); J. Haskell Murray & Edward I. Hwang, *Purpose with Profit: Governance, Enforcement, Capital-Raising and Capital Locking in Low-Profit Limited Liability Companies*, 66 U. MIAMI L. REV. 1, 8 (2011) (discussing the "Low-Profit Limited Liability Corporation," a hybrid entity designed to attract private foundation funds).

social entrepreneurship based on the concepts of value creation and value capture, which has recently been advanced in business literature, and argues that, with slight modification, this approach provides a more sound and rigorous basis for evaluating and defining this phenomenon and serves as a better basis for legal and policy prescriptions regarding social enterprise. Finally, Part V concludes with a discussion, derived from this value-based definition of "social enterprise," of whether the creation of new business entity forms or reforms of existing corporate governance laws are necessary to advance the concepts underlying the social enterprise movement.

I. EXAMPLES OF SOCIAL ENTERPRISES

Before discussing some of the proffered definitions of "social entrepreneurship" and "social enterprise," it is important to consider real-world examples of organizations that self-identify as social businesses. Understanding characteristics of organizations that identify themselves as social enterprises is essential because definitions in this area are not attempts to define an abstract concept. Rather, they are attempts to define a real-world phenomenon. Reviewing examples of existing social enterprises provides a basis for understanding how these organizations operate and why defining terms in this area has proven difficult.

A. D.LIGHT DESIGN, INC.

d.light design, Inc. (d.light) is a company with a mission to help provide quality lighting to the significant portion of the world that does not have access to reliable electricity.[6] Without access to electricity, household lighting is typically provided by kerosene lanterns.[7] Kerosene lanterns provide poor quality of light; are a safety hazard due to the potential for ingestion, burns, and fires; and are also a key contributor to indoor air pollution.[8] d.light has developed and sells a variety of affordable and durable solar lanterns that provide better, safer light without the need for access to traditional electric utilities.[9]

Rather than operating as a non-profit organization and relying on donations, d.light is a for-profit corporation organized under the laws of the state of California[10] that self-identifies as a social enterprise.[11] d.light describes itself as "a for-profit social enterprise whose purpose is to create

6. *Who We Are*, D.LIGHT DESIGN, http://www.dlightdesign.com/who-we-are/ (last visited Apr. 11, 2014).

7. *See Customer Benefits*, D.LIGHT DESIGN, http://www.dlightdesign.com/impact-dashboard/customer-benefits/ (last visited Apr. 11, 2014).

8. *Id.*

9. *Id.*

10. *Business Search—Results*, CAL. SEC'Y ST., http://kepler.sos.ca.gov/ (last visited Apr. 11, 2014) (select "Corporation Name" as the "Search Type"; then type "d.light" as the "Entity Name"; then select "Search").

11. *Who We Are*, *supra* note 6.

new freedoms for customers without access to reliable power so they can enjoy a brighter future. We design, manufacture and distribute solar light and power products throughout the developing world."[12] In addition to self-identifying as a social enterprise, d.light has been recognized by numerous independent organizations for its efforts as a social enterprise.[13]

B. WOMEN'S BEAN PROJECT

The Women's Bean Project "strives to break the cycle of chronic unemployment and poverty by helping women discover their talents and develop skills by offering job readiness training opportunities."[14] The women involved in the project help create products such as gourmet food and beverages, gift baskets, and handcrafted jewelry.[15] Through working with the Women's Bean Project, these women learn valuable job readiness and interpersonal and life skills to help them gain future, long-term employment.[16]

The Women's Bean Project self-identifies as a social enterprise[17] and has been recognized as such by the Social Enterprise Alliance.[18] However, unlike d.light, the Women's Bean Project is organized as a non-profit corporation in the state of Colorado.[19] While it receives seventy percent of its operating budget from the sales of the products made by the women, the Women's Bean Project relies on donations for the remainder of its operating budget.[20]

C. COOPERATIVE HOME CARE ASSOCIATES

Cooperative Home Care Associates, Inc. (CHCA) is a for-profit corporation organized under the laws of the state of New York.[21] CHCA

---

12. *Id.*
13. *See Recognitions*, D.LIGHT DESIGN, http://www.dlightdesign.com/who-we-are/recognitions/ (last visited Apr. 11, 2014).
14. *What We Do*, WOMEN'S BEAN PROJECT, http://www.womensbeanproject.com/whatwedo.html (last visited Apr. 11, 2014).
15. *Online Store*, WOMEN'S BEAN PROJECT, http://www.womensbeanproject.com/online-store.html (last visited Apr. 11, 2014).
16. WOMEN'S BEAN PROJECT, http://www.womensbeanproject.com/ (last visited Apr. 11, 2014).
17. *Id.*
18. *Social Enterprise Examples*, SOC. ENTER. ALLIANCE, https://www.se-alliance.org/social-enterprise-examples (last visited Apr. 11, 2014).
19. *Summary*, COLO. SEC'Y ST., http://www.sos.state.co.us/biz/BusinessEntityDetail.do?quitButtonDestination=BusinessEntityResults&fileId=19901020146&masterFileId=19901020146&srchTyp=ENTITY&entityId2=19901020146&nameTyp=ENT (last visited Apr. 11, 2014).
20. *Donate*, WOMEN'S BEAN PROJECT, http://www.womensbeanproject.com/donate.html (last visited Apr. 11, 2014).
21. *Entity Information*, N.Y. ST. DEP'T. ST., http://appext20.dos.ny.gov/corp_public/CORPSEARCH.ENTITY_INFORMATION?p_nameid=1050594&p_corpid=949129&p_entity_name=cooperative%20home%20care&p_name_type=A&p_search_type=BEGINS&p_srch_results_page=0 (last visited Apr. 11, 2014).

works in cooperation with two sister organizations—Independence Care Systems (a non-profit, Medicaid-managed, long-term care plan) and PHI (a national policy organization).[22] CHCA's mission is to provide reliable, high-quality home health care while also offering the highest possible salaries and benefits for its home health care workers.[23] By providing high-quality jobs for direct-care workers, CHCA believes that the individuals it serves will receive high-quality home health care as well.[24] To this end, CHCA is employee-owned and focuses on providing employee training.[25] The owner-employees of CHCA are African American and Latino women, and seventy percent of them were previously on public assistance.[26] It has 1600 workers, and it has historically paid wages that are twenty percent higher than the industry average.[27] The Schwab Foundation for Social Entrepreneurship recognized CHCA's founder, Rick Surpin, as its 2003 social entrepreneur of the year.[28]

These examples provide a small sample of the numerous organizations that are considered to be social enterprises or founded by social entrepreneurs. They illustrate the wide variety of business models and missions that are found within this broad field. Because of this variety and the fluidity with which the term is used, it is easy to understand the difficulty in defining the concepts of social enterprise and social entrepreneurship.[29]

II. COMMON DEFINITIONS OF SOCIAL ENTERPRISE AND SOCIAL ENTREPRENEURSHIP

An analysis of most proposed definitions of "social entrepreneurship" and "social enterprise," the two terms most commonly used to describe the individuals and organizations in this movement, reveals a tendency to define these terms self-referentially by using the term "social" to define "social entrepreneurship."[30] Once the term "social" is used as a defining

---

22. *History*, INDEPENDENCE CARE SYS., http://www.icsny.org/about-us/history/ (last visited Apr. 11, 2014).

23. *Our Mission*, COOP. HOME CARE ASSOCS., http://www.chcany.org/ (last visited Apr. 11, 2014).

24. *Rick Surpin*, SCHWAB FOUND. FOR SOC. ENTREPRENEURSHIP, http://www.schwabfound.org/content/rick-surpin (last visited Apr. 11, 2014).

25. *Training + Employment*, COOP. HOME CARE ASSOCS., http://www.chcany.org/ (last visited Apr. 11, 2014).

26. *Rick Surpin*, *supra* note 24.

27. *Id.*

28. *Id.*

29. *See, e.g.*, BILLITTERI, *supra* note 2, at 3 (describing an Aspen Institute roundtable on social enterprise and noting, "As quickly became apparent from the discussion, no single definition of social enterprise exists, and no single organizational model covers all possible approaches").

30. *See* Dacin et al., *supra* note 1, at 42 ("[T]he notion of providing social value or some derivative of social value appears to be a common theme across the majority of social entrepreneurship definitions.").

characteristic, then it is necessary to define this term in order for the definition to have meaning. This is usually done by contrasting an organization's "social" purpose, typically expressed in terms such as "social mission" or creating "social value," against a more traditional business or economic purpose for an organization, typically expressed in terms of profit.[31]

A. SOCIAL ENTREPRENEURSHIP

Despite its frequent use, "social entrepreneurship" has been given wide and various meanings in legal and business academic literature, as well as in the popular press.[32] These various definitions are somewhat similar in that virtually all of them define the term as entrepreneurship involving a "social" mission or objective.[33] However, further details of the definitions of this term can, and often do, vary.

Professor J. Gregory Dees, widely regarded as one of the leading minds in developing the academic study of social entrepreneurship, has defined the subject broadly:

> Social entrepreneurs play the role of change agents in the social sector, by:
>
> - Adopting a mission to create and sustain social value (not just private value),
> - Recognizing and relentlessly pursuing new opportunities to serve that mission,
> - Engaging in a process of continuous innovation, adaptation, and learning,
> - Acting boldly without being limited by resources currently in hand, and
> - Exhibiting heightened accountability to the constituencies served and for the outcomes created.[34]

Professor Dees acknowledges that this is a somewhat "idealized" definition: "The closer a person gets to satisfying all these conditions, the more that person fits the model of a social entrepreneur."[35] A fundamental basis of this definition is the "social mission" distinguishing social entrepreneurship from regular business entrepreneurship, which Dees defines as seeking the creation of "private benefits" through "financial returns or consumption benefits."[36] Notably, Dees' definition does not limit

---

31. *See, e.g.*, J. Gregory Dees, The Meaning of "Social Entrepreneurship," 2–3 (May 30, 2001) (unpublished manuscript), *available at* http://www.caseatduke.org/documents/dees_sedef.pdf (distinguishing between "social value" and "private value" in defining social entrepreneurship).

32. *See* Dacin et al., *supra* note 1, at 39–41 (providing thirty-seven different definitions of "social entrepreneurship" and "social entrepreneur").

33. *Id.*

34. Dees, *supra* note 31, at 4.

35. *Id.*

36. *Id.*

social entrepreneurship to organizations with social missions that also seek to make a profit or earn income to further and sustain those missions. Under Dees' broad definition, a social entrepreneur could operate solely within the non-profit sector, seeking grants or donations to fund its mission; could operate within the business sector and fund its mission using an earned income strategy; or could operate as a hybrid organization with characteristics of both a non-profit and a for-profit business.[37]

Most other definitions of social entrepreneurship follow this same basic formula, defining the term through a reference to a social mission or social activity. However, these definitions vary in other important respects, particularly as to whether a social entrepreneur must operate like a business and earn income to fund its social mission. For example, the following definitions focus on seeking financial return while also furthering a social mission:

- "Similar to conventional entrepreneurship, [social entrepreneurship] involves the provision of goods or services. However, the provision of the product or service is not an end in itself, but an integral part of an intervention to achieve social objectives, thereby contributing to social change. Thus, rather than being only economic endeavors, SE initiatives aim primarily to pursue a social mission and to ultimately transform their social environment."[38]
- "The term social entrepreneur is used to refer to one who is willing to create a CSR [corporate social responsibility] firm at a financial loss. The latter sacrifices financial return but gains social satisfaction. Social entrepreneurs are shown to be willing to absorb a financial loss to form a CSR firm and may prefer to form a CSR firm rather than a profit-maximizing firm."[39]
- "Social entrepreneurship is strategic investing that generates two interrelated results: social progress and financial return . . . . [S]ocial entrepreneurship approaches a social problem in the same way a traditional business entrepreneur approaches a market opportunity."[40]

However, the following definitions, like that of Professor Dees, do not see financial returns as the sine qua non of social entrepreneurship, but instead focus on pursuing a social mission in an innovative manner as social entrepreneurship's defining characteristic:

---

37. *Id.*

38. Johanna Mair et al., *Organizing for Society: A Typology of Social Entrepreneuring Models*, 111 J. BUS. ETHICS 353, 353 (2012).

39. David P. Baron, *Corporate Social Responsibility and Social Entrepreneurship*, 16 J. ECON. & MGMT. STRATEGY 683, 686 (2007).

40. Janet E. Kerr, *Sustainability Meets Profitability: The Convenient Truth of How the Business Judgment Rule Protects a Board's Decision to Engage in Social Entrepreneurship*, 29 CARDOZO L. REV. 623, 634 (2007).

- "[I]nnovative, social value creating activity that can occur within or across the non-profit, business, or government sectors."[41]
- "Society's change agents: creators of innovations that disrupt the status quo and transform our world for the better."[42]
- "Social entrepreneurs are individuals with innovative solutions to society's most pressing social problems. They are ambitious and persistent, tackling major social issues and offering new ideas for wide-scale change."[43]

This non-exhaustive sample of the numerous definitions of "social entrepreneur" and "social entrepreneurship" that have been proffered[44] serves to illustrate the common thread that runs throughout virtually every definition of this phenomenon—a "social" objective of some kind that serves as the organization's defining purpose.[45] This social mission or objective as the defining characteristic is used in an attempt to create a dichotomy between these organizations and traditional business entrepreneurs with an economic focus, which is usually defined as a private profit motive.[46]

B. SOCIAL ENTERPRISE

The term "social enterprise" is also commonly used in the area of social business, and is often used as a virtual synonym for, or a corollary to,

---

41. James Austin et al., *Social and Commercial Entrepreneurship: Same, Different, or Both?*, 30 ENTREPRENEURSHIP THEORY & PRAC. 1, 2 (2006).

42. *About*, SKOLL FOUND., http://www.skollfoundation.org/about/ (last visited Apr. 11, 2014).

43. *What is a Social Entrepreneur?*, ASHOKA, https://www.ashoka.org/social_entrepreneur (last visited Apr. 11, 2014). Ashoka is one of the leading financing and support organizations for social entrepreneurs.

44. *See* Bacq & Janssen, *supra* note 1, at 373–75 (discussing the numerous definitions of "social entrepreneurship," "social entrepreneur," and "social entrepreneurship organization"); *see also* Dacin et al., *supra* note 1.

45. Dacin et al., *supra* note 1, at 42 ("[T]he notion of providing social value or some derivative of social value appears to be a common theme across the majority of social entrepreneurship definitions."); *see also* Bacq & Janssen, *supra* note 1, at 384 (discussing three different schools of thought on defining "social entrepreneurship" and noting that "[d]espite some differences in the way of expressing it, the three schools of thought clearly agree on the fact that the social mission is at the core of social entrepreneurship").

46. *See* Dees, *supra* note 31, at 3; *see also* Christian Seelos & Johnna Mair, *Social Entrepreneurship: Creating New Business Models to Serve the Poor*, 48 BUS. HORIZONS 241, 244 (2005) (citing Sankaran Venkataraman, *The Distinctive Domain of Entrepreneurship Research: An Editor's Perspective*, 3 ADVANCES ENTREPRENEURSHIP FIRM EMERGENCE & GROWTH 119 (1997)) ("Venkataraman, studying traditional entrepreneurship, sees the creation of social wealth as a by-product of economic value created by entrepreneurs. In [social entrepreneurship], by contrast, social value creation appears to be the primary objective, while economic value creation is often a by-product that allows the organization to achieve sustainability and self-sufficiency.").

"social entrepreneurship."[47] For example, social entrepreneurs are frequently referenced as creating or running social enterprises.[48] Thus, social entrepreneurs are typically discussed as the actors and social enterprises as the organizations through which social entrepreneurs act.[49]

Since these concepts are so closely related, it is not surprising that the definitions of "social enterprise" closely mirror those of "social entrepreneurship" or "social entrepreneur." "Social enterprise," like "social entrepreneurship," is typically defined by a reference to an overriding "social" mission or objective that the enterprise seeks to fulfill, as opposed to the profit-seeking objective of a traditional business enterprise. For example, one law review article defines "social enterprise" using the following characteristics:

> [A] social enterprise, for purposes of identifying an appropriate legal structure, is (1) an organization that serves first and foremost a social mission, (2) through the use of sophisticated business models typically associated with traditional corporate activity, (3) pursuing multiple financing options, and (4) facing novel governance challenges when balancing the interests of donors and investors.[50]

This particular definition focuses on the hybrid aspect of a social enterprise in that the enterprise is defined as having characteristics of both a for-profit and not-for-profit organization. Notably, this definition does not provide any guidance on what differentiates a "social mission" from any other organizational mission.[51] However, as with the definitions of "social entrepreneurship," definitions of "social enterprise" do not always limit the term's applicability to enterprises that use traditional business models or make a profit. Some definitions focus only on the social mission and innovation aspects of the organization and allow that a social enterprise could exist solely in the non-profit sphere.[52] Because these terms are frequently used as synonyms and refer essentially to the same business phenomenon, for ease of reference and clarity this Article will henceforth use only the term "social enterprise" when broadly referring to the social

---

47. *See, e.g.*, Dacin et al., *supra* note 1, at 39 (including definitions of "social enterprise" in their analysis of definitions of "social entrepreneurship"); Dart, *supra* note 1, at 414 (using definitions of "social entrepreneurship" interchangeably with definitions of "social enterprise").

48. *See, e.g.*, Keren G. Raz, *Toward an Improved Legal Form for Social Enterprise*, 36 N.Y.U. REV. L. & SOC. CHANGE 283, 286 (2012) (noting that social entrepreneurs are one of the groups advocating for the creation of new legal forms to accommodate the needs of social enterprises).

49. *See, e.g.*, Robert A. Katz & Antony Page, *The Role of Social Enterprise*, 35 VT. L. REV. 59, 59 (2010) ("Social enterprises are founded by 'social entrepreneurs,' a broader term that denotes an ambitious person who seeks social change on a large scale, characteristically through earned income strategies.").

50. Raz, *supra* note 48, at 287–88 (internal citations omitted).

51. *See id.* at 286.

52. *See* Dart, *supra* note 1, at 414 (noting that some definitions of "social enterprise" frame the phenomenon in terms of revenue generation and market-based strategies, while other definitions are broader and generically focus on social value creation).

entrepreneurship movement and the business organizations created thereunder.

C. Defining a Social Mission or Objective

Once the term "social" is used as a defining characteristic for a social enterprise, then it is necessary to establish exactly what this term means in order for the definition to have significance. Despite the importance of this distinction to the above definitions, there has been relatively little rigorous explanation of exactly what is meant by the term "social" in this particular context. Indeed, most of the literature in this area cavalierly uses terms such as "social mission" or "social value" without providing any explanation of exactly what is meant other than by providing examples of companies that are considered to have a social mission.[53] However, some attempts have been made to define exactly what types of missions or objectives these organizations undertake that make them social.

1. Creating Social Value as Opposed to Private Value as a Defining Characteristic

Professor Dees' abovementioned definition of "social entrepreneurship" focuses on the creation of "social value" as opposed to "private value."[54] He bases the distinction between these two forms of value on customers' ability to pay for the value provided by the business.[55] Thus, he defines private value creation as "specifically the creation of value for customers who are willing and able to pay."[56] His definition of social value is not quite as easily ascertained, but he appears to define it as the opposite of this private value: "In particular, markets do not do a good job of valuing social improvements, public goods and harms, and benefits for people who cannot afford to pay. These elements are often essential to social entrepreneurship. That is what makes it social entrepreneurship."[57]

Thus, it appears that in Dees' definition, the defining characteristic distinguishing private value creation from social value creation is ability or willingness to pay for the value being provided. That is to say, an enterprise with a primary mission of providing value to customers who are willing to pay a market price for the value provided is participating in private value

---

53. *See, e.g.*, Seelos & Mair, *supra* note 46, at 242–44 (using terms such as "social value" and "social needs" to define "social entrepreneurship" but providing no precise definitions therefor other than broad and relatively imprecise references to providing for basic human needs to the poor and sustainable development); *see also* Jean J. Boddewyn, *Understanding and Advancing the Concept of "Nonmarket,"* 42 BUS. & SOC'Y 297, 298 (2003) (discussing the shifting definitions of "non-market" and noting that the terms "economic" and "social" are also frequently used without a corresponding definition).

54. *See* Dees, *supra* note 31, at 2–3.

55. *Id.* at 3.

56. *Id.*

57. *Id.*

creation, but an enterprise with a primary mission of providing value to a group of people who cannot afford to pay for the value provided participates in social value creation and is more likely to be engaged in social entrepreneurship under Dees' definition.

This distinction is problematic. Classifying value to customers based on willingness and ability to pay as "private value" implies that value provided to paying customers does not result in value to other members of society, but only results in value to the market participants in the transaction. This conclusion is refuted by a long-held understanding that market transactions have externalities—that is, benefits or burdens borne by those who were not a party to the market transaction.[58] Dees' distinction seems to ignore the fact that economic development and social development are often synonymous, and profits created or value purchased by customers cannot truly be seen as a purely private benefit.[59]

For example, the rise and proliferation of smartphones has certainly resulted in tremendous profits for the companies that sell them, as well as private consumption benefits for those who purchase them. However, as smartphones have begun to spread to developing countries, they have also been powerful drivers for societal benefits by providing access to information and acting as tools for business and public development in areas where such growth is sorely needed.[60] These benefits exist not only for those who pay to purchase and use smartphones, but also for those non-paying members of society who benefit in a more general way from the advancement that arises from the access to information that smartphones provide.

Under Dees' distinction, the value provided to paying customers would be *private*, and the value provided to non-paying customers would be *social*.[61] A defining characteristic of social entrepreneurship under Dees' definition is "adopting a mission to create and sustain social value (not just private value)."[62] It would appear then, for an organization that creates both social and private value,[63] whether or not that organization qualifies as a

58. *See* Filipe M. Santos, *A Positive Theory of Social Entrepreneurship*, 111 J. BUS. ETHICS 335, 341 (2012).

59. *See, e.g.*, Michael E. Porter & Mark R. Kramer, *Creating Shared Value*, HARV. BUS. REV., Jan.–Feb. 2011, at 63 (arguing that businesses should focus on creating "shared value," not just short-term profits, and noting that "[c]apitalism is an unparalleled vehicle for meeting human needs, improving efficiency, creating jobs, and building wealth").

60. *See, e.g.*, David Talbot, *Kenya's Startup Boom*, MIT TECH. REV. (Feb. 21, 2012), http://www.technologyreview.com/featuredstory/426983/kenyas-startup-boom/ (noting that mobile phones have been instrumental in aiding Kenya in business development and may also aid in significant public health developments).

61. *See* Dees, *supra* note 31, at 2–3.

62. *Id.* at 4.

63. *Id.* ("Making a profit, creating wealth, or serving the desires of customers may be part of the model, but these are means to a social end, not the end in itself. Profit is not the gauge of value creation; nor is customer satisfaction; social impact is the gauge.").

social enterprise becomes self-defining. If the organization decides to frame its mission in terms of the *social* value it creates, then it could be a social enterprise, regardless of its actual societal impact.[64] Conversely, if the organization decides to frame its mission in terms of the *private* value it creates (i.e., profit), then Dees would appear to argue that it cannot be a social enterprise, even if it has a tremendously positive societal impact.[65]

Thus, using the smartphone example, a company like Apple or Samsung that sells millions of phones on a profitable basis may have a much larger impact on society as a whole, to both paying and non-paying individuals, than a very small company that sells some phones but also uses the profits generated thereby to give phones away to create "social" value for those individuals who are unable or unwilling to pay. However, because neither Apple nor Samsung define their corporate purpose in terms of a social mission, Dees would not consider them to be social enterprises, regardless of their positive social impact.[66] If the small company were to frame its purpose in terms of its social mission of providing free phones, Dees would seem to declare it a social enterprise, regardless of the scope of its actual social impact.[67]

If Dees' definition is used to distinguish between two operational models for purposes of studying the benefits and detriments on society of framing corporate purpose in this manner, the distinction is perhaps a valid one. Certainly, analyzing whether a business model focused on serving individuals who are unable to pay for the value they have been provided actually benefits society more than a traditional, *economic* business model is an important endeavor, and understanding such distinctions can help guide strategic choices made by entrepreneurs. However, it is not at all clear that such a distinction serves to classify a social enterprise as its own type of business entity. An organization could decide to provide goods or services to a populace that is underserved but still able and willing to pay for the service provided and have a tremendous positive societal impact by providing the service.[68]

---

64. *Id.* Notably, we cannot say that the enterprise *would* be a social enterprise because under Dees' definition, adoption of a social mission is a necessary but not exclusive element of the definition.

65. *Id.*

66. *Id.*

67. *Id.*

68. An example of this is the business of microfinance, which provides small loans to individuals in developing countries who do not otherwise have ready access to capital to start businesses. *See, e.g.*, *How Kiva Works*, KIVA, http://www.kiva.org/about/how (last visited Apr. 11, 2014). The individuals who are loaned the money do not receive it for free and are expected to pay it back. Nevertheless, microfinance is widely considered to be an area of social enterprise. *See, e.g.*, Santos, *supra* note 58, at 338 (discussing microfinance as an area of social enterprise—particularly Grameen Bank, founded by Nobel Peace Prize winner Muhammad Yunus). One could argue that giving individuals loans that must be paid back, rather than handouts, is a critical part of the social value created.

2. The Social Action Framework

Another attempt to distinguish between social and business actions in social enterprises is Professor Brenda Massetti's "Social Action Framework" (SAF).[69] Massetti acknowledges the lack of a sound and consistent definition of "social enterprise," but she notes how existing definitions reflect a distinction and interplay between ethics, business, and social actions within an organization.[70] Based on this distinction, Massetti utilizes "social action," defined as "behavior which accounts for the conduct of others," as the unit of analysis for her SAF.[71] The overarching purpose of the SAF is to aid organizations in making strategic choices of social actions that are congruent with their business strategy.[72] However, Massetti's model is relevant and useful to a discussion of defining "social enterprise" because it assumes a distinction between social actions and business actions, which she defines as "value-for-value exchange,"[73] and ultimately through this framework provides a definition of what constitutes a valid social action for a social enterprise.[74]

At the outset, Massetti notes that a key consideration for social action is that the action be considered "legitimate," which she defines as the "extent that it is deemed welfare-enhancing by prevailing social institutions."[75] This is an important distinction because it explicitly acknowledges that the question of what is considered "social" is subjective and based on prevailing societal norms. Additionally, Massetti expressly acknowledges that an action may be useful and benefit society but not be considered socially legitimate.[76] Within this realm of social legitimacy, Massetti states that an action may be "socially established" (widely accepted by society as legitimate) or "socially innovative" (considered legitimate, but new and unfamiliar to society).[77]

Massetti also makes a distinction between social actions that are "community-internalizing" as opposed to "community-externalizing."[78] Community-internalizing social actions are those that "support the welfare

---

69. *See* Brenda Massetti, *The Duality of Social Enterprise: A Framework for Social Action*, REV. BUS., Winter 2012/2013, at 50.

70. *Id.* at 51–52.

71. *Id.* at 52.

72. *Id.* at 55.

73. *Id.* at 51.

74. *Id.* at 59.

75. *Id.* at 53 (citing Deborah Vidaver-Cohen & Peggy Simcic Bronn, *Corporate Citizenship and Managerial Motivation: Implications for Business Legitimacy*, 113 BUS. & SOC'Y REV. 441 (2008)).

76. Massetti, *supra* note 69, at 64 n.2 ("An organization may perform functionally useful actions which are not considered socially legitimate. If the action is not considered socially legitimate, then it is not relevant for analysis in the SAF. It is the nature of the action's social legitimacy (i.e. established or innovative) that is considered in the SAF.").

77. *Id.* at 53.

78. *Id.* at 54.

of the community at least as much as the welfare of the organization."[79] Community-externalizing social actions are those where "the community supports the welfare of the organization as much as its own."[80] Based on these distinctions, Massetti defines a social enterprise as

> an organization where the majority of its social actions:
> 1. Are congruent with the organization's mission and have some degree of social legitimacy;
> 2. Are community internalizing regardless of whether they are required or chosen; [and]
> 3. Make clear social contributions while producing financial contributions (i.e. profits) that exceed their resource consumption.[81]

Massetti's SAF is a very useful tool for aiding an organization in making strategic business choices that are also welfare-enhancing for society. However, as a definitional tool it still suffers from the inherent problem of subjectivity with respect to social action. Massetti's SAF does ameliorate this problem somewhat by shifting the focal actor for the subjective determination of what constitutes a social action from the business to society as a whole.[82] It does not focus as heavily on a distinction between social and business concerns as Dees' definition, but the final definition still relies on distinctions between social and financial contributions.[83]

3. Value Proposition as a Defining Characteristic

Roger Martin and Sally Osberg have distinguished the social mission of the social enterprise, not by focusing on the motivations of the social entrepreneur, but by focusing on the value proposition of the organization itself.[84] They note that focusing on motivation as if social entrepreneurs are driven by altruism and business entrepreneurs are driven by money is an oversimplification.[85] This is because all entrepreneurs, including business entrepreneurs, "are strongly motivated by the opportunity they identify, pursuing that vision relentlessly, and deriving considerable psychic reward

---

79. *Id.* Massetti provides the example of Patagonia, an outdoors clothing company that "provides paid environmental internships [for] employees and agrees to bail them out of jail if they [are] arrested protesting a cause they care deeply about." *Id.* This provides at least as much benefit to the community, if not more, as it does to the organization.

80. *Id.* Massetti provides the example of tax subsidies received by Goldman Sachs to build its headquarters in Manhattan. In this example, the community is supporting the welfare of Goldman Sachs through the tax subsidy and will not have the opportunity to benefit until Goldman Sachs has.

81. *Id.* at 59.

82. *Id.* at 53.

83. *Id.* at 59.

84. *See* Roger L. Martin & Sally Osberg, *Social Entrepreneurship: The Case for Definition*, STAN. SOC. INNOVATION REV., Spring 2007, at 34 ("We believe that the critical distinction between entrepreneurship and social entrepreneurship lies in the value proposition.").

85. *Id.*

from the process of realizing their ideas."[86] Since motivations for all entrepreneurs are similar, they argue that the defining characteristic of the social enterprise is the value proposition of the organization, which is distinctly different from that of the business entrepreneur.[87]

In defining this value proposition, Martin and Osberg focus, like Dees, on the target market that social enterprises seek to serve: namely, those individuals who are the neglected and disadvantaged members of society.[88] Thus, their definition is specifically stated:

> We define social entrepreneurship as having the following three components: (1) identifying a stable but inherently unjust equilibrium that causes the exclusion, marginalization, or suffering of a segment of humanity that lacks the financial means or political clout to achieve any transformative benefit on its own; (2) identifying an opportunity in this unjust equilibrium, developing a social value proposition, and bringing to bear inspiration, creativity, direct action, courage, and fortitude, thereby challenging the stable state's hegemony; and (3) forging a new, stable equilibrium that releases trapped potential or alleviates the suffering of the targeted group, and through imitation and the creation of a stable ecosystem around the new equilibrium ensuring a better future for the targeted group and even society at large.[89]

While this definition is similar to Dees' in its focus on serving a marginalized population, it provides more detail and is also broader because it does not require that the target market be unable to pay for the value provided.[90] While it may be unlikely that such a target market will pay due to their status, ability to pay is not the defining characteristic. Rather, it is the marginalized status of the target demographic.[91]

Notably, this definition draws fairly distinct boundaries around what it means to be a social enterprise.[92] These boundaries are intentional, as Martin and Osberg state: "In defining social entrepreneurship, it is also important to establish boundaries and provide examples of activities that may be highly meritorious but do not fit our definition. Failing to identify boundaries would leave the term social entrepreneurship so wide open as to be essentially meaningless."[93]

---

86. *Id.*
87. *Id.*
88. *Id.* at 35 ("Unlike the entrepreneurial value proposition that assumes a market that can pay for the innovation, and may even provide substantial upside for investors, the social entrepreneur's value proposition targets an underserved, neglected, or highly disadvantaged population that lacks the financial means or political clout to achieve the transformative benefit on its own.").
89. *Id.*
90. *Id.*
91. *Id.*
92. *Id.* at 36.
93. *Id.*

They continue by distinguishing social enterprise from other socially valuable activities that are still inherently different from social enterprise: social service provision and social activism.[94] They define "social service" provision as activity that identifies an unfortunate, stable equilibrium in society and provides limited, localized services to an affected population without seeking large-scale change towards a new societal equilibrium like social enterprise.[95] They define "social activism" as activity that also identifies an unfortunate equilibrium but seeks to address the problem through the indirect action of influencing others, such as governments, NGOs, or consumers.[96]

Martin's and Osberg's point is well taken: it is important to draw boundaries around the definition of "social enterprise" such that it can be distinguished from other concepts. However, the more tightly drawn the boundaries, the more limited the concept becomes. If a definition of the concept is to be used for purposes of crafting legal policy designed to obtain the maximum benefit for society, care must be taken not to limit the definition too much.

These varying definitions illustrate the lack of consensus in defining "social enterprise." This difficulty is understandable. There is a relatively wide swath of individuals and businesses in this area that consider themselves a part of this new movement, each with different operating models and missions, making neat and precise definitions difficult.[97] Additionally, this area is continuously developing, often in innovative and creative ways, further complicating theoretical and definitional certainty. However, we argue that there are problems with existing attempts to define these terms that are entirely endemic to the nature of the definitions themselves.

III. CRITIQUE OF COMMON DEFINITIONS

These definitional problems largely develop from the use of the term "social" in a self-referential manner to define "social enterprise," followed by attempts to explain how calling an organization or its mission "social" makes it different from "non-social" missions. This problem is exacerbated when attempts to define "social" in this context contrast the term with economic concerns.[98] This is because attempting to define social concerns as something inherently different than the ordinary concerns that businesses

---

94. *Id.* at 36–37.

95. *Id.* Martin and Osberg provide the example of a school established to care for AIDS orphans in Africa. While such a school will benefit those children affected and is a meritorious endeavor, it will not break out of its limited frame of serving this local population.

96. *Id.* at 37.

97. *See, e.g.*, *supra* Part I.

98. *See* Santos, *supra* note 58, at 337. Professor Filipe M. Santos has noted this precise problem and written very persuasively on the topic in developing his own positive theory of social entrepreneurship, which is discussed *infra* in Part IV.

face is based on a false dichotomy. When businesses are properly understood as inherently social constructs, the distinctions between a social mission and a business mission, for purposes of corporate governance and the structure of business entities, are in fact illusory.

A. GENERALLY DEFINING "SOCIAL" AND "ECONOMIC"

If a social enterprise is indeed an organization that is engaged in some mission that is somehow different from that of a normal business or non-profit organization, then the starting point for understanding social enterprise must be an understanding of what the word "social" means. Additionally, since the aforementioned definitions frequently contrast social concerns with the economic or business concerns of organizations, a definition of the term "economic" is also critical. Defining these terms with their commonly understood English meanings provides some insights into the problems encountered when a social enterprise is conceived as a new organizational type based on a social mission or objective.

"Social," in a general sense, simply means "of or relating to society or its organization: of or relating to rank and status in society: needing companionship and therefore best suited to living in communities: relating to or designed for activities in which people meet each other for pleasure."[99] Massetti recognizes the breadth of this concept in utilizing the term "social action," broadly defined as "behavior which accounts for the conduct of others," in her Social Action Framework.[100] All organizations, whether for-profit or not-for-profit, are inherently social entities that are constantly engaged in social actions. Thus, if one refers to an organization as being engaged in an act that creates social value[101] or as having a social objective,[102] one has not said anything that distinguishes that organization from any other unless the word "social" is given an entirely new meaning from what it generally means in English.[103]

---

99. NEW OXFORD AMERICAN DICTIONARY 1657 (Angus Stevenson & Christine A. Lindburg eds., 3d ed. 2010).

100. Massetti, *supra* note 69, at 52.

101. *See* Dees, *supra* note 31, at 4.

102. Mair et al., *supra* note 38, at 353.

103. We certainly acknowledge the fact that in English we frequently co-opt a word and combine it with another to create a new concept which may have a distinct meaning from the words so co-opted—for example "social security." And of course, words can also take on new meaning through usage. The point made here is simply that if you are going to ascribe new meaning to a word or combination of words, you must define what the new meaning is, and you must do so without attempting to use the co-opted term itself, unless the co-opted term retains its traditional meaning. If the co-opted term does not maintain its traditional meaning and you attempt to define a compound term using the term itself, your new definition is meaningless unless you develop a wholly new meaning for the co-opted term and explain that meaning. The previous definitions discussed for compound terms such as "social enterprise" and "social value" have not provided any type of unique definition for the term "social," and thus we argue it is valid to use its traditional meaning in attempting to understand these definitions.

The term "economics" has been notoriously difficult to define precisely and has seen many differing definitions throughout history.[104] The most widely accepted definition today is that "economics" refers to how society allocates scarce resources.[105] Any time an organization acts to allocate resources, it engages in economic activity.[106] In this vein, Massetti's adoption of a broad definition of business as "value-for-value exchange" is appropriate.[107] The conceptualization of economic or business actions of an organization should not be limited to the profit-making functions of the business, as some advocates of social enterprise have done.[108] To do so is to oversimplify how businesses interact with and impact society. Business activity, one of the critical pieces of our economic system, is a complex social activity that involves the allocation of scarce resources among members of society through value-for-value exchanges.[109]

With these broad definitions as a starting point, we argue next that attempts to distinguish between those activities that are social and those that are economic are counter-productive in analyzing organizational activities.

B. The Separation Thesis and the False Dichotomy Between Social and Economic Purpose

Ultimately, defining "social enterprise" based on a distinction between social and economic organizational purpose is problematic because this distinction does not exist in the manner its proponents advocate. Using the broad definitions previously discussed, any legitimate enterprise, whether for-profit or not-for-profit, is inherently both social and economic.[110] This attempt to create a dichotomy where none exists is a species of what R.

---

104. *See* Roger E. Backhouse & Steve G. Medema, *Defining Economics: The Long Road to Acceptance of the Robbins Definition*, 76 ECONOMICA 805, 810–13 (2009) (discussing various definitions of "economics" used in textbooks throughout the years).

105. *Id.* at 805 (citing LIONEL ROBBINS, AN ESSAY ON THE NATURE AND SIGNIFICANCE OF ECONOMIC SCIENCE 15 (2d ed. 1932)) (providing Robbins' definition of economics—"Economics is the science which studies human behaviour as a relationship between ends and scarce means which have alternative uses"— as the most widely accepted in modern times); *see also* B. DOUGLAS BERNHEIM & MICHAEL D. WHINSTON, MICROECONOMICS 3 (2008) ("The field of economics . . . concerns the allocation of scarce resources. If everyone could have whatever they wanted whenever they wanted it, there would be no need for economics.").

106. BERNHEIM & WHINSTON, *supra* note 105, at 3 (noting that the field of economics addresses how resources are allocated and examining how society addresses three issues regarding resource allocation: "what to produce," "how to produce goods," and "who gets what").

107. Massetti, *supra* note 69, at 51.

108. *See* Dees, *supra* note 31, at 4; *see also* Seelos & Mair, *supra* note 46, at 244 (contrasting social value creation and economic value creation and referring to economic value creation as merely "being able to capture part of the created value in financial terms").

109. *See* Massetti, *supra* note 69, at 51.

110. *See* Seelos & Mair, *supra* note 46, at 243 ("The greatest challenge in understanding [social entrepreneurship], though, lies in defining what we mean by 'social.' First of all, there is no such thing as 'non-social' entrepreneurship . . . . [T]raditional entrepreneurship creates the majority of jobs in developed countries—certainly an important social function.") (internal citations omitted).

Edward Freeman refers to as the "separation thesis."[111] Freeman states the separation thesis as follows: "The discourse of business and the discourse of ethics can be separated so that sentences like 'x is a business decision' have no moral content, and 'x is a moral decision' have no business content."[112]

Freeman believes that this dichotomy is false, expressly denying the separation thesis and referring to it also as the "separation fallacy."[113] While Freeman specifically discusses the separation thesis in terms of business and ethics, the thesis is also relevant to this proposed dichotomy between the economic and social. We argue that a dichotomy between social and economic activities does not exist, and that placing these activities in separate spheres ultimately creates confusing definitions and perpetuates a societal and policy view that profit is necessarily made at the expense of societal benefit.[114]

When businesses create economic value, such value is inherently social because all businesses are necessarily social institutions and exist only because they create value for members of society. Once social and economic missions are dichotomized into separate spheres, then the burden arises to explain how the definitions of these two terms describe different sets of activities and motives. The problem with crafting such definitions is that one cannot engage in any meaningful economic activity alone—in order for business or economic activity to be meaningful, some interaction with other members of society must be assumed.[115] Any action that involves interaction with other members of society is the very definition of a social activity.[116] Since economic value is a social phenomenon, at least some economic activity will be inherently subsumed under any reasonable definition of the term "social."

Some commentators have recognized a problem with this dichotomy and have argued that this distinction between social and economic concerns is not dichotomous but continuous.[117] This argument posits that all of the social and economic outcomes of business activity lie on a continuum, with purely social outcomes at one end and purely economic outcomes at the

---

111. R. Edward Freeman, *The Politics of Stakeholder Theory: Some Future Directions*, 4 BUS. ETHICS Q. 409, 412 (1994).

112. *Id.*

113. *See* Lauren S. Purnell & R. Edward Freeman, *Stakeholder Theory, Fact/Value Dichotomy, and the Normative Core: How Wall Street Stops the Ethics Conversation*, 109 J. BUS. ETHICS 109, 112 (2012).

114. *See, e.g.*, Porter & Kramer, *supra* note 59, at 4 (arguing that government and civil society may be partially to blame for helping perpetuate this dichotomy through policy choices that presume "trade-offs between economic efficiency and social progress").

115. *See* BERNHEIM & WHINSTON, *supra* note 105, at 3. If economic activity is the allocation of scarce resources, then there must be more than one entity with whom the resources are to be allocated.

116. *See* NEW OXFORD AMERICAN DICTIONARY, *supra* note 99, at 1657.

117. Austin et al., *supra* note 41, at 3.

other.[118] Thus, activities of any organization will rest somewhere along this continuum, and there is no particular dividing point at which one has crossed from the realm of the social to the economic.[119] We argue that even such a continuum based distinction is false because economic matters are inherently social.[120]

A more accurate metaphor would be that the universe of social activities is a sphere in which sits a smaller sphere of economic activities as one type of social activity. For example, an individual may engage in a social activity that is not inherently economic (for example, loving a family member or friend, which does not necessarily require an allocation of resources), but one cannot engage in economic activity that is not social. Arguably, and broadly conceived, there is no activity of an organization that is not in some sense economic or business-oriented.[121] Since organizations are conglomerations of individuals or other organizations, an organization's entire reason for being is to allocate resources among various parties through value-for-value exchanges.[122]

Because all organizations are inherently social entities constantly engaging in economic activity through the allocation of resources, attempting to define "social enterprise" through reference to social activity that is conceptualized as different from standard economic activity does not reach the core of what actually distinguishes a social enterprise. By defining "social enterprise" through particular actions of an enterprise that one subjectively considers to be worthy of the moniker "social," these definitions are also inherently normative rather than descriptive. Additionally, they serve only to identify certain behaviors or strategies in which any organizational form may decide to engage. Because all organizations are constantly engaged in social and economic activities, they do not provide any principled basis for identifying social enterprises as a fundamentally different type of organization.

118. *Id.*

119. *Id.*

120. Even the proponents of this continuum argument acknowledge that their conceptualization is problematic, stating, "Even at the extremes, however, there are still elements of both [economic and social]. That is, charitable activity must still reflect economic realities, while economic activity must still generate social value." *Id.*

121. *See* KENNETH J. ARROW, THE LIMITS OF ORGANIZATION 15–29 (1974) (arguing that the essential purpose of organizations is to achieve the benefits of collective action in allocating finite resources in situations where the price system fails).

122. *Id.* The only exception to this is perhaps religious organizations. While religious organizations certainly engage in the allocation of resources, one could argue it is not their primary reason for being as with other organizations. However, since none of the definitions of social enterprise involve the actions of purely religious organizations, a discussion of such organizations is not relevant to this Article.

IV. A VALUE CREATION/CAPTURE THEORY OF SOCIAL ENTERPRISE

Noting some similar problems with the dichotomy discussed above, Professor Filipe M. Santos argues that a strong theory of social enterprise is needed that avoids using the term "social" to characterize the definition and is positive in nature, not normative.[123] Professor Santos has thus developed a distinctly different and positive theory of social entrepreneurship, which attempts to rectify the problems of normative, dichotomy-based definitions and provide a better, more descriptive basis for defining this concept so that further study can be conducted.[124] Santos' theory is based on a distinction between the strategic, organizational choice of primarily seeking value creation over value capture.[125]

Santos builds this theory on a holistic conception of value as simply "an increase in the utility of society's members."[126] Using this broad definition of "value," the activities of any organization can be described in terms of value creation or value capture.[127] Value creation occurs when "the aggregate utility of society's members increases after accounting for the opportunity cost of all the resources used in that activity."[128] Value capture occurs when "the focal actor is able to appropriate a portion of the value created by the activity after accounting for the cost of resources that he/she mobilized."[129] Thus, value capture is essentially synonymous with making a profit.[130] Some amount of value creation is necessary in order to have value capture (an organization cannot legitimately capture value unless it has created some to capture), and some amount of value capture is necessary in order to continue to fuel the value-creating activity.[131]

While these two functions are interrelated, they are not perfectly correlated.[132] An organization can, and often must, emphasize one at the expense of the other, since organizations are often faced with situations where they cannot maximize both at the same time.[133] Because of this

---

123. *See* Santos, *supra* note 58, at 337 ("In order to develop a well-bounded theory, I argue that first we need to abandon the traditional distinction between economic and social value that is so often associated with definitions of social entrepreneurship.").

124. *Id.* at 336–37.

125. *Id.* at 339 ("I argue that what distinguishes social entrepreneurship from commercial entrepreneurship is a predominant focus on value creation as opposed to value capture.").

126. *Id.* at 337.

127. *Id.* The concepts of value creation and value capture have long existed in business strategy literature. *See, e.g.*, Natalie Mizik & Robert Jacobson, *Trading Off Between Value Creation and Value Appropriation: The Financial Implications of Shifts in Strategic Emphasis*, J. MARKETING, Jan. 2003, at 63.

128. Santos, *supra* note 58, at 337.

129. *Id.* (citing Mizik & Jacobson, *supra* note 127, at 63).

130. *Id.*

131. *Id.*

132. *Id.* at 338.

133. *Id.* Santos provides the example of free cataract surgery for low-income individuals who cannot afford to pay as an example of an activity that creates substantial value for society, but will

nature of value creation and value capture, Santos asserts that organizations are constantly faced with trade-offs between the two, and typically will "maximize on one . . . and sacrifice on the other . . . ."[134] Thus, Santos argues that a critical, strategic decision for an organization is whether the organization will have a predominant focus on value creation or value capture.[135] Given the importance of this decision, Santos argues that a key distinction between social entrepreneurship and commercial entrepreneurship is a predominant strategic focus on value creation over value capture.[136] Accordingly, activities perceived by society as having a high potential for value creation and a low potential for value capture (such as helping economic development in low income areas) will naturally be areas where one would expect to find social entrepreneurs.[137]

Professor Santos' theory is valuable because it avoids defining social entrepreneurship through use of the term "social," and thus avoids making any normative judgment regarding exactly what is or is not an adequately social goal. By focusing purely on a predominant strategic choice of value creation as the characteristic that distinguishes the social enterprise from the commercial enterprise, Santos' definition also acknowledges that all enterprises are inherently economic actors, and it thus emphasizes allocation of resources as the distinguishing characteristic. Building from this powerful premise, Santos provides further propositions regarding why we have observed the activities of social enterprises in certain areas of society.

If a strategic focus on value creation is the distinguishing characteristic of the social enterprise, the question naturally arises: value creation for whom? Must the value creation be directed towards some disadvantaged portion of society in order to be considered social, as some have argued?[138] If one injects such a distinction into Santos' theory, it once again becomes normative because the proponent of the definition must make a moral judgment about what actions are considered "good" or "moral."[139] Santos

---

not lead to value capture for the organization providing the surgery because of inability to pay. He additionally explains that raising prices of a product to increase revenues and profits to the organization, but which results in lower sales, is an example of an action that increases value capture for the organization but results in less value created.

134. *Id.* at 339.

135. *Id.* at 338.

136. *Id.* at 339.

137. *Id.* at 340.

138. *See* S. Trevis Certo & Toyah Miller, *Social Entrepreneurship: Key Issues and Concepts*, 51 BUS. HORIZONS 267, 267 (2008) ("Social value has little to do with profits but instead involves the fulfillment of basic and long-standing needs such as providing food, water, shelter, education, and medical services to those members of society who are in need."). Such a definition begs the question: what member of society does not need these things? Does providing these things for a profit (as a local grocery store would) make that grocery store any less "social" or any less an important part of society?

139. *See* Santos, *supra* note 58, at 343.

rightfully avoids making any such value judgments, notes that this value creation occurs and is measured at the societal level, and does not consider the member of society receiving the created value as a relevant distinction for categorizing an organization as a social enterprise.[140] This begs the question: why do we most often see social enterprises operating to aid the disenfranchised or disadvantaged?[141] Santos explains this with two very insightful propositions.

"**Proposition 1:** The distinctive domain of action of social entrepreneurship is addressing neglected problems in society involving positive externalities."[142] This proposition flows from the strategic logic of primarily seeking value creation. If an enterprise is predominantly seeking to create value, it will naturally seek areas where the potential for value creation is highest.[143] Areas where there is a high potential for value capture will likely already be served by commercial enterprises, impeding the opportunity for social entrepreneurs to operate effectively.[144] However, areas where there are strong opportunities for positive externalities tend to be neglected by commercial enterprises because the positive externalities result in "leaks" in the value chain, limiting opportunities for value capture.[145] Conversely, the opportunity for positive externalities increases the likelihood of value creation because the social entrepreneur is creating more positive societal impact per resource expended.[146]

"**Proposition 2:** Social entrepreneurs are more likely to operate in areas with localized positive externalities that benefit a powerless segment of the population."[147] Santos notes that helping the poor is not a sine qua non of social entrepreneurship, but simply points out that most areas of neglected problems with positive externalities happen to be areas that affect disadvantaged populations.[148] This is due to the fact that the government is a typical provider of goods where markets fail to provide them and strong positive externalities exist.[149] However, where a particular populace also has little political power such that the government is not incentivized to meet the societal need, that segment of the populace is unlikely to be provided for at all.[150] This leaves a gap in the current societal framework for social entrepreneurs to act without being crowded out by either the

140. *Id.* at 337, 343.
141. *See* Seelos & Mair, *supra* note 46, at 242–43 (discussing how social entrepreneurship typically caters to fulfilling basic human needs for those who cannot afford them and providing case examples).
142. Santos, *supra* note 58, at 342.
143. *Id.*
144. *Id.*
145. *Id.* at 342–43.
146. *Id.*
147. *Id.* at 343.
148. *Id.*
149. *Id.* at 341.
150. *Id.* at 343.

government or the market.[151] This proposition explains the observable phenomena where we typically see social enterprises operating with disadvantaged populations, and yet it does not make a normative judgment that such organizations must or should operate in such a sphere in order to be considered social enterprises.[152]

Santos' theory provides a very powerful explanatory framework for viewing social entrepreneurship and avoids making any distinctions between economic and social activities. It also avoids making any normative judgments regarding whether an organization's mission is "social" enough to qualify as a social enterprise. By giving social enterprise a defined role within the economic system without making any such normative judgments, we argue that using this theory of social entrepreneurship is a much better starting point for evaluating whether business entity law needs to be reformed to account for social enterprises, and if so, how.

A simple example of an actual company illustrates how this theory avoids the normative problems of previous definitions of social enterprise. As previously discussed, d.light is a self-described social enterprise that designs and sells solar lamps throughout the developing world.[153] If one utilizes one of the common definitions discussed above to determine whether d.light is in fact a social enterprise, we must make the normative judgment of whether its mission of providing light in the developing world is in fact a "social mission" or is creating "social value."[154]

Most members of society would look at d.light's mission and answer in the affirmative, but it is difficult to determine a principled reason for why this is the case. If the standard of judgment for what constitutes "social value" is that used by Professor Dees, which relies on creating value for those who cannot afford to pay,[155] then arguably d.light is not in fact a social enterprise. d.light's business model is not based on giving its solar lanterns away—it sells them.[156] Thus, under Dees' definition, one could argue that d.light's business model is focused on creating and sustaining

151. *Id.* Traditional non-profits certainly help fill this gap as well. However, social entrepreneurs are also finding the ability to make an impact in these areas using more business-based strategies typically not implemented by more traditional non-profits. Notably however, under Santos' theory of social entrepreneurship, a social enterprise could operate as a for-profit or a not-for-profit entity.

152. *Id.* at 343–44. Santos notes that efforts to help advantaged populations can also be considered social entrepreneurship and provides the example of Wikipedia. He argues that Wikipedia benefits mainly advantaged populations (literate audiences with Internet access) but still represents a social enterprise using an innovative value creation strategy to benefit society. *Id.*

153. *See Who We Are*, *supra* note 6.

154. *See supra* Part II.

155. *See* Dees, *supra* note 31, at 2–3. Dees appears to define "social value" as creating value for those who cannot afford to pay for it.

156. *See Customer Benefits*, *supra* note 7.

private value for its customers, since they are paying for the goods they receive.[157]

Alternatively, one could state that d.light pursues a "social mission" because its goal is to help a disadvantaged population in developing nations.[158] However, this argument is based on an inherently normative judgment that providing a service to the poor is more social than providing a service to the wealthy. The basic meaning of the term "social" is not "poor" or "disadvantaged"—it simply means, in the most basic sense, "of or relating to society or its organization."[159] Certainly all members of society, not just the poor, have basic needs that must be met, and meeting those needs should be considered to be a social act. Additionally, some companies, such as Walmart, provide products and services mainly targeted towards lower income households but are not typically acknowledged as social enterprises, even though they may create tremendous societal benefits by providing affordable food and other goods to a large number of people.[160] This example illustrates again how defining "social enterprise" through a false dichotomy between social and economic goals ultimately requires a normative and subjective attribution to the term "social," thus creating difficulties in defining these organizations in a principled manner.

Santos' value creation-based theory, however, provides us with a more principled basis for categorizing d.light as a social enterprise and differentiating it from a traditional business. d.light's organizational objective can be readily identified as one focusing on value creation over value capture.[161] It has chosen to target a market where it will have the most opportunity to create broad value at the expense of the opportunity to capture more value by targeting other, more profitable markets.[162] Santos' two propositions regarding social enterprise also fit well and serve to

---

157. *Id.*

158. *See* Seelos & Mair, *supra* note 46, at 243 (indicating that they would define a social mission this way: "Social entrepreneurship creates new models for the provision of products and services that cater directly to basic human needs that remain unsatisfied by current economic or social institutions"); *see also* Martin & Osberg, *supra* note 84, at 35 ("Unlike the entrepreneurial value proposition that assumes a market that can pay for the innovation, and may even provide substantial upside for investors, the social entrepreneur's value proposition targets an underserved, neglected, or highly disadvantaged population that lacks the financial means or political clout to achieve the transformative benefit on its own.").

159. NEW OXFORD AMERICAN DICTIONARY, *supra* note 99, at 1657.

160. *Our Story*, WALMART, http://corporate.walmart.com/our-story/ (last visited Apr. 11, 2014) ("Each week, more than 245 million customers and members visit our 11,000 stores under 69 banners in 27 countries and e-commerce websites in 10 countries.").

161. *Who We Are*, *supra* note 6 ("d.light is a for-profit social enterprise whose purpose is to create new freedoms for customers without access to reliable power so they can enjoy a brighter future.").

162. *Id.* ("We design, manufacture and distribute solar light and power products throughout the developing world.").

explain why d.light has chosen to focus on developing markets in fulfilling its value creation mission.[163]

This example illustrates how Santos' positive theory provides a very powerful explanatory framework for understanding social entrepreneurship yet refrains from making any distinctions between economic and social activities. It avoids using the term "social" tautologically, thus avoiding the problem of twisting this word to mean something that it does not, as well as the requirement of a normative judgment of whether an organization's mission is "social" enough to qualify as a social enterprise. We argue that using this theory of social entrepreneurship to delineate what is meant by a social enterprise is a much better starting point for evaluating whether corporate law needs to be reformed to account for this phenomenon because it provides a more objective basis for distinguishing social enterprise business models from traditional business models.

We do recommend some slight modifications to the definition for purposes of analyzing how social enterprise fits within existing corporate governance law and whether any modification to existing law is necessary. Santos' theory focuses on value creation but does not speak to whether the organization utilizes a profit-generating strategy of any kind. If value creation is the only defining characteristic, then every non-profit is a social enterprise because pure non-profits by their very nature focus only on value creation and do not engage in value capture at all. Thus, we argue that a definition of social enterprise, for purposes of determining an adequate legal entity, should include a reference to an earned income or profit-generating strategy as a distinguishing characteristic.

Additionally, for purposes of clarity, we argue that the definition needs to expressly state, in broad terms, for whom the organization is creating value. Broadly understood, Santos' theory describes value creation for any party besides the corporation's shareholders.[164] In both business and legal literature, all of the various parties with an interest in the organization—such as customers, employees, suppliers, creditors, and stockholders—are commonly referred to as "stakeholders."[165] Thus, we advocate a definition of social enterprise expressly stating that social enterprise has the primary mission of seeking value creation for one or more stakeholder groups besides shareholders or owners of the organization.

With these two slight addendums, we propose the following definition of "social enterprise": ***an organization that utilizes an earned income strategy to accomplish a primary organizational mission of creating value for one or more stakeholders besides the organizations' shareholders or***

163. *See* Santos, *supra* note 58, at 342–43.

164. *See id.* at 337, 343.

165. *See* R. Edward Freeman & David L. Reed, *Stockholders and Stakeholders: A New Perspective on Corporate Governance*, CAL. MGMT. REV., Spring 1983, at 88–91 (discussing the development, adoption, and definition of the term "stakeholder").

owners. We believe this definition is superior to previous ones because it avoids the problematic distinction between social and economic functions of organizations while also reaching the core of what distinguishes social enterprises at the organizational level. Social enterprises, like non-profits, focus on value creation over value capture.[166] However, like for-profits, they seek to create this value through a strategy of earning income and do not abandon the potential for value capture.[167]

V. SOCIAL ENTERPRISE AND THE LAW

Developing a consistent and principled theory of social enterprise is critical to law and policy development because how "social enterprise" is defined will ultimately drive one's view of how it should be treated under the law. If one's starting point is defining "social enterprise" through a dichotomy characterizing the social and economic functions of organizations as distinct spheres of activity, then a logical conclusion is that new legal entity forms are necessary to accommodate these enterprises. However, if the social enterprise is understood as a decision to focus on value creation over value capture, then social enterprise is best conceptualized not as a uniquely different type of business necessitating a new legal entity structure, but as a strategic choice that can be implemented by any business organization.

With this understanding of social enterprise as a foundation, a strong argument can be made for a different set of legal reforms and policy proscriptions aimed at incentivizing social enterprise strategies to spread as widely as possible, rather than limiting them to a certain sector of society or entity type. By proposing the adoption and use of a value creation theory of social enterprise, we argue that developing new entity types is unnecessary and may have the unintended consequence of limiting the growth of social enterprise. We advocate that instead of limiting social enterprise by creating new entity forms, legal scholars and practitioners should focus on policies and legal reforms that highlight the ability of all organizational types to operate under a social enterprise strategy of focusing on value creation.

A. SOCIAL ENTERPRISE CAN OPERATE WITHIN EXISTING CORPORATE FORMS

Some commentators have argued that because social enterprises appear to straddle the line between for-profit and not-for-profit organizations, new

166. *See* Santos, *supra* note 58, at 339. While Santos limits his discussion to the distinction between value creation and value capture, we argue that this distinction can be used to describe the activity of non-profits as primarily focused on value creation rather than value capture.

167. *See* Kerr, *supra* note 40, at 634 (noting that social entrepreneurship involves seeking both a "financial return" and "social progress"); *see also, e.g.*, *Who We Are*, *supra* note 6 (noting that while its mission is to spread light to the developing world, it still operates as for-profit, and thus has not eliminated the opportunity for value capture).

hybrid entities are needed to accommodate these special organizations.[168] The fundamental reason for such a view is the acceptance of a dichotomy-based distinction between the economic and the social, which leads to a conceptualization of a social enterprise as a new sector of society requiring its own unique set of laws in order to function. This argument is also based on the belief that for-profit organizations are required by law to pursue financial profits for shareholders to the detriment of creating value for other members of society.[169] According to this argument, if social enterprises pursue a mission of value creation rather than acting solely to capture value for shareholders, such a strategy is a breach of fiduciary duty, necessitating new corporate forms with different corporate governance structures.[170] This viewpoint is based on a fundamental misunderstanding of corporate governance law,[171] as well as the misguided belief that a focus on providing profits to shareholders must necessarily come at the expense of society or other stakeholders.[172]

The reality of operating a profitable enterprise is that *all* businesses must serve a broad variety of stakeholders beyond their shareholders and must deliver some type of benefit to these stakeholders in order to succeed.[173] Any business that does otherwise will cease to exist, as it will be unable to generate sustainable income.[174] Nevertheless, critics frequently allege that the legal norm of shareholder primacy, which states that fiduciary duties of directors and officers are owed only to the corporation

---

168. *See, e.g.*, BILLITTERI, *supra* note 2, at 2 (discussing social enterprise and noting that "[t]his new generation of hybrid organizations is taking root in a fertile space between the corporate world, which is constrained by its duty to generate profits for shareholders, and the nonprofit world, which often lacks the market efficiencies of commercial enterprise"); SABETI & THE FOURTH SECTOR NETWORK CONCEPT WORKING GRP., *supra* note 4, at 4–5 (advocating certain core characteristics of an archetypal "For-Benefit" organization); Clark & Babson, *supra* note 5, at 825–38.

169. *See, e.g.*, BILLITTERI, *supra* note 2, at 14 ("Because traditional corporations have a duty to maximize financial returns for shareholders, broadening that mandate to include a duty to a social mission could require revisions in state corporate law.").

170. *Id.*

171. *See* Justin Blount & Kwabena Offei-Danso, *The Benefit Corporation: A Questionable Solution to a Non-Existent Problem*, 44 ST. MARY'S L.J. 617, 659–60 (2013) (noting that current corporate law does not require that companies focus only on maximizing shareholder profits); *see also* Kerr, *supra* note 40, at 659–68 (arguing that the business judgment rule allows boards of directors of for-profit corporations to direct the corporation to engage in social entrepreneurship without violating their fiduciary duties).

172. *See* Porter & Kramer, *supra* note 59, at 64 ("Business and society have been pitted against each other for too long. That is in part because economists have legitimized the idea that to provide societal benefits, companies must temper their economic success.").

173. *See* Max B. E. Clarkson, *A Stakeholder Framework for Analyzing and Evaluating Corporate Social Performance*, 20 ACAD. MGMT. REV. 92, 107 (1995) ("The corporation's survival and continuing success depend upon the ability of its managers to create sufficient wealth, value, or satisfaction for those who belong to each stakeholder group, so that each group continues as a part of the corporation's stakeholder system.").

174. *Id.*

and its shareholders,[175] prevents for-profit corporations from seeking to create value for stakeholders, or at least limits their incentive to do so.[176] This is because the shareholders' best interest is typically articulated by courts in terms of maximizing the value of the shareholders' ownership interest in the organization.[177] However, numerous legal scholars have argued that this belief—that the norm of shareholder primacy restricts for-profit corporations from pursuing the creation of value for non-shareholder stakeholders—is erroneous and not supported by the law.[178] One reason for this is the courts' implementation of the *business judgment rule*, which insulates directors and officers from liability in carrying on the business of the organization as long as their decisions are made in good faith and attributable to a rational business purpose.[179] Because of the business judgment rule, for-profit organizations can engage in a myriad of value-creating activities without violating their fiduciary duties.[180]

175. *See* D. Gordon Smith, *The Shareholder Primacy Norm*, 23 J. CORP. L. 277, 296 (1998); *see also* Mills Acquisition Co. v. Macmillan, Inc., 559 A.2d 1261, 1280 (Del. 1989).

176. *See, e.g.*, BILLITTERI, *supra* note 2, at 15 (quoting a document outlining a Minnesota proposal for a "Socially Responsible Corporation" as stating, "Corporations would no longer be required by law, as they are now, to maximize short-term profits.").

177. *See, e.g.*, eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1, 34 (Del. Ch. 2010) ("Having chosen a for-profit corporate form, the [C]raigslist 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.").

178. *See, e.g.*, Virginia Harper Ho, *"Enlightened Shareholder Value": Corporate Governance Beyond the Shareholder Stakeholder Divide*, 36 J. CORP. L. 59, 74 (2010) ("Indeed, neither case law nor corporate statutes impose on directors and officers an obligation to maximize shareholder wealth. Even in Delaware, whose corporate code is less receptive to stakeholder interests than many other state corporate statutes, there is no requirement that management decision-making maximize shareholder wealth or even be justified solely in terms of shareholder interests.") (footnote omitted); Kerr, *supra* note 40, at 669 ("However, the existing framework of corporate governance law allows for social impact considerations. Under the laws of corporate governance, specifically the duty of care as protected by the business judgment rule, board decisions are protected."); David Millon, *Two Models of Corporate Social Responsibility*, 46 WAKE FOREST L. REV. 523, 527 (2011) (noting that while Delaware courts have referred to a duty to "maximize the long-run interests of the corporation's stockholders," they have never articulated a duty to "maximize profits without regard to competing nonshareholder considerations"); Judd F. Sneirson, *Green Is Good: Sustainability, Profitability, and a New Paradigm for Corporate Governance*, 94 IOWA L. REV. 987, 1007 (2009) ("In sum, corporate law contains no general requirement that directors and officers maximize shareholder profits and only departs from this view in rare instances that should not affect most green business decisions . . . . Thus, to the extent there is a 'duty' to maximize shareholder wealth and refrain from sustainable business practices, the duty is not a legal one.").

179. S*ee* Sinclair Oil Corp. v. Levien, 280 A.2d 717, 720 (Del. 1971) ("A board of directors enjoys a presumption of sound business judgment, and its decisions will not be disturbed if they can be attributed to any rational business purpose."); *see also eBay Domestic Holdings*, 16 A.3d at 33 ("When director decisions are reviewed under the business judgment rule, this Court will not question rational judgments about how promoting non-stockholder interests—be it through making a charitable contribution, paying employees higher salaries and benefits, or more general norms like promoting a particular corporate culture—ultimately promote stockholder value.").

180. *See eBay Domestic Holdings*, 16 A.3d at 29.

In addition to the business judgment rule, the social enterprise's focus on value creation is not necessarily at odds with the norm of shareholder wealth maximization.[181] There is a tendency to view profits to shareholders as an accrual of wealth at the expense of the rest of society.[182] In the short term, organizations often encounter trade-offs that require them to allocate value to one stakeholder group at the expense of another.[183] Such trade-offs are unavoidable. However, while these trade-offs loom large in the short term, maximizing value for shareholders in the long term does not have to occur at the expense of society as a whole.[184] Businesses can, and often do, increase the entire pool of value such that they can create shared value for both society and shareholders.[185] Thus, a strategic organizational focus on value creation for one or more stakeholders can, and often does, lead to optimal value capture for shareholders in the long term.[186]

Clearly, social enterprises can operate in a standard, for-profit corporate form. This is manifestly the fact because many existing social enterprises already do so.[187] As long as the officers and directors of the corporation can articulate a rational business reason for how the social enterprise goal of the organization is in the best interest of the corporation and its shareholders, current corporate governance law does not prevent a for-profit organization from pursuing its corporate purpose as a social enterprise. Properly understanding a social enterprise as one that focuses on value creation, as opposed to a false dichotomy between social and economic concerns, makes this point all the more clear. Additionally, as a practical matter, as long as the shareholders are knowledgeable about the social enterprise goals of the organization and in agreement with the strategy, the risk of them bringing a lawsuit to enforce a duty to maximize their profits is virtually

181. *See* Porter & Kramer, *supra* note 59, at 6 (arguing that businesses should seek to create shared value, not just profits, stating, "The concept of shared value can be defined as policies and operating practices that enhance the competiveness of a company while simultaneously advancing the economic and social conditions in the communities in which it operates. Shared value creation focuses on identifying and expanding the connections between societal and economic progress.").

182. *Id.*

183. *Id.*

184. *Id.*; *see also* R. Edward Freeman, *Managing for Stakeholders: Trade-Offs or Value Creation*, 96 J. BUS. ETHICS 7, 9 (2010) (arguing that business decision-making can transcend focusing on trade-offs between stakeholders, and quoting Bill George, the former CEO of MedTronic, as stating, "Serving all your stakeholders is the best way to produce long term results and create a growing, prosperous company . . . . Let me be very clear about this: there is no conflict between serving all your stakeholders and providing excellent returns for shareholders. In the long term it is impossible to have one without the other. However, serving all these stakeholder groups requires discipline, vision, and committed leadership.").

185. *See, e.g.*, Freeman, *supra* note 184, at 9.

186. *Id.*; *see also* Michael C. Jensen, *Value Maximization, Stakeholder Theory, and the Corporate Objective Function*, 12 BUS. ETHICS Q. 235, 246 (2002) ("Indeed, it is obvious that we cannot maximize the long-term market value of an organization if we ignore or mistreat any important constituency. We cannot create value without good relations with customers, employees, financial backers, suppliers, regulators, communities, and so on.").

187. *See, e.g.*, *Who We Are*, *supra* note 6.

nonexistent, particularly given how difficult it is to win such a suit in light of the business judgment rule.[188] While not necessary, if a social enterprise wishes to mitigate this slight risk, there are relatively simple additional steps that can be taken to solidify the value creation purpose, such as establishing articles of incorporation or shareholder agreements that expressly acknowledge the value creation strategy as being in the best interest of the corporation.[189]

B. NEW ENTITY FORMS WILL NOT MAKE IT EASIER TO OPERATE A SOCIAL ENTERPRISE

It is clear that social enterprises can operate within the current corporate governance framework. However, it is also important to address whether they can operate within this system *optimally*, or whether the focus on value capture for shareholders acts as a constraint on social enterprise. Some commentators have argued that this is the case, and that while social enterprises can operate within the current framework, their actions are sufficiently restrained in significant ways such that new legal entity forms would help their growth and advancement.[190] However, a close inspection of these arguments shows that the problems raised are inherent in the operation of any organization with multiple stakeholders and will exist under any entity structure.

1. Concerns with Raising Capital

Commentators often argue that existing legal forms act as a constraint on a social enterprise's ability to raise capital.[191] If a social enterprise forms as a non-profit entity, it will be unable to obtain investment funds because non-profits are prohibited by law from distributing profits to investors.[192] Thus, the social enterprise will be limited to seeking capital through grants

---

188. *See* Smith, *supra* note 175, at 285–86 (discussing the norm of shareholder wealth maximization, and noting, "If a director deviates from that standard by preferring the interests of a nonshareholder constituency to the interests of shareholders, the director technically violates the fiduciary duty of care. This would only be a 'technical' violation because, in duty of care cases, the universal application of the business judgment rule makes the shareholder primacy norm virtually unenforceable against public corporations' managers.").

189. Blount & Offei-Danso, *supra* note 171, at 663–69 (discussing various existing corporate law mechanisms available to those operating a social enterprise in a for-profit corporate form); *see also* Jonathan R. Macey, *A Close Read of an Excellent Commentary on* Dodge v. Ford, 3 VA. L. & BUS. REV. 177, 185 (2008) ("The goal of profit maximization for shareholders is the law, but it is only a default rule. If the shareholders and other constituents of the corporate enterprise could agree on some other goal for the corporation, then the law clearly should not interfere.").

190. *See* Murray & Hwang, *supra* note 5, at 8–21 (setting forth various limitations of existing legal forms with respect to social enterprise); *see also* Clark & Babson, *supra* note 5, at 818–19; Raz, *supra* note 48, at 291–93.

191. *See* Murray & Hwang, *supra* note 5, at 12.

192. *Id.* at 10.

and donations.[193] If a social enterprise forms as a for-profit entity, it may be difficult to attract investment from non-profit organizations or the government because of IRS restrictions on non-profits.[194] Additionally, a for-profit social enterprise may find it difficult to find private investors who are willing to tolerate reduced profits at the expense of the social enterprise's mission, and accepting private investors may additionally weaken the mission in favor of profits.[195]

These arguments raise valid concerns with starting and operating a social enterprise. However, to blame the nature of available legal entities for these problems is to point the finger at the wrong causal agent. These concerns are endemic to the nature of the social enterprise because of its focus on value creation and do not arise from issues of legal entity structure or corporate governance law, nor will they be alleviated by creating new entity forms.

The issue of charitable donations and program-related investments (PRI) in for-profit social enterprises is at its core an issue of federal tax law reform, not of entity structure.[196] Many states have attempted to make PRIs in social enterprises easier by adopting the "low profit limited liability company (L3C)."[197] However, the value of this new organization has been called into question, partially because the federal tax code has never been amended to entitle the L3C to any special presumption as a PRI.[198] Indeed, some have argued that the L3C form may actually make it less likely for an organization to receive PRI funding because its form does not precisely match IRS rules.[199]

Regarding private investment in for-profit social enterprises, there is no reason to believe that a change in entity type would encourage more investment in a social enterprise if investors were not willing to do so before. To believe this is to believe that investors either cannot understand

---

193. *Id.* at 12.

194. *Id.* at 24 (noting that under IRS provisions, tax exempt foundations can make "program related investments" in for-profit entities, provided that "(1) the foundation must be motivated solely by a desire to further its exempt charitable purpose; (2) the production of income or the appreciation of property may not be a significant factor behind the foundation's investment; and (3) only limited lobbying purposes, and no electioneering, may be served by the investments") (internal citations omitted); *see also* Raz, *supra* note 48, at 292 (noting that for-profit social enterprises cannot receive tax-exempt donations, and foundations rarely make grants to businesses).

195. *See* Murray & Hwang, *supra* note 5, at 10; *see also* Raz, *supra* note 48, at 295.

196. *See* J. William Callison & Allan W. Vestal, *The L3C Illusion: Why Low-Profit Limited Liability Companies Will Not Stimulate Socially Optimal Private Foundation Investment in Entrepreneurial Ventures*, 35 VT. L. REV. 273, 291 (2010).

197. *Id.* at 273, 291.

198. *Id.* at 291.

199. *Id.* ("Since the L3C gadget does not match the PRI rules, it is likely that non-L3C LLCs can adopt a form that better enhances their ability to receive PRIs. However, the existence of the L3C form gives rise to the delusion that the form actually does something, and ill-advised people may use it believing that the form enables PRI treatment.").

the value proposition of a social enterprise unless it is formed under a special entity structure or are naïve enough to be tricked into accepting potentially lower returns because the organization has a new and different entity structure.[200] There is no reason to believe that this is the case. Rather, the core issue is simply that most investors, even those who wish to make investments in socially responsible companies, still care about their investment returns.[201] For this reason, alternative entity structures may actually make it harder for social enterprises to find investors because forming under a different entity structure may result in the perception that the social enterprise is limited, either practically or by law, in how much financial return it can provide its shareholders.

2. Governance Challenges

Another argument for new legal entity forms is that, because social enterprises must balance the competing interests of their value creation mission against seeking profits, a new corporate form that shifts the organizational focus away from shareholders is necessary.[202] As with the concerns about raising capital, the difficulty of balancing the need for profits against the needs of various stakeholders is obviously a valid issue confronted by social enterprises. However, it is an issue that every profit-making organization must face and will not be alleviated in any way by creating new entity structures.

As previously discussed, all organizations must constantly balance the needs of various organizational constituents.[203] Even if a new entity is devised with the statutory mandate that the directors and officers of the entity must place the importance of the organization's mission over the interests of creating profit for the shareholders, the directors and officers will still be faced with decisions of balance. Under any conceivable corporate governance structure, the need to balance the interests of various competing stakeholders will always exist.[204] Simply because social enterprises have a primary focus of fulfilling a mission of creating value for a non-shareholder constituency does not mean that this balance is any more of a pressing concern for these organizations than any other or that a new entity structure will alleviate this problem.

---

200. *See* Clark & Babson, *supra* note 5, at 823 (arguing that a social enterprise formed under a hybrid entity structure, in this case the benefit corporation, will be better able to attract socially responsible investment because it can distinguish itself "among the sea of companies that claim to be 'socially responsible'").

201. *See, e.g.*, Meir Statman, *Quiet Conversations: The Expressive Nature of Socially Responsible Investors*, J. FIN. PLAN., Feb. 2008, at 40, 44 ("Socially responsible investors care about their investment returns. They generally believe that they can expect returns no lower than other investors.").

202. *See* Raz, *supra* note 48, at 295–97.

203. *See* Clarkson, *supra* note 173, at 107.

204. *Id.*

3. Branding and Legitimacy

A final argument for new entity forms is that creating new entities will allow social enterprises to brand themselves more easily as a different type of business in the minds of both consumers and investors.[205] This argument posits that branding is necessary because the number of companies that claim to be socially responsible is growing, and thus it is more difficult for consumers to determine which companies are legitimately social and which use social responsibility as a façade to gain business.[206] Thus, they argue that new entity forms will lend social enterprises that incorporate under a new hybrid entity form a level of legitimacy in the marketplace and provide assurance for consumers and investors.[207]

If valid and widely accepted measures of social responsibility existed, perhaps creating new entity forms that required public reporting of such measures would aid consumers and investors in determining which organizations are truly operating legitimately as social enterprises. However, agreed-upon standards for social responsibility reporting do not currently exist, and thus the currently proposed and adopted hybrid entity forms rely on third-party organizations, chosen by the social enterprise itself, to set standards for social responsibility reporting.[208] Therefore, there is no added transparency or branding benefit to consumers or investors created by these hybrid entity forms that cannot be gained by any other organization through simply engaging in annual social responsibility reporting audited by an established third party.[209] Additionally, if widely accepted reporting measures for social responsibility are eventually developed, society would be better served by requiring all public corporations to publicly report on such measures along with their financial reports rather than only requiring this reporting from a subset of special entity forms.

The belief that these particular issues are unique to social enterprises once again stems from the mistaken view that what distinguishes a social

---

205. *See* Clark & Babson, *supra* note 5, at 838 (arguing that new entity forms such as the benefit corporation aid consumers, investors, and entrepreneurs in differentiating true social enterprises from those which merely claim to be socially responsible).

206. *Id.* at 845.

207. *Id.*

208. *Id.* at 842 ("Unlike in the financial area, where standardized conventions for reporting financial performance have developed, there does not yet exist a standard way to report on social and environmental performance. Thus, the statutes permit benefit corporations to pick the standard that they will use.").

209. *See, e.g.*, James Weber & Kathryn A. Marley, *In Search of Stakeholder Salience: Exploring Corporate Social and Sustainability Reports*, 51 BUS. & SOC'Y 626, 628–29 (2012) (noting that corporate social responsibility and sustainability reporting by businesses worldwide has increased); *see also* Rajendra P. Srivastava et al., *Planning and Evaluation of Assurance Services for Sustainability Reporting: An Evidential Reasoning Approach*, 27 J. INFO. SYS. 107, 108–10 (2013) (discussing third-party assurance and auditing services available to for-profit corporations to verify sustainability reports).

enterprise from other organizations is a focus on a "social mission" that is distinct from the standard business focus of profit-making.[210] However, when social enterprise is properly understood through the value-creation and value-capture conceptualization that we advocate, it becomes clear that the main issues raised by advocates of hybrid entities are operational ones. Such issues exist in any business organization because of the necessity of balancing the needs and interests of multiple stakeholders.[211] Perhaps some of these issues, such as the issue of raising capital, are slightly more pronounced in a social enterprise because of the voluntary, strategic choice to focus on allocating value to non-shareholders. However, creating a new entity structure will not make this issue, or any of the others, any less pronounced.

C. THE POTENTIAL DANGER OF CREATING NEW HYBRID ENTITIES

A counterpoint to our argument must be addressed: even if new entity forms may not help individuals form and operate social enterprises, would new entity forms have the unintended consequence of harming or stifling the social enterprise movement? If these new entity forms would not cause any harm, then although they may be unnecessary, their adoption would be no cause for alarm. However, we argue that there are significant potential and unintended harms that are inherent in creating these new entity forms that cannot be ignored.

The danger of creating new entity forms is that in the long term, limiting social enterprise to certain entity forms may result in marginalizing the value creation concepts of social enterprise to a subset of business entities, which has the potential to limit social enterprise's impact on society.[212] The creation of new hybrid entities also tacitly gives credence to the widely held but inaccurate view that standard, for-profit corporations can legally justify misconduct or unethical decision-making as the relentless pursuit of profits required by corporate law.[213] However, if social enterprise is understood broadly as an organizational focus on value creation over value capture, and if such a focus is not contrary to corporate law or the realities of running a profitable business, then social enterprise has the potential to best aid society through proliferation of its value creation principles across all organizational types rather than limiting itself to a particular sector.

---

210. *See supra* Part III.

211. *See* Clarkson, *supra* note 173, at 107.

212. *See* Michaela Driver, *An Interview with Michael Porter: Social Entrepreneurship and the Transformation of Capitalism*, 11 ACAD. MGMT. LEARNING & EDUC. 421, 425 (2012). Professor Michael Porter states this same concern, arguing that continuing to view social entrepreneurship too narrowly creates the risk of undergirding a narrow definition of capitalism as something that does not address "social" issues, and social entrepreneurship's job as to "bail us out of problems created by a narrow definition of capitalism." *Id.*

213. *See id.*

When properly understood as a focus on value creation, social enterprise may represent the beginning of a general shift in focus of entrepreneurs and business managers. If more "mainstream" businesses begin to realize that focusing more on value creation or creating shared value does not prevent them from making profit and may actually lead to higher long-term profits and shareholder value, the potential positive effect of social enterprise will be increased. However, marginalizing and limiting social enterprise to certain entities that behave like non-profits and only operate in certain markets, such as serving the poor and disadvantaged, weakens this potential. Thus, the better societal outcome is for the value creation strategy of social enterprise to spread, and through broader corporate law reforms, the law can help incentivize this spread.

D. AIDING THE GROWTH OF SOCIAL ENTERPRISE BY CHANGING THE NARRATIVE OF CORPORATE GOVERNANCE

While we, and others, have argued that existing law clearly allows for-profit corporations to pursue a strategic organizational focus of value creation for non-shareholder stakeholders, nevertheless the widespread perception persists that corporations can only seek to maximize profits to the detriment of society and are required to do so by law.[214] Thus, while it may not be necessary to reform the actual underlying doctrines of corporate governance to allow social enterprise to exist, consideration should be given to how the law can change the *narrative* of existing corporate governance law to combat the popular perception that corporations must maximize profits at all costs and to make it clear that businesses can, and should, focus on creating value for society while fulfilling an objective of maximizing value for their shareholders.[215]

Courts' framing of fiduciary duties almost exclusively in terms of maximizing shareholder value has contributed to the prevailing narrative of greed and self-interested behavior that has permeated the popular perception of business and capitalism in general.[216] This narrative has in some cases become a self-fulfilling prophecy as unethical business leaders

---

214. *See, e.g.*, BILLITTERI, *supra* note 2, at 14 ("Because traditional corporations have a duty to maximize financial returns for shareholders, broadening that mandate to include a duty to a social mission could require revisions in state corporate law."); *see also* Clark & Babson, *supra* note 5, at 832 (arguing that the norms of shareholder primacy and shareholder wealth maximization prevent organizations from acting to benefit non-shareholder stakeholders).

215. *See, e.g.*, Lyman Johnson, *Pluralism in Corporate Form: Corporate Law and Benefit Corps.*, 25 REGENT U. L. REV. 269, 276 (2013) ("As this author has earlier noted, the above statements about the need for Benefit Corp. legislation result from 'the perception . . . that for-profit corporations must/should serve shareholder interests exclusively or primarily.' And consequently, these perceptions, which stem from 'conventional wisdom,' however faulty or ill-founded that wisdom may be, 'are the key for law reform.' Law reform, after all, typically takes place against a perception of need for corrective action, whether grounded rightly or wrongly.") (footnotes omitted).

216. *See supra* note 177 and accompanying text.

have wrongfully leaned on the crutch of maximization of shareholder value to justify bad behavior that often actually destroys long-term value for their shareholders.[217] In their book *Conscious Capitalism*, John Mackey, the co-CEO of Whole Foods, and Professor Raj Sisodia of Bentley University quote Marc Gafni, the director of the Center for World Spirituality, on the importance of narratives:

> Narratives are the stories that infuse our life with meaning. The narrative of business matters greatly, not only to the business community, but to every human being alive. The majority of people on the planet work in some form of business. But the dominant narrative about business is that it is greedy, exploitative, manipulative and corrupt. The majority of human beings on the planet thus experience themselves as furthering and supporting greed, exploitation, manipulation and corruption. When people experience themselves that way, they actually begin to become that way. But the true narrative is that by participating in business, they are creating stable conditions for families to be raised, they are helping build communities that can create schools, they are creating places for people to exchange value, find meaning, build relationships and experience intimacy and trust. When people realize that they are part of the largest force for positive social transformation in history, their self-perception changes.[218]

We argue not only that social enterprises *can* operate within the existing corporate governance framework, but that society is better served if they *do* operate within this framework. Their operation in this sector can help change the narrative of what it means to be a business and what business's role in society is. The key to changing this narrative is to focus on the value creation function of *all* businesses and the important societal purposes that business serves—namely, creating value for society and allocating it to its best purpose in the most efficient manner possible.[219] Continued

---

217. *See* Sumantra Ghoshal, *Bad Management Theories Are Destroying Good Management Practice*, 4 ACAD. MGMT. LEARNING & EDUC. 75, 81 (2005) (arguing that a focus only on corporate governance and management theories that can be scientifically modeled, such as the maximization of shareholder wealth, has led to managers making bad decisions in attempting to follow the theories they were taught in business school); *see also* Freeman, *supra* note 184, at 9 ("However, the assumption of narrow self-interest is extremely limiting, and can be self-reinforcing—people can begin to act in a narrow self-interested way if they believe that is what is expected of them, as some of the scandals such as Enron have shown."); Thomas M. Jones & Will Felps, *Shareholder Wealth Maximization and Social Welfare: A Utilitarian Critique*, 23 BUS. ETHICS Q. 207, 211 (2013) (noting that thinking solely in terms of management theories focused on shareholder wealth maximization and that assume that individuals are "largely self-interested, even opportunistic" can "become self-fulfilling prophecies, thus causing the underlying theories to become more descriptively valid").

218. JOHN MACKEY & RAJ SISODIA, CONSCIOUS CAPITALISM: LIBERATING THE HEROIC SPIRIT OF BUSINESS 23–24 (2013).

219. *See* R. H. Coase, *The Nature of the Firm*, 4 ECONOMICA 386, 387–89 (1937) (noting that the factors of production and allocation of resources in the economy are coordinated mainly through voluntary exchange and the pricing mechanism, not by economic planning, and noting, "An economist thinks of the economic system as being co-ordinated by the pricing mechanism

dichotomization of social versus economic functions is detrimental to changing this narrative. Thus, we argue that rather than creating new legal entities with new corporate governance structures, reform efforts would be better spent on broad-based corporate governance reforms that make it clear all businesses can, and should, focus on creating value for society in general while pursuing the creation of profit for shareholders.

Rather than creating a new "Fourth Sector" populated by social enterprises, a value-creation approach instead tears down the imaginary barriers between sectors and recognizes that businesses can operate profitably, and without violating any fiduciary duties, in markets that have typically been the domain of non-profits and governments.[220] Because of the massive amounts of wealth and resources available to business corporations, incentivizing the growth of social enterprise within traditional corporate entities has the potential of transforming how business as a whole is conducted rather than creating a smaller subset of businesses which we call "social."[221]

Effective reforms in this area will likely be difficult to implement, particularly given the nature of corporate law in the United States as a matter addressed at the state level.[222] Additionally, some of the most important reforms in how we view the role of business in society and what goals businesses should pursue need to occur in business schools and

---

and society becomes not an organisation but an organism. The economic system 'works itself.'") (internal citations omitted).

220. *See, e.g.*, Driver, *supra* note 212, at 425. Michael Porter argues forcefully for a transformation of mainstream capitalism from a focus on only profits to a focus on creating shared value:

> Yesterday there were a bunch of bankers in the room and I said: "Look, one of the largest banking services on the face of the earth you guys completely missed. Microfinance. There is now a lot of for-profit activity in microfinance. You missed the whole thing. Shame on you. How could you have missed it?" And that was because they were in a bubble. They were thinking about meeting the same old conventional needs of the same old conventional types of customers, not thinking about those customers in this broader sense that we need to learn to think of.
>
> I think we ought to be encouraging the social entrepreneurship movement . . . with some of the key concepts of shared value. Shared value is a way to help them [social entrepreneurs] think about what they are really doing here and that is really creating economic value simultaneously. I think those people then can be one of the market forces that start to push and prod corporations and inspire them to do things differently.

Id.

221. *See id.* (arguing that continuing to view social entrepreneurship too narrowly creates the risk of undergirding a narrow definition of capitalism as something that does not address "social" issues, and social entrepreneurship's job as to "bail us out of problems created by a narrow definition of capitalism").

222. *See* JAMES D. COX & THOMAS L. HAZEN, BUSINESS ORGANIZATIONS LAW 3 (3d ed. 2011).

business management practice, not just in the law.[223] Nevertheless, legal reforms can serve a vital function in this area by helping reshape the narrative of corporate law so that it matches the legal reality—that businesses are not required to focus on profits to the detriment of all other concerns. The difficulty in this area is that the narrative needs to be reshaped without destroying the valuable attributes of the U.S. corporate law system, such as shareholder primacy, which have played a pivotal role in the United States' economic success.[224] This nuanced approach is arguably more difficult to implement than simply creating new business entities, but we believe the potential benefits to society more than justify working to change the narratives of corporate law in spite of that difficulty.

CONCLUSION

In order to properly address the growing social enterprise movement, we must first start with a rigorous and accurate concept of exactly what a social enterprise is. When social enterprise is understood in terms of its value creation mission, rather than through a narrow conception of what it means to be "social," then we can understand a social enterprise not only on the level of what distinguishes it from mainstream businesses, but also by what it has in common with them. All businesses create value, not just in a constrained sense of creating profits or monetary value, but broadly in terms of the products they create, the services they offer, and the communities they serve. With this more accurate understanding of the nature of business and its role in society, a better and more precise picture of the social enterprise movement emerges. We argue that understanding social enterprise in terms of value creation leads to the conclusion that policy-makers and academics should focus on corporate governance reforms aimed at expressly broadening our understanding of what businesses can do and how they can benefit society rather than limiting social enterprise to certain social missions or sectors of society.

223. *See* Ghoshal, *supra* note 217, at 76 ("I suggest that by propagating ideologically inspired amoral theories, business schools have actively freed their students from any sense of moral responsibility.").

224. *See* Stephen M. Bainbridge, *In Defense of the Shareholder Wealth Maximization Norm: A Reply to Professor Green*, 50 WASH. & LEE L. REV. 1423, 1446 (1993) ("For many years, the basic rule that shareholder interests come first has governed public corporations. That rule has helped produce . . . the highest standard of living of any society in the history of the world.").