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**Bankruptcy & the Benefit Corporation**

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INTRODUCTION: VeggieTales and Ben & Jerry’s

I. Shareholder Value Versus Stakeholder Interests
   A. The Corporation as Servant to Human Values
   B. Enhanced Scrutiny and Job Security
   C. Pre-Existing Solutions
      1. Nonprofit corporations
      2. Tailored charters
      3. Permissive constituency statutes
      4. Low-profit limited liability companies (L3C)
   D. The Benefit Corporation
      1. Incorporation, directors, and officers
      2. Transparency and accountability
      3. Benefit enforcement proceedings
      4. Fiduciary duty and liability shield
      5. High hopes and early results
      6. Proposals for further legislative change

II. Rethinking Creditor Primacy In Financial Distress
   A. Duty-Based Approaches
      1. Contract model
      2. Enterprise model
   B. Consequence-Based Approaches

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As pressure grows for money-making businesses to prioritize social responsibility, the benefit corporation — a recent innovation in corporate governance — promises to require the directors of socially minded businesses to balance public benefit with shareholder interests. But will that promise survive the crucible of financial distress? While most discussions of the benefit corporation give only passing treatment to insolvency (or ignore it altogether), this Article provides the first complete analysis of how bankruptcy principles would apply to benefit corporations, informed by the practical context of out-of-court workouts and negotiations that take place in the shadow of the bankruptcy laws. After analyzing three normative models, including an innovative application of the channelling function of law, this Article answers that the benefit corporation's key innovations should persist in bankruptcy. But with the reticulated provisions of creditor-debtor law and the Bankruptcy Code, the Article warns that the application of that principle is complicated and provides a detailed map of some of the major considerations — and pitfalls.
INTRODUCTION: VEGGIETALES AND BEN & JERRY’S

Corporations today face growing demands to prioritize social responsibility while making money. Over the past decade, a new innovation in corporate governance — the benefit corporation — has swept the United States, introducing a new corporate form to the mix. Benefit corporations straddle the line between nonprofits and business corporations: Unlike business corporations, the directors and officers of benefit corporations have a statutory mandate to consider public benefit alongside the interests of shareholders. Yet unlike nonprofits, benefit corporations can also turn a profit and make distributions to their shareholders.

Benefit corporations have indeed been profitable and have increased in popularity. Their ranks now include household names such as Patagonia and King Arthur Flour. Liberal and conservative governors alike have signed benefit corporation legislation into law. At the same time, the benefit corporation’s unique innovations are designed (at least in part) for situations that arise during financial distress or sales of the company. And while the legal history of the benefit corporation is short, we have not yet seen the fundamental concept of the benefit corporation tested in the crucible of bankruptcy.

Since most new businesses fail, understanding the legal treatment of insolvent benefit corporations is both important and inevitable: Does financial distress require the abandonment of public benefit?

In this Article, I lay out a comprehensive map of how the law of benefit corporations would affect a benefit corporation’s course through insolvency and into bankruptcy proceedings. I draw from three theoretical approaches to argue that the key innovations of the benefit corporation should persist into bankruptcy. I then show how those innovations are just one piece of a very complex puzzle.

This expedition contributes to both bankruptcy and corporate governance theory. It also provides a useful guide to directors and officers of benefit corporations, shareholders, creditors, and courts as new issues are litigated — in most instances for the first time.


2CHRISTOPHER MARQUIS, BETTER BUSINESS: HOW THE B CORP MOVEMENT IS REMAKING CAPITALISM 83, 98 (2020).

3In 2021, a Delaware benefit corporation named Medolac Laboratories filed for bankruptcy in Nevada, see In re Medolac Labs. a Public Benefit Corp., No. 21-11271 (Bankr. D. Nev.), but that case has not yielded any published rulings on the issues raised here. While the most likely explanation for the relative dearth of filings by benefit corporations is that the corporate form is fairly new and formal bankruptcy proceedings fairly rare, this absence of bankruptcy filings to date may be in part because benefit corporations struggling financially may face pressure to reincorporate as business corporations.
Financial distress is the field on which the benefit corporation must prove itself. Two stories, one about vegetables and one about ice cream, show the importance of hard times for testing new ideas in corporate governance:

First story. Bob the Tomato and Larry the Cucumber are the lead characters of the hit animated cartoon series VeggieTales. The creator of VeggieTales, Phil Vischer, founded Big Idea Productions in 1993 as a Christian animation studio that aspired to become "the next Disney." With its groundbreaking computer animation techniques, silly sense of humor, and gentle approach to religious messaging, VeggieTales became a smash hit in the mid-1990s. Throughout its meteoric rise, Vischer steadfastly refused any distribution deals or sales that would strip the Christian content from the series. And he kept the ownership of VeggieTales among a small group to preserve its mission.

But by 2002, Big Idea was in trouble. Sales had not kept pace with overhead, and Big Idea's new full-length feature film (Jonah) didn't earn enough at the box office to save the company. Ensnared in litigation with one of its distributors, Big Idea faced a jury verdict for almost $11 million and owed approximately $10 million to LaSalle Bank, who held a lien on substantially all of its assets.

Big Idea filed for bankruptcy and undertook to sell the company through an asset sale under § 363 of the Bankruptcy Code. Multiple Christian companies laid down bids, wanting to preserve Big Idea's religious heritage. But even though the two leading bids were almost double what Big Idea owed LaSalle Bank, the bank wanted assurance that the winning bidder was good for the money, and Big Idea was forced to sell VeggieTales to a secular company named Classic Media, which in turn was bought by湿泥，一个基督教组织，提交了最高的美元价值投标为$19.6 million，强烈抗议Big Idea接受$19.3 million bid by Classic Media. See Obj. of Wet Cement Prods., Inc. to Entry of Sale Order at ¶ 4, In re Big Idea (Oct. 29, 2003) (on file with author), ECF No. 161. It argued that Big Idea should not have been allowed to add a requirement mid-auction that bidders substantiate their ability to consummate the auction sale, id., an argument that the bankruptcy
DreamWorks. In 2014, DreamWorks then rolled out a new version of VeggieTales on Netflix, stripped of the original, religious content.

Second story. Ben & Jerry's is an ice cream company known not only for quirky flavors like “Cherry Garcia” but also for socially conscious positions like investing in the local community, pioneering energy-efficient freezer technology, and being among the first companies to offer equal health care to same-sex partners. Founded in 1978 by childhood friends Ben Cohen and Jerry Greenfield, Ben & Jerry’s long stood for socially conscious entrepreneurship, placing a social mission alongside economic outcomes, a practice called “linked prosperity.”

By 2000, Ben & Jerry’s stood at a crossroads. Facing heavy competition, the board weighed whether to take the company private or sell it. When the board concluded that the company would have to be sold, Ben Cohen and a group of socially responsible investors rushed to put together a bid. But when a competitor offered $40 a share in a stock swap, the board felt that they had to allow all bidders to “put their best offers on the table” and “sell to the highest bidder or get sued.” Cohen's group couldn't keep pace. The board eventually sold the ice cream company to Unilever, a global food giant based in the Netherlands. At the time, many concerned members of the Ben & Jerry's community wondered if the company had sold out — and if the fear of lawsuits had spelled the end of its socially conscious mission.

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16See Hays, supra note 15 (noting that Vermont had passed a permissive constituency law, dubbed the “Ben & Jerry's Law,” but that the board did not want to engage in a sale that would inevitably be followed by a costly lawsuit); DANA BRAKMAN REISER & STEVEN A. DEAN, SOCIAL ENTERPRISE LAW: TRUST, PUBLIC BENEFIT, AND CAPITAL MARKETS 149-53 (2017) (arguing that the Vermont constituency law would likely have protected the board if the matter had been litigated).

17See EDMONDSON, supra note 15, at 177-78.

Would these stories have turned out differently if Big Idea and Ben & Jerry’s had been incorporated as benefit corporations? Each company faced moments of financial crisis — insolvency in one, a sale of the business in the other — and, in each situation, corporate law doctrines played a role in the decision to turn the company over to the highest monetary bidder. This sparked an existential crisis over whether these two companies, one a liberal Vermont ice cream company and the other a conservative Christian animation studio, could preserve their social mission in the face of the bottom line.

The scholarly literature has just begun to analyze these issues. Naturally, the literature on the corporate governance innovation of the benefit corporation is particularly well developed. But many authors fail to cover bankruptcy at all. Even those sources that explore financial distress frequently underappreciate the practical context of the out-of-court workouts and negoti-
tions that take place in the shadow of the bankruptcy laws.22

To be sure, a handful of scholars and practitioners have begun to explore how benefit corporations would fare during times of financial distress and into bankruptcy. Many of these commentators raise more questions than answers,23 and some, like Professors Dana Brakman Reiser and Steven A. Dean, argue that the bankruptcy process is completely inhospitable to social mission and propose other "exit strategies" to get around formal bankruptcy proceedings.24

I think bankruptcy is more hospitable to social purpose than that. Indeed, Professor Jonathan Brown's important scholarship reaches much the same theoretical conclusion as this Article does: the benefit corporation's commitment to public benefit should persist into bankruptcy.25 But Brown's treatment of bankruptcy law finds conflicts where actually the law is more unsettled or open to favorable interpretation by bankruptcy courts, leading Brown to conclude that legislative change is required.26 This conclusion is common. Many writers seem to think that further guidance from Congress or state legislatures is required.27

This Article joins Brown and others in a growing scholarly consensus that the benefit corporation's commitment to general and specific public benefit should not vanish at the onset of financial distress.28 Yet this Article is the first piece to consider fully both the implications for corporate governance and the implications for bankruptcy law, and to unite both in an analysis that explains how the benefit corporation innovation would fare in bankruptcy courts without the need for additional legislative change. This Article, in contrast with many others, concludes that no legislative change is necessary,
so long as bankruptcy courts interpret the special innovation of the benefit corporation in line with preexisting law.29

Crucially, a rarely cited provision in the Judicial Code (28 U.S.C. § 959) unequivocally provides that debtors in bankruptcy are required to manage the property entrusted to them in accordance with state law.30 Section 959 means that the leadership of a benefit corporation is required to consider public benefit in bankruptcy, just as they would outside bankruptcy. This result is consistent with the foundational principle of Butner v. United States31 that bankruptcy courts should apply state law unless there is a clear federal (bankruptcy) interest to the contrary.32

The Article proceeds as follows: Section I describes the problem that led to the development of the benefit corporation, explains the benefit corporation legislation and how it works, and compares it to other options among the panoply of corporate forms available to entrepreneurs today.

Section II provides three theoretical approaches to the question whether the benefit corporation's commitment to public benefit should persist into insolvency and bankruptcy and concludes that (for those which yield a clear answer) the answer is yes. In Section II, I introduce a form of normative reasoning not typically used in bankruptcy or corporate governance scholarship. As Professor Carl E. Schneider pointed out, one of the functions of law is to channel human activity into a manageable number of forms, so that actors in the world can understand who or what they are dealing with. I argue that, as applied to the benefit corporation, the channelling function of law suggests that the distinctive features of the benefit corporation should be retained during financial distress.

Section III points out, however, that the benefit corporation's intervention is to fiduciary duty only — just one piece of the puzzle. Even if that intervention is applied straightforwardly during times of financial stress or sales of the company, benefit corporations will nonetheless face liability from standard creditor-debtor law and generally applicable bankruptcy rules. Notably, the traditional protections given to secured creditors remain unaltered by the benefit corporation legislation. And since many companies in bankruptcy have taken on secured debt, the role of the secured creditor remains paramount.

Based on that key insight, Section IV explores how a benefit corporation would fare in times of financial distress and in formal bankruptcy proceedings. In Section IV, I explain how the innovation of the benefit corporation would

29 See infra Section III.B.1.
32 See infra note 213 and accompanying text.
operate alongside well-trod bankruptcy rules and procedures and show how various legislative proposals would (if enacted) play out in a bankruptcy.

In the end, this Article concludes that the benefit corporation’s key innovation not only should persist into financial distress, but also that its directors and officers can follow that mandate during hard times, including into a formal bankruptcy procedure, so long as they also follow all the other rules, such as absolute priority.

The Article is therefore optimistic about the distinctiveness of this new corporate form and the unique features it brings to American corporate law, while realistic about the challenges that face all enterprises when they face financial distress. Put differently, being a benefit corporation would not save the next Big Idea or Ben & Jerry’s from insolvency or tough decisions, but it would give its leadership greater latitude to face those headwinds while maintaining its distinct mission. That result paves the way for businesses to make money while doing good, knowing that financial distress will not spell the end of that endeavor.

I. SHAREHOLDER VALUE VERSUS STAKEHOLDER INTERESTS

This Section introduces the key debate over corporate purpose, which was inflamed by certain Delaware caselaw and motivated the creation of the benefit corporation. Then it identifies the specific doctrinal problems that spurred the development of the benefit corporation, explains how benefit corporations are supposed to work, and analyzes how well the legislation appears to be working in practice.

A. THE CORPORATION AS SERVANT TO HUMAN VALUES

A long-simmering debate in corporate law bubbles over from time to time: whom does the corporation serve, and to what end?

One school of thought (which I present first only because it is narrower) teaches that the business corporation’s purpose for existing is to deliver value to the shareholders. As economist Milton Friedman put it fifty years ago, “the social responsibility of business is to increase its profits.” In an early twentieth-century case, *Dodge v. Ford Motor Co.*, the Supreme Court of Michigan forced the Ford Motor Company to make a distribution to shareholders over the objections of Henry Ford, who wanted to reinvest in workers.

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33170 N.W. 668 (Mich. 1919).
34Id. at 683. In a short but provocative article, Stout argues that law schools should stop teaching *Dodge v. Ford* for a variety of reasons, including because the key language from the opinion was dicta. Lynn Stout, *Why We Should Stop Teaching Dodge v. Ford*, 3 Va. L. Bus. Rev. 163, 165 (2008).
More recently, in eBay Domestic Holdings, Inc. v. Newmark, the Delaware Court of Chancery assessed a board’s attempt to withstand a hostile takeover by repeated reference to “stockholder value.” The board of craigslist, Inc. was committed to a “community-service approach to doing business.” eBay was a minority shareholder of craigslist and was described, by contrast, as a “moniker for monetization.” Uncomfortable with eBay’s growing control over the company, craigslist’s two other directors implemented a series of protective measures designed to prevent eBay from expanding its toehold into craigslist’s business. Chancellor William B. Chandler III, writing for the Court of Chancery, held that the directors’ attempt to dilute eBay’s voting power and protect craigslist’s culture violated their fiduciary duties, since “[p]romoting, protecting, or pursuing nonstockholder considerations must lead at some point to value for stockholders.”

“Having chosen a for-profit corporate form,” Chancellor Chandler continued, “the craigslist directors are bound by the fiduciary duties and standards that accompany that form.”

A second school of thought sees the business corporation as holding social responsibility in addition to its responsibility to shareholders. Sometimes described as the “triple bottom line,” this view teaches that the business corporation has a broader goal, of contributing to social and environmental goals alongside monetary profits. Professor Lynn Stout saw the doctrine that corporations needed to prioritize shareholder value as wrongheaded and injurious. In 2019, the Business Roundtable, a nonprofit association whose members are chief executive officers of major United States companies, issued a Statement on the Purpose of a Corporation, in which the officers of over a hundred corporations committed to delivering value for “all of our stakeholders,” including customers, employees, suppliers, communities, and shareholders. In this vein, an increased number of people, including many of the

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36 A.3d 1 (Del. Ch. 2010).
37 Id. at 8.
38 Id. at 9.
39 Id. at 21.
40 Id. at 32.
41 Id. at 34.
44 Business Roundtable, Statement on the Purpose of a Corporation (Aug. 19, 2019). Whether this statement reflected genuine commitment or empty talk has recently been called into question. See Lucian
Millennial and Gen-Z generations, prefer for businesses to seek profit with an eye to social responsibility. While the 2010 eBay decision reignited the debate, these two schools of thought were articulated in a pair of articles in the Harvard Law Review in the 1930s. Professor Adolf A. Berle argued in 1931 that “all powers granted to a corporation or the management of a corporation ... are necessarily and at all times exercisable only for the ratable benefit of all the shareholders as their interest appears.” The next year, Professor E. Merrick Dodd fired back, arguing that “there is in fact a growing feeling not only that business has responsibilities to the community but that our corporate managers who control business should voluntarily and without waiting for legal compulsion manage it in such a way as to fulfill those responsibilities.”

To be fair, the gap between the two schools of thought is not as insurmountable as it may initially seem. First, even if social responsibility is not an express goal of the business corporation, the directors may consider it as part of a strategy for delivering long-term value to shareholders, instead of focusing on short-term monetary goals. Second, and even more fundamentally, the unspoken assumption of the first school is that the value sought by shareholders is monetary profit. But commentators have long recognized that this is not necessarily true.

B. ENHANCED SCRUTINITY AND JOB SECURITY

This theoretical debate about the purpose of a corporation plays out in the doctrine of the fiduciary duties that the corporation owes to its shareholders and that the directors and officers (as the ones who control the cor-
Courts have distilled these fiduciary duties into the duty of loyalty and the duty of care. The duty of loyalty requires directors and officers to act in the best interests of the corporation and, in some states, to forego personal opportunities that should be routed to the corporation and not to the individual. This duty requires directors and officers to manage the corporation free of undue influence from interested parties, including other directors, officers, and shareholders.

The duty of care requires directors and officers to make careful, informed decisions in their management of the corporation. In doing so, directors and officers are entitled to "rely on information, opinions, reports or statements"

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50 As noted above, the core concept of the modern corporation is the separation of ownership and control. See, e.g., Eugene F. Fama & Michael C. Jensen, Separation of Ownership and Control, 26 J. L. & ECON. 301 (1983); Adolf A. Berle & Gardiner Means, The Modern Corporation and Private Property (1932). Shareholders own the corporation, which is controlled by its officers and directors. The trust that is placed in directors and officers, however, is not without guidance. To ensure that their exercise of control is undertaken in service to the shareholders' ownership interests, the law places fiduciary duties on the directors and officers of the corporation. Professor Stephen Bainbridge famously analyzed corporate governance through "means" and "ends," arguing that boards of directors should control the company but that shareholder wealth should remain their objective. See Stephen M. Bainbridge, Director Primacy: The Means and Ends of Corporate Governance, 97 N.W. U. L. REV. 547 (2002). For a thorough and persuasive argument that employees should be brought alongside shareholders in corporate governance, as in Germany's codetermination model, see Grant M. Hayden & Matthew T. Bodie, Reconstructing the Corporation (2020).


52 See Broz v. Cellular Info. Sys., 673 A.2d 148, 154-55 (Del. 1996) (setting forth the "corporate opportunity" doctrine, and circumstances which demonstrate a corporate officer improperly seized a business opportunity the corporation could have undertaken); Guth v. Loft, 5 A.2d 503, 511 (Del. 1939) (holding directors of a corporation cannot lawfully seize an opportunity that the corporation would be reasonably able and expected to undertake). The fiduciary duty owed to officers receives less theoretical attention and, lamentably, the enforcement regime operates less effectively as applied to officers. Professor Megan Shaner has underscored this problem and proposed corrections, including bypassing the demand requirement and more searching scrutiny into special litigation committees. See Megan W. Shaner, The (Un)Enforcement of Corporate Officers’ Duties, 48 U.C.D. L. REV. 271 (2014); see also Megan Wischmeier Shaner, Officer Accountability, 32 GA. ST. U. L. REV. 357 (2016) (surveying ten years of Delaware caselaw).

53 Directors or officers who stand to benefit personally from a transaction or other decision should abstain from the decision. See Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984) (holding that directors and officers who stand to gain personally, or who "appear on both sides of a transaction," are likely not disinterested decision-makers). When some directors or officers have a conflict that would impair their ability to decide in line with the duty of loyalty, the corporation can set up an independent committee to make a disinterested decision.
presented by professional experts. Under In re Caremark International Inc. Derivative Litigation, the duty of care also encompasses a duty of oversight: directors cannot ignore red flags or obvious lacunae in best practices. For example, in Marchand v. Barnhill, the plaintiff alleged a complete absence of food safety controls at Blue Bell Creameries, leading to a listeria outbreak. The Delaware Supreme Court revived a Caremark claim that had been dismissed by the trial court, holding that Caremark "require[s] that a board make a good faith effort to put in place a reasonable system of monitoring and reporting about the corporation's central compliance risks."

These fiduciary duties are owed to the corporation itself, as well as to its shareholders. For this reason, the corporation and its shareholders can bring claims against the directors and officers for breach of fiduciary duty. Shareholders can also bring a derivative lawsuit on behalf of the corporation and against directors or officers, stepping into the corporation's shoes.

At the same time, a board committed to making socially responsible business decisions generally has broad latitude to do so. Decisions made by a disinterested and informed board will be reviewed under the "business judgment rule," and that permissive, deferential standard will almost never be overturned by a court. So long as the board's decision comes from a ra-

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55698 A.2d 959 (Del. Ch. 1996).
56Id. at 967.
57212 A.3d 805 (Del. 2019).
58Id. at 808.
59Id. at 824. For Blue Bell Creameries, food safety was naturally paramount. For other companies, boards might be required to consider other dangers, such as sexual harassment, hacking, or ransomware.
60Many states require shareholders first to demand that the board bring the claim itself. If the board declines to do so, shareholders may seek derivative standing to sue instead. Shareholders may also sue derivatively in the first instance, but to do so they must persuade a court that making demand on the board would have been futile, because a majority of the board could not have considered the demand in a disinterested way. See, e.g., United Food and Comm. Workers Union and Participating Food Indus. Emps. Tri-State Pension Fund v. Zuckerberg, 262 A.3d 1034, 1058 (Del. 2021) (adopting universal three-part test for demand futility). Proving that a majority of the board is disinterested is difficult to do, and courts have emphasized that would-be derivative plaintiffs ought to begin with a records disclosure lawsuit so that they have an evidentiary basis for their argument that the board was unable properly to consider demand. See Guttmann v. Huang, 823 A.2d 492, 493 (Del. Ch. 2003).
61To be sure, the board still faces entire fairness review when the board is not disinterested or informed, but that scrutiny is worth imposing on any corporation, and a socially minded one would not attempt to evade that sort of oversight. Where a majority of the board is interested, or where a majority shareholder stands on both sides of a transaction, a reviewing court will apply a form of strict scrutiny called "entire fairness." See, e.g., Krasner v. Moffett, 826 A.2d 277, 287 (Del. 2003). In contrast to the business judgment rule, the entire fairness standard is demanding and requires an examination into both fair process and fair price. See, e.g., In re Investors Bancorp, Inc. Stockholder Litig., 177 A.3d 1208, 1217 n.35 (Del. 2017); Calma ex rel. Citrix Sys., Inc. v. Templeton, 114 A.3d 565, 577 (Del. Ch. 2015) (quoting Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 361 (Del 1993), decision modified on reargument, 636 A.2d 956 (Del. 1994)). While it is not impossible to meet this standard, courts routinely emphasize that it is difficult to pass. In an important new article, Professor Lyman Johnson challenges the doctrinal construct.
tional business purpose, a court will uphold the decision and avoid “substan
tive second-guessing of the merits of the business decision.”

But that broad latitude has two notable exceptions where intermediate or
enhanced scrutiny applies, both connected to change-of-control transac-
tions. It is the court decisions establishing these exceptions that led to the
development of the benefit corporation.

First, under *Unocal Corp. v. Mesa Petroleum Co.*, a board cannot unre-
asonably adopt defensive measures to protect against a hostile takeover. The
board in *Unocal* was confronted with a takeover effort and responded with a
selective repurchase of stock to dilute the holdings of the challenger. The
Delaware Supreme Court pointed out that the board faced a conflict due to
the ever-present desire to save one’s job, and held that the board must show
that “they had reasonable grounds for believing there was a danger to corpo-
rate policy and effectiveness” and must analyze “the nature of the takeover
bid and its effect on the corporate enterprise.” Later that same year, the
Delaware Supreme Court applied similar reasoning to a rights plan that
would dilute the voting power of any would-be challenger.

Second, under *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*, when
a change of control is inevitable, the board breaches the duties of care and
loyalty when it unreasonably blocks efforts to obtain the best sale
price. In *Revlon*, the board effectively ended an active auction of the com-
pany by entering into an exclusive lock-up agreement, complete with a $25
million cancellation fee, with an investment group as a defensive measure
against a hostile takeover by another firm. The Delaware Supreme Court

of standards of review as unhelpful and redundant when layered on top of standards of conduct. See Lyman Johnson, *The Three Fiduciaries of Delaware Corporate Law — and Eisenberg’s Error*, in *FIDUCIARY OBLI-
gATIONS IN BUSINESS* (Arthur B. Laby & Jacob Hale Russell eds., 2021).

*In re Dow Chemical Co. Deriv. Litig., No. 4349-CC, 2010 WL 66769, at *9 (Del. Ch. Jan. 11, 2010); see also Corwin v. KKR Fin. Holdings LLC, 125 A.3d 304, 313 (Del. 2015) (describing the “core rationale of the business judgment rule” as that “judges are poorly positioned to evaluate the wisdom of business decisions”).

*Alexander, supra note 21, at 120. Another example of intermediate scrutiny is the “compelling
justification” demanded by the Delaware courts for decisions that interfere with stockholder voting. Bla-
sius Indus., Inc. v. Atlas Corp., 564 A.2d 651, 661 (Del. Ch. 1998); see also Coster v. UIP Companies, Inc.,
255 A.3d 952 (Del. 2021) (reversing the Court of Chancery for failing to apply the Blasius standard);
Omari Scott Simmons, *Judging the Public Benefit Corporation*, in *THE CAMBRIDGE HANDBOOK OF SOCIAL
ENTERPRISE LAW* 363 (Benjamin Means & Joseph W. Yockey eds., 2018) (discussing the Blasius standard
in the context of benefit corporations).

*493 A.2d 946 (Del. 1985).
*Id. at 956.
*Id. at 955.
*506 A.2d 173 (Del. 1986).
*Id. at 182.
*Id. at 178.
observed that the board had reached the judgment that the company had to be sold.71 Once the board decided to sell, its obligation “changed from the preservation of Revlon as a corporate entity to the maximization of the company’s value at a sale for the stockholders’ benefit,” and the directors became, in effect, “auctioneers.”72

Apart from the threat of a sale or a hostile takeover, shareholder action can cause directors to focus narrowly on pecuniary benefit. Let’s imagine that a corporation balances shareholder value alongside other constituencies, and as a result the price of its shares on the market is measurably lower than it otherwise would be. Shareholders seeking a higher return might buy those shares with an eye to replacing the board with directors more narrowly focused on profit motive.

The enhanced scrutiny of Unocal and Revlon—inflamed by Chancellor Chandler’s opinion in eBay—caused significant concern that social enterprises could not pursue their mission without significant risk of litigation.

C. PRE-EXISTING SOLUTIONS

For founders or owners of business who wish to pursue profit alongside social responsibility, corporate law already provided a number of potential solutions. None of them, however, filled the need in quite the way that the benefit corporation eventually would.73

1. Nonprofit corporations

The first option, of course, is the nonprofit corporation. The founders of a nonprofit corporation must identify its “civic, educational, charitable, benevolent or religious purpose,”74 which can be articulated either broadly or with sharp focus. Once the purpose of a nonprofit corporation is articulated and approved in its articles of incorporation, the board has a duty of obedience to those articles.75 Furthermore, state law gives the members, directors, and the attorney general the ability to enforce those articles through a derivative action.76 And generally applicable state law restricts the dissolution and the dispositions of assets of a nonprofit corporation, sometimes requiring the attorney general or the court system to approve a sale of substantially all
assets of the nonprofit corporation.77 Those provisions must be respected in any sale of assets or confirmation of a plan in bankruptcy.78

Nonprofit corporations receive special protection from some of the most aggressive creditor remedies. An involuntary bankruptcy petition cannot be filed against a corporation that is not a “moneyed, business, or commercial corporation.”79 And if a nonprofit corporation voluntarily files for bankruptcy protection under chapter 11 of the Bankruptcy Code, it retains tighter control over its bankruptcy case. While creditors can move to convert a chapter 11 reorganization to a chapter 7 liquidation, conversion is not available when the debtor is a nonprofit corporation, unless it consents.80

Those protections make it easier for a nonprofit corporation to stay on mission, and some nonprofit corporations have done so for hundreds of years. But the nonprofit corporation does not really meet the desire for socially responsible profit. After all, a nonprofit cannot have equity holders who receive distributions from profits.

2. Tailored charters

The second option is a custom-built charter: founders of a socially conscious corporation could amend the articles of incorporation, attempting to pin down the corporate purpose with greater specificity. With a tighter fo-

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78See 11 U.S.C. §§ 363(d)(1), 1129(a)(16); see also In re United Healthcare System, Inc., Case No. 97-1159, 1997 WL 176574, at *5 (D.N.J. Mar. 26, 1997) (noting the nonprofit board's “fiduciary obligation to act in furtherance of the organization’s charitable mission” in the context of selecting a bid in bankruptcy and reversing bankruptcy court for refusing to approve the sale). At the same time, courts have found that paying creditors is consistent with a nonprofit’s charitable mission. In In re Boston Regional Med. Ctr., Inc., the bankruptcy court rejected the proposition that “a charitable organization’s payment of creditors, to whom the organization incurred debts in order to further the charitable mission of the organization, is somehow separate from the charitable purpose of the organization and of gifts to that organization” and noted that “[t]he honoring of obligations at the end of a charitable organization’s life is no less integral to its mission than was the incurring of those obligations to further that mission.” 298 B.R. 1, 28 (Bankr. D. Mass. 2003), adopted as modified, No. CIV A. 03-12215RG3, 2004 WL 1778881 (D. Mass. Aug. 9, 2004), aff’d, 410 F.3d 100 (1st Cir. 2005).


8011 U.S.C. § 1112(c).
cus in its articles of incorporation, decisions of the corporation might be kept “on mission.”

This approach has been met with widespread skepticism. The fiduciary duty of the directors and officers is a matter of statutory law or common law. Whether a corporation can alter those duties through well-drafted articles of incorporation remains unclear. 81

3. Permissive constituency statutes

The third option is permissive constituency statutes. Beginning in the 1980s, in response to a wave of hostile takeovers, many states enacted constituency statutes. 82 These statutes expressly allowed corporations to consider the interests of stakeholders alongside shareholders, including in the context of change-of-control transactions (which would cover Revlon and Unocal). 83 For example, New York’s permissive constituency statute states that a director is “entitled to consider . . . the effects that the corporation’s actions may have in the short-term or in the long-term” upon employees, retirees, pensioners, customers, creditors, and the communities in which it does business. 84

Today, more than thirty states have permissive constituency statutes, with the notable exception of Delaware. 85

For many founders and stakeholders, however, the permissive constituency statutes did not go far enough. First, while such statutes allow the directors of a corporation to consider the interests of stakeholders, they do not require it. 86 And because they apply to all corporations generally, they do not signal any particular commitment on the part of any one corporation and therefore do not help a corporation marshal support for, and rally a community around, a uniquely social mission. Even more troubling, a study conducted by Professors Lucian Bebchuk, Kobi Kastiel, and Roberto Tallarita indicates that permissive constituency statutes were not used in practice to deliver wins for stakeholders at all, but rather for shareholders, executives,

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81 Attorney Frederick H. Alexander, who prepared the initial drafts of Delaware’s public benefit corporation legislation, argues that such private ordering of shareholder rights is dubious under Delaware law. See Alexander, supra note 21, at 149–52.
84 N.Y. Bus. Corp. § 717(b).
85 Orts, supra note 82, at 27–28.
86 Relatedly, because the statutes are permissive, stakeholders within the constituency probably have no standing to enforce them, and no one else does either. Indeed, the permissive constituency statutes for New York and Pennsylvania explicitly state that they create no duty toward stakeholders. See N.Y. Bus. Corp. Law § 717(b); 15 Pa. Cons. Stat. § 1717; see also Stephen M. Bainbridge, Interpreting Non-shareholder Constituency Statutes, 19 Pepp. L. Rev. 971, 992–93 (1992).
and directors.  

4. **Low-profit limited liability companies (L3C)**

Fourth, the low-profit LLC (or L3C), a precursor of sorts to the benefit corporation, was invented in 2008. First made available in Vermont, the L3C is a corporate form designed to take advantage of a tax exemption for certain nonprofit investments made for a socially beneficial purpose. Like the benefit corporation, the L3C must perform a socially beneficial activity. But the corporate form does not come with any enforcement mechanism. Even more problematically, the IRS did not issue any blanket approval for L3Cs, and so each company would have to apply for IRS recognition individually. As a result, interest in the L3C hit a plateau.

D. **THE BENEFIT CORPORATION**

Finally, in the early 2000s, in part due to the limitations of the alternatives and in part as a response to eBay, a movement for a new corporate form gained hold. Consumer trends reflected a desire for corporations to create value for both shareholders and society at the same time, yet corporate law and capital markets lacked the infrastructure to support that desire. In response, the benefit corporation sought to harness the power of business to address social challenges.

The benefit corporation label began as a certification for socially conscious businesses called “B Corps” (akin to Fair Trade or USDA Organic), launched and monitored by a nonprofit called B Lab. Over time, it morphed into a new corporate form. Attorney William H. Clark, Jr. drafted the

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89See BRAXMAN REISER & DEAN, supra note 16, at 64.


91As the Delaware Chancery Court stated, "[a] corporation cannot . . . defend a business strategy that openly eschews stockholder wealth maximization — at least not consistently with the director's fiduciary duties under Delaware law." eBay Domestic Holdings, Inc. v. Newmark, 16 A.3d 1, 35 (Del. Ch. 2010).

92The difference between the “B Corp” certification and the corporate form can be confusing but is vital for purposes of the legal analysis. A benefit corporation, the focus of this Article, is a legal form of organization that a firm can opt into through either an initial or amended certificate of incorporation. B Corp certification, by contrast, is a private status given to companies that meet rigorous standards of social and environmental performance, accountability, and transparency. B Lab, Certification, https://bcorporation.net/certification (Feb. 21, 2021). As stated earlier, B Corp status is akin to Fair Trade or USDA Organic certification. See Berrey, supra note 20, at 35. Moreover, B Corp status has no legal effect, but certification requires adherence to statutory requirements of benefit corporations. B Lab, Legal Requirements, https://bcorporation.net/certification/legal-requirements (Feb. 21, 2021).
Model Legislation, which has evolved as B Lab incorporated feedback from a wide range of sources over the past several years.

The benefit corporation aims directly at the premise that directors should prioritize the financial interests of shareholders over the interests of other stakeholders or values. Departing from the traditional for-profit corporate model, the benefit corporation places social objectives, accountability, and transparency alongside the interests of shareholders. The benefit corporation form encourages relationships among social enterprises to fulfill their benefit mission and generate capital to do so.

In 2010, Maryland became the first U.S. state to pass benefit corporation legislation, and Delaware passed its own version in July 2013. To date, thirty-three states and the District of Columbia have enacted benefit corporation statutes. This subsection lays out the core characteristics of the benefit corporation, drawing from the Model Legislation and noting differences in certain states, especially Delaware, due to Delaware’s long-standing centrality to the development of corporate law.

1. Incorporation, directors, and officers

A benefit corporation has the purpose of creating general public benefit, which the Model Legislation defines as “[a] material positive impact on society and the environment, taken as a whole, from the business and operations of a benefit corporation assessed taking into account the impacts of the benefit corporation as reported against a third-party standard.” The benefit corporation’s articles of incorporation may also identify one or more “specific public benefits” that the benefit corporation will act to create alongside general public benefit. The Model Legislation provides a nonexhaustive list of specific public benefits, including serving low-income communities, car-
ing for the environment, improving human health, and promoting the arts and sciences.\textsuperscript{103}

Currently, there are over 7,000 benefit corporations with a range of public benefits provided.\textsuperscript{104} For example, Patagonia aims to build the best product, cause no unnecessary harm, and use business to protect nature.\textsuperscript{105} Danone North America, producers of Dannon, Silk, Activia, and Oikos yogurts, aims to “nourish lives and inspire a healthier world through food.”\textsuperscript{106}

Once a corporation has been formed as a benefit corporation, or has converted to become one, it cannot terminate its status without a supermajority vote of the shareholders, nor can it (without that supermajority vote) consummate a transaction that would have the same practical effect, such as a merger or sale of substantially all its assets.\textsuperscript{107} Under Delaware law, however, a majority of the shareholders can vote to convert back to a regular corporation.\textsuperscript{108}

Directors of a benefit corporation are required to “consider the effects of any action or inaction upon” the various stakeholders of the benefit corporation, including shareholders alongside employees, suppliers, customers, the community, the local and global environment, and the benefit corporation’s purpose (both general and specific), both short-term and long-term.\textsuperscript{109} Officers of the benefit corporation must operate under the same rules where they have discretion to act and their action (or inaction) “may have a material effect” on the benefit corporation’s creation of general or specific public benefit.\textsuperscript{110} Delaware uses the language of “balanc[ing]” the interests of the vari-

\textsuperscript{103}Id. § 102 (defining “Specific public benefit”).

\textsuperscript{104}See, e.g., Berrey, supra note 20, at 26.


\textsuperscript{107}Model Legislation § 105(a)-(b); see also id. § 101 (defining “minimum status vote” as two-thirds of each class or series of equity interests, regardless of any limitation in the articles of incorporation or bylaws on the voting rights).

\textsuperscript{108}See 8 Del. C. § 361.

\textsuperscript{109}Model Legislation § 301(a)(1). A benefit corporation may appoint a benefit director and a benefit officer who, if appointed, are empowered to create general or specific public benefit and are charged with preparing the annual benefit report. Id. §§ 302, 304. In an important analysis, Johnson (despite approving of the big-picture goal of benefit corporations) criticizes this approach for failing to focus the directors’ fiduciary duties on the purpose of the corporation. See Lyman Johnson, Managerial Duties in Social Enterprise: The Public Benefit Corporation, in THE CAMBRIDGE HANDBOOK OF SOCIAL ENTERPRISE LAW, supra note 63, at 347–49. Indeed, focus on a unitary goal has long been recognized as a way to drive action. See, e.g., Matthew 6:22 (“[I]f your eye is clear, your whole body will be full of light”) (NASB).

\textsuperscript{110}Model Legislation § 303. Johnson also criticizes several state statutes for failing to articulate any
ous groups. If the state has a permissive constituency statute, the directors are permitted to consider those constituencies as well. Directors are not required to ascribe any particular priority to these stakeholders unless the articles of incorporation say so.

These provisions are “at the heart of what it means to be a benefit corporation,” and comprise a full-throated rejection of the articulation of the primacy of monetary value in *Dodge v. Ford* and *eBay*. They also put the directors and officers of a benefit corporation in the same company as directors and officers of a nonprofit corporation in their focus on the mission of the company.

2. **Transparency and accountability**

The first line of enforcement of the benefit corporation’s purpose is transparency. A benefit corporation must prepare an annual benefit report that describes its attempts to create general and specific public benefit and assesses its performance against a third-party standard. The report must describe whether the directors and officers complied with their duties under the statute. The annual benefit report must be provided to the shareholders, filed with the secretary of state of the state of incorporation, and made publicly available. Delaware requires the benefit corporation to include in

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111 "The board of directors shall manage or direct the business and affairs of the public benefit corporation in a manner that balances the pecuniary interests of the stockholders, the best interests of those materially affected by the corporation's conduct, and the specific public benefit or public benefits identified in its certificate of incorporation." DEl. CODE ANN. tit. 8, § 365(a) (West 2020).

112 Model Legislation § 301(a)(2).

113 See id. § 301(a)(3).

114 See id. § 301 cmt.

115 See id. (expressly stating that the section is meant to reject the holdings of *Ford* and *eBay*); see also *BraKman Reiser & Dean*, supra note 16, at 228. That said, the benefit corporation legislation can be enforced only by shareholders, not stakeholders, so in that fashion the benefit corporation legislation is indeed consistent with the law of shareholder primacy, which Professor Robert Rhee demonstrates to be a “filamentary principle that weaves through many important rules of corporate law and the corporate system.” Robert J. Rhee, *A Legal Theory of Shareholder Primacy*, 102 MINN. L. REV. 1951, 1999 (2018).


118 Model Legislation § 302(c).

119 See DEl. CODE ANN. tit. 8, § 366(a) (West 2020).
every notice of a shareholder meeting a disclosure of its benefit corporation status.120

3. Benefit enforcement proceedings

The benefit corporation statute provides a limited avenue for litigation to enforce the special duties of the directors and officers. Under the statute, all legal actions predicated on the benefit corporation’s “failure . . . to pursue or create general public benefit or a specific public benefit” or “violation of an obligation, duty, or standard of conduct” must be brought as a “benefit enforcement proceeding.”121

The benefit corporation may bring a benefit enforcement proceeding directly against a director or officer,122 or a shareholder or group of shareholders (whose equity interests exceed a certain threshold) may bring such claims derivatively.123 In a derivative benefit enforcement proceeding, like any derivative suit, the shareholders step into the shoes of the corporation and enforce the fiduciary duties owed to it. The derivative suit must follow state law and court rules governing derivative actions generally,124 which means that derivative plaintiffs must give the board a chance to bring the claim directly first (i.e., make demand), or plead that making such a demand would have been futile because the board could not have considered such a demand in a disinterested way.125

Benefit enforcement proceedings can be brought for injunctive or declaratory relief only. Shareholders might, for example, seek to enjoin a sale or ask a court to order the board to deliver the annual benefit report.126 Benefit corporations are exonerated from monetary damages in benefit enforcement proceedings,127 as are directors and officers who act disinterestedly, unless

120DEL. CODE ANN. tit. 8, § 366 (West 2020).
121Model Legislation § 305(a).
122Id. § 305(c)(1).
123Id. § 305(c)(2). The Model Legislation grants derivative standing to shareholders holding 2% of any class of shares or 5% of the benefit corporation’s parent organization. Id. Delaware has slightly different thresholds, 2% of outstanding shares, or for a publicly traded corporation, 2% or $2 million in value, whichever is lower. 8 DEL. CODE ANN. tit. 8, § 367 (West 2020). States have different thresholds — some zero, others 10% or more for a parent. See CLARK, supra note 21, at A-27.
124See Model Legislation § 305(c)(2); 8 DEL. CODE ANN. tit. 8, § 367 (West 2020) (“This section shall not relieve the plaintiffs from complying with any other conditions applicable to filing a derivative action including § 327 of this title and any rules of the court in which the action is filed.”).
126The comments to the definition for “benefit enforcement proceeding” specifically describe a benefit enforcement proceeding to enforce “the obligations of a benefit corporation under section 402(b) to post its benefit reports.” Model Legislation § 102 cmt.
127Id. § 305(b). The Model Legislation statute could be read to suggest that a plaintiff may seek monetary damages for the benefit corporation’s failure to make its annual benefit report available, but it is hard to imagine how a plaintiff would prove damages on that theory.
provided otherwise in the articles of incorporation or bylaws. 128

4. Fiduciary duty and liability shield

The benefit corporation legislation also clarifies the content of the general fiduciary duties of the directors and officers. As the official comments make clear, the benefit enforcement proceeding does not displace traditional actions (whether direct or derivative) for traditional breaches of duty, those not based on the unique duties under the benefit corporation legislation. 129

What the statute does, instead, is specify that directors and officers comply with their fiduciary duties when they are disinterested, reasonably informed, and acting in good faith. 130 In effect, this provision deems the enhanced scrutiny of Revlon and Unocal to have been met. 131 When the board of a benefit corporation approaches a sale of the company or a hostile bid, then, it may balance pecuniary interests alongside public benefit in making its decision.

5. High hopes and early results

How has all of this worked? To start, a significant number of corporations re-incorporated as benefit corporations, 132 and still more have been founded as benefit corporations. Today, there are more than 7,000 benefit corporation entrepreneurs who have collectively received more than $2.5 billion in investments. 133 Senator Elizabeth Warren proposed federalizing the

128 Id. §§ 301(c), 303(c).

129 Id. § 305 cmt. ("This section only applies to actions or claims arising under this chapter. Lawsuits for breaches of duty arising outside of this chapter, or for breach of contract by directors, officers, or the benefit corporation are not subject to this section."). As a threshold matter, the statute makes clear that beneficiaries of the benefit corporation's general or specific public benefit do not have standing to sue the officers and directors for breach of duty. Id. §§ 301(d), 303(d); accord DEL. CODE ANN. tit. 8, § 365(b). See also CLARK, supra note 21, at A-28.

130 A director who makes a business judgment in good faith fulfills the duty under this section if the director: (1) is not interested in the subject of the business judgment; (2) is informed with respect to the subject of the business judgment to the extent the director reasonably believes to be appropriate under the circumstances; and (3) rationally believes that the business judgment is in the best interests of the benefit corporation." Model Legislation § 301(e); see also id. § 303(e). The Delaware statute makes this more explicit, providing that "[a] director . . . with respect to a decision implicating the balance requirement [under the statute], will be deemed to satisfy such director's fiduciary duties to stockholders and the corporation if such director's decision is both informed and disinterested and not such that no person of ordinary, sound judgment would approve." DEL. CODE ANN. tit. 8, § 365 (West 2020).

131 See ALEXANDER, supra note 21, at 123-26.


133 See B Lab, Benefit Corporations Raising Capital, https://benefitcorp.net/benefit-corporations-raising-capital. At least one author has engaged in a robust empirical study of adoption of the public benefit
concept by requiring all corporations with more than $1 billion in annual revenue to get a federal benefit corporation charter. The benefit corporation concept has migrated to other countries.

Less enthralled with the concept, some scholars have suggested that the benefit corporation legislation was wholly unnecessary, since a corporation that wishes to pursue public benefit can do so in many ways without reincorporating as a benefit corporation. Stout argued, for example, that corporate governance principles afforded ample room for directors to pursue public benefit. On the other side of the field are commentators like the Honorable Leo E. Strine, Jr., former Chief Justice of the Delaware Supreme Court, who argues that Delaware law emphasizes shareholder welfare throughout — a stark reality that, in his view, makes the benefit corporation legislation necessary, a "modest, but genuine, example of... a step forward."

As for the protections afforded to the board of benefit corporations, the liability shield removing enhanced scrutiny appears to have worked. The provisions have not been cited in published opinions, and this author is una-
ble to find any instances of the directors or officers of a benefit corporation being sued for breach of fiduciary duty.

On the other hand, less than ten percent of benefit corporations even produce annual reports, and while shareholders can bring benefit enforcement proceedings to enforce this obligation, such lawsuits seem not to have occurred. Similarly, no benefit enforcement proceedings have been brought — at least none reflected in reported decisions — an observation made previously by others. Some, like Brakman Reiser and Dean, conclude that benefit corporations “do not have the teeth needed for the task.”

6. Proposals for further legislative change

Due to dissatisfaction with the enforcement of the benefit corporation’s purpose, a number of commentators (including Brown, Schildhorn, and Keilson) have suggested further amendments to the benefit corporation legislation. Most prominently, several commentators advocate for empowering state attorneys general to enforce the statutory mandate, along with share-
holders. Others have suggested that state law restrict transfers of substantially all assets of benefit corporations in the same way that it restricts such transfers for nonprofits.

II. RETHINKING CREDITOR PRIMACY IN FINANCIAL DISTRESS

As described above, the clear intent of the benefit corporation legislation was to empower — indeed, to mandate — that the board of a benefit corporation consider general and specific public benefit. How should that corporate law innovation operate when a benefit corporation experiences financial distress?

The answer to this question is core to the fate of the benefit corporation. Indeed, it is in times of financial crisis (insolvency or a sale of the company, when Revlon and Unocal loom on the horizon) that the benefit corporation's innovations matter most. But if a benefit corporation acts the same as a business corporation in such times, the key differences between the benefit corporation and its less socially conscious neighbors vanish. This was precisely the concern for both Big Idea and Ben & Jerry's.

In this Section, I discuss two standard ways of talking about this question: duty and consequences. This Section analyzes each in turn and also introduces a third approach, corporate character and the channelling function of law, which I argue provides the most helpful frame for the questions we are grappling with here. While duty and consequences are either circular, inconclusive, or awaiting further data, the channelling function of law helpfully illustrates the following two points: first, benefit corporations should have distinctive features that enable them to attract community support, and second, those features should persist into financial distress.

A. DUTY-BASED APPROACHES

The first theoretical approach is through the lens of duty. The grounding question in this approach is to ask what we owe each other. In the context discussed here, the grounding question is: when a benefit corporation experiences financial distress, what duty do the directors have to the corporation's stakeholders? This is a classic question in corporate law, and it is one that has been debated extensively.

Duty-based approaches to creditor primacy in financial distress focus on the obligations of the directors to the corporation's creditors. This approach argues that the directors have a duty to maximize the recovery of creditors' claims, even at the expense of the corporation's other stakeholders. The argument is that creditors are entitled to the full return of their investment, and that the directors have a duty to ensure that this is achieved.

However, this approach has been criticized for being too narrow and excluding the interests of other stakeholders, such as the corporation's shareholders and employees. Moreover, it has been argued that duty-based approaches are circular and inconclusive, as they do not provide a clear answer to the question of how to balance the interests of creditors and other stakeholders.

In contrast, a duty-based approach that focuses on the rights of creditors may be more effective in ensuring that creditors are treated fairly. This approach argues that the directors have a duty to protect the interests of creditors, and that this duty is stronger than any other duty that the directors may have.

Nonetheless, this approach has also been criticized for being too narrow and excluding the interests of other stakeholders. Moreover, it has been argued that duty-based approaches are circular and inconclusive, as they do not provide a clear answer to the question of how to balance the interests of creditors and other stakeholders.

In summary, duty-based approaches to creditor primacy in financial distress are a useful starting point for understanding the obligations of the directors to the corporation's creditors. However, they are limited in their ability to provide a clear answer to the question of how to balance the interests of creditors and other stakeholders.
text of this discussion, that question becomes what duties the benefit corporation (and its directors and officers) owes to shareholders and creditors. Once a corporation is insolvent, creditors take the place of shareholders as the focus of the board’s fiduciary duties. But that only makes the question more complicated. On the one hand, if creditors are simply stepping into shareholders’ shoes, then perhaps the creditors should be owed the same duties as the shareholders were owed when the company was solvent. On the other hand, perhaps the adjustments to the fiduciary duty owed to shareholders should remain isolated to the shareholders. After all, creditors may not have consented to being subordinated to a public benefit — certainly not involuntary creditors, like tort victims.

The theoretical literature provides two models for thinking about the duties owed by corporations.

1. *Contract model*

The contract model conceives of the corporation in a narrow sense: shareholders contract with the corporation to provide a certain benefit, traditionally, a monetary one. But in the case of a benefit corporation, the implicit premise of that contract — profit motive at all costs — is fundamentally altered. Since the purpose of a benefit corporation expressly includes general and specific public benefit, one should assume that shareholders of such a corporation have agreed that monetary benefit is not the only thing that they believe the benefit corporation owes to them.

But that leaves untouched the assumptions about what duties an insolvent benefit corporation owes to creditors, an observation shared by Brown. On the one hand, while the shareholders of a benefit corporation may have agreed to a socially responsible model, creditors have not made such an agreement — especially involuntary creditors, like tort victims. On the other hand, why should we assume that the creditors place an overriding value on money when the shareholders do not? A benefit corporation might

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145 See *infra* Section III.A.1.
146 To be sure, corporate law theorists have debated whether this benefit is understood to be on a short-term or long-term basis, a question which has profound implications for corporate governance.
147 See Brown, *supra* note 25, at 40.
148 See id. at 38–39 & n.166. This problem is widespread: one study found that almost a quarter of unsecured debt in certain bankruptcy cases was owed to “reluctant creditors.” See TERESA A. SULLIVAN, ELIZABETH WARREN & JAY L. WESTBROOK, AS WE FORGIVE OUR DEBTORS 18, 294 (1989). The problem of involuntary creditors is not unique to the benefit corporation and would apply just as forcefully in the context of non-profits. Even with standard for-profit companies, the low priority of most involuntary creditors raises a significant challenge to the fairness and adequacy of bankruptcy proceedings. Some scholars, such as Lynn LoPucki, have proposed giving such involuntary creditors superpriority in bankruptcy, a solution that would carry over into the bankruptcy of a benefit corporation. See Lynn M. LoPucki, *The Unsecured Creditor’s Bargain*, 80 VA. L. REV. 1887 (1994).
attract socially responsible lenders who want to invest in a socially responsible organization.149 Even those lenders who are not socially responsible lenders are on notice that they are dealing with a benefit corporation. Furthermore, not all creditors are lenders: the creditor constituency also includes groups, such as employees or sustainable suppliers, that may be expressly included within the scope of general public benefit that the benefit corporation is required to consider. Those creditors, too, may prioritize a broader conception of corporate duty.

2. Enterprise model

By contrast, the enterprise model of a corporation, championed by Professors Margaret Blair and Lynn Stout (among others), sees the corporation as a joint enterprise including everyone involved in the corporation’s activities in the world.150 Under the enterprise model, the corporation has obligations not only to its owners but also to everyone else who supports and advances the enterprise.

One might think that the enterprise model straightforwardly counsels in favor of the benefit corporation’s distinct mandate persisting into conditions of financial distress. Indeed, financial distress may be precisely when it is most important for a socially responsible enterprise to cleave to its mission. Shouldn’t bankruptcy “honor its obligations to all who made firm-specific investments at the invitation of the firm”?151 And indeed, such stakeholders are already recognized by the Bankruptcy Code in some respects.152

But this is not necessarily true. The enterprise model assumes a going concern. But under conditions of insolvency, the enterprise’s liabilities outweigh its assets, and (let’s imagine) there are no prospects of a change on fortunes. How does the theory account for a failed enterprise? Shouldn’t the

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149See, e.g., David Nows & Jeff Thomas, Delaware’s Public Benefit Corporation: The Traditional VC-Backed Company’s Mission Driven Twin, 88 UMKC L. Rev. 873, 900–16 (2020) (discussing best practices for financing a public benefit corporation, including strategies for attracting impact investors and socially-minded lenders); Dana Brakman Reiser & Steven A. Dean, Financing the Benefit Corporation, 40 Seattle U. L. Rev. 793, 795–810 (2016) (discussing attributes of current financial instruments used to provide capital to public benefit corporations, and theorizing tailored instruments to better achieve that purpose). The idea of mission-driven investment with potentially lower financial payoffs, or “impact investing,” has become more popular since the mid-2000s. See generally ANTHONY BUGG-LEVINE & JED EMERSON, IMPACT INVESTING: TRANSFORMING HOW WE MAKE MONEY WHILE MAKING A DIFFERENCE (2011) (describing various investment strategies as part of the growing field of impact investing).

150See, e.g., Margaret M. Blair & Lynn A. Stout, A Team Production Theory of Corporate Law, 85 Va. L. Rev. 247 (1999). Justice Douglas articulated this perspective in Pepper v. Litton, 308 U.S. 295 (1939), stating that the “standard of fiduciary obligation is designed for the protection of the entire community of interests in the corporation — creditors as well as stockholders.” Id. at 307 (citations omitted).


corporation prioritize its obligations to creditors, many of whom will already be participants in the enterprise?

Ultimately, the issue with relying on a deontological or duty-based approach is that any answer can readily be accused of question-begging. This is especially true of a new corporate form where the scope of the duties involved do not have a long history. Over time, as the issues raised in this Article are resolved by courts, the duties of the benefit corporation will come into sharper focus. Until then, a duty-based approach can help us articulate multiple ways that these duties could be understood, but it cannot guide us to a resolution.

B. Consequence-Based Approaches

The second theoretical approach is through the lens of consequences and incentives, drawing from utilitarian ethics. This approach asks us to consider the effects upon the world — both directly and indirectly — through the setting of ex ante incentives. If the benefit corporation retained its mandate into financial distress, to the detriment of creditors, how would that affect prudent management, the cost of lending, and takeover risk?

1. Prudent management

To be sure, if a benefit corporation can maintain its commitment to public benefit through insolvency and bankruptcy, that might incentivize riskier business practices. Put differently, the prospect that the benefit corporation would be treated just as any other corporation in insolvency and bankruptcy could incentivize more prudent stewardship of resources, in the interest of keeping the benefit corporation solvent.

At the same time, the threat of abandoning social purpose in insolvency might be too strong of an incentive, leading entrepreneurs to be overly cautious and insufficiently aggressive in pursuing their mission — or it might make them abandon the concept altogether. Indeed, the whole premise of the benefit corporation seems couched in a legislative judgment that the incentives created by the standard approach are insufficiently hospitable to social enterprise.

2. Cost of lending

One could argue that a benefit corporation that maintains its commitment to public benefit would face a higher cost of capital. Lenders who know that their interests will be discounted during times of financial distress may be less inclined to lend, or they may only lend at higher rates. For

153 The role of courts is precisely to clarify legal obligations and so where those obligations are uncertain, the declarative function of courts comes into sharper focus.

154 This language draws from consequentialist or utilitarian ethics, which traces back to (at least) English philosopher Jeremy Bentham (b. 1748).
similar reasons, lenders may be more likely to insist on taking a security interest to guarantee their loan (and they may be more likely to foreclose on that security interest at the first sign of financial distress). Similarly, a firm commitment to public benefit could shrink the pool of potential investors. Lenders who seek repayment at all costs would avoid the benefit corporation, and it would attract only socially conscious lenders.

But whether such a firm commitment would actually raise the cost of capital (and by how much) is impossible to say without empirical data on social enterprises. A 2015 study on the effects of constituency statutes on investment behavior found no meaningful change, expressly suggesting that its results might have applications to "alternative purpose firms" like the benefit corporation. After all, lenders, sometimes called impact investors, do lend money to nonprofit corporations and social enterprises. And arguably, the distinctiveness of a benefit corporation may be an asset for raising funds, both from equity investors and from lenders. A benefit corporation's legal form may serve as a kind of signaling. While a firm commitment to

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155 See Christopher Geczy et al., Institutional Investing When Shareholders Are Not Supreme, 5 HARV. BUS. L. REV. 73, 116 (2015). Attorney Kyle Westaway, whose practice focuses on advising social entrepreneurs, points out that even if interest rates are not higher for social enterprises, the process of borrowing money for nonprofits and social enterprises may simply take more time. KYLE WESTAWAY, PROFIT & PURPOSE 77 (2014) ("Many of the executive directors I speak with regularly spend 40 percent or more of their time in any given week fundraising . . . Time is the key cost of philanthropic capital."). Despite the lack of empirical studies, some commentators have at least discussed the practical concerns between lenders and nonprofit borrowers. See, e.g., Rick Hyman & Christine Walsh, Considerations When Lending to a Not-For-Profit Entity, NEW YORK LAW JOURNAL, https://plus.lexis.com/api/permalink/533e9263-03ec-42c4-8fa1-3a1f66c5e665/?context=1530671 (June 22, 2015) (highlighting concerns for lenders in the nonprofit space); Woods Bowman, The Price of Nonprofit Debt, NONPROFIT Q. (Aug. 6, 2015), https://nonprofitquarterly.org/the-price-of-nonprofit-debt/ (providing overview of strategies nonprofit entities use for financing). Other commentators focus on risks to a public benefit corporation's stated public benefit. See, e.g., BRAKMAN REISER & DEAN, supra note 16, at 797–99 (discussing tension between traditional financing mechanisms and social mission).


Of course, if investors took the benefit corporation's form into account at the point of lending and baked it into the interest rate or some other feature of the loan agreement, then it would be a windfall to the lender if the benefit corporation did not pursue its mission into financial distress.

157 See Michael Spence, Job Market Signaling, 87 Q.J. OF ECON. 355 (1973). According to Spence, manipulable signals, like a college degree or a certification, can bring a benefit but also come with signaling
BANKRUPTCY & THE BENEFIT CORP.

public benefit could shrink the pool of potential investors, it is not clear that it would, and it's equally uncertain whether such a reduction in potential investors would come with a higher cost of capital.

3. Takeover risk

Equity investors who do not place the same value on general and specific public benefit may also have an incentive to try to take over the company. While the benefit corporation legislation makes it difficult to strip the corporation of its benefit corporation status, a change in control could be enough to refocus the corporation on short-term or long-term monetary gain. The risk of takeover is heightened during periods of financial distress, since the value of the company is low and creditors could leverage the debt owed to them into an ownership stake, whether through an out-of-court negotiation or through a formal bankruptcy case.

As above, absent empirical data, it is difficult to know whether a firm commitment to public benefit would make a company more or less susceptible to takeover. To be sure, a commitment to public benefit that inures to the detriment of creditors might make them more likely to attempt to take over the company. At the same time, many of the creditors of a benefit corporation may have lent in support of its mission. Furthermore, lenders might believe that the going-concern value of the benefit corporation is ineluctably tied to its mission. Unless the company is in liquidation proceedings, even creditors that prioritize monetary benefit might hesitate to adjust the benefit corporation's mission and vision as a formal matter — even in times of financial distress.

The inconclusive nature of the empirical data available make it challenging to rely on a utility-based approach. And unfortunately, good data may never become available. As benefit corporations continue to rise and fall, courts will be asked to resolve the questions posed by this Article. As while empiricists rely on variety and control groups, courts look to precedent and authority. Courts will likely try to resolve these questions in a consistent way, as a matter of corporate law. Unless benefit corporations set out a variety of approaches in their articles of incorporation (and unless courts give

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\[\text{Dana Brakman Reiser \& Steven A. Dean, The Social Enterprise Life Cycle, in The Cambridge Handbook of Social Enterprise Law, supra note 63, at 225.}\]
effect to that a la carte approach), we may never have data sets from the field that can provide conclusive answers.

C. CHARACTER-BASED APPROACHES

As I have just articulated, duty-based and consequence-based approaches have fundamental limitations. Here, I propose a third theoretical approach originally stemming from family law scholarship.160 That approach looks at benefit corporations through the lens of channelling — law’s promotion of stable ways of being in the world. While it may seem strange to use the language of character in the corporate context, a corporation is in real-world terms a joint endeavor of individuals striving to undertake some mission together. Those individuals collectively generate shared values and a shared culture.

1. The channelling function of law

In a seminal law review article, Schneider laid out five functions of family law and focused on one that he saw as “less self-evident,” the “channelling” function of law.161 For Schneider, law not only establishes duties and liabilities, not only promulgates incentives for desirable behavior and disincentives for undesirable behavior; it also channels human activity into a manageable number of forms, so that actors in the world can understand who or what they are dealing with. The channelling function of law thus arises where “law creates or (more often) supports social institutions which are thought to serve desirable ends.”162 According to Schneider, law “recruits” social institutions, “mold[s] and sustain[s] them,” and channels people into them through “recognition and endorsement,” “rewarding participation,” “disfavoring competing institutions,” and “directing penalizing the non-use of the institution.”163 Identifying a manageable number of institutional forms to serve as

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160The basic insight has not been lost on commentators analyzing the benefit corporation. See generally MARQUIS, supra note 2 (outlining impetus for the creation of public benefit corporation).


The same kind of concept has been discussed at length in a seminal law review article by Professors Thomas W. Merrill and Henry E. Smith, who point out that — unlike contract law, which allows for a dizzying array of private arrangements — "property rights exist in a fixed number of forms." Thomas W. Merrill & Henry E. Smith, Optimal Standardization in the Law of Property: The Numerus Clausus Principle, 110 Yale L.J. 1, 3 (2000). Merrill and Smith make a structurally similar argument to the one that I advance here: for a variety of reasons, having an optimally sized "menu" of choices is efficient and makes good sense, though Merrill and Smith advance their argument through the lexicon of consequences, see id. at 26-42, rather than seeing such an argument (as I do) as a third kind of approach.

162Schneider, supra note 161, at 498.

163Id. at 503-04. A similar phenomenon is described by Professor Robert C. Clark, Moral Systems in the Regulations of Nonprofits: How Value Commitments Matter, HAUSER INS. WORKING PAPERS (2006),
templates can be efficient and can promote integration by uniting people under common institutions. Too few forms would not adequately capture the need for human conduct and expression; too many would make the world unduly complex.

How does the channelling theory of law apply to benefit corporations? To start, the benefit corporation legislation establishes one additional form of corporation, adding to preexisting forms like the business corporation and the nonprofit corporation. To be sure, some commentators have argued that the establishment of the benefit corporation would unduly confuse corporate law. On the one hand, a corporate form already exists for those who wish to pursue public benefit: the nonprofit corporation. On the other hand, business corporations can pursue public benefit alongside their pursuit of shareholder value, and some commentators have expressed concern that the establishment of the benefit corporation would — by contrast — suggest to the directors of officers and directors of business corporations that they no longer needed to do so.

What did not exist, however, was a fully-fledged option for those who wish to seek profit and public benefit in conjunction, like Big Idea and Ben & Jerry’s. Along with similarly motivated innovations like the L3C and permissive constituency statutes, the benefit corporation provides a new and distinct form for profitability with social purpose.


Schneider, supra note 161, at 505.

Id. at 511.

See, e.g., Kevin V. Tu, Socially Conscious Corporations and Shareholder Profit, 84 GEO. WASH. L. REV. 121, 167-71 (2016). In a similar vein, one might argue that bankruptcy itself is a form of channeling, one where insolvent companies are “channeled” into a specialized forum that focuses on the repayment of creditors in an orderly fashion. Understood in that way, the form of the debtor and the form of the court clash — and the conceptual challenge is determining which form of channeling takes priority over the other.


For a thorough discussion of what he calls the “corrosion critique,” see Brett McDonnell, The Corrosion Critique of Benefit Corporations, 101 B.U. L. REV. 1421 (2021); see also Fershee, supra note 167, at 388-90 (arguing public benefit corporation legislation unfairly usurps director authority to pursue social good in a traditional business corporation). To alleviate this concern, the Model Legislation specifies that the existence of the legislation “shall not of itself create an implication that a contrary or different rule of law is applicable to a business corporation that is not a benefit corporation.” Model Legislation § 101(b). To be fair, though, even if that provision would provide meaningful guidance to lawyers and judges engaged in litigation over the duties of a business corporation, it may have less of a mitigating effect on the directors of business (non-benefit) corporations — who may still reason that the existence of the option for a benefit corporation suggests that they should focus more intently on shareholder value and profit motive.
This point is paramount for understanding value. Take the example of Big Idea. Classic Media was unable to monetize VeggieTales effectively, as were subsequent new owners. A secular version of the VeggieTales series was widely criticized by faith groups.\textsuperscript{169} Eventually the brand was licensed to a Christian network that brought on Phil Vischer to consult on a new VeggieTales series that would be more faithful to the original.\textsuperscript{170} A similar story happened with Ben & Jerry’s. Recognizing the importance of the mission and the charisma of the founders, Unilever forged an explicit agreement with Ben & Jerry’s that preserved its independence and allowed it to keep its B Corp status, even though it is not formally incorporated as a benefit corporation.\textsuperscript{171}

Retaining the distinctiveness of the benefit corporation is crucial, according to a channelling theory of law. And while the lexica of duty and consequences tend to focus on specific decision-making moments, the channelling function of law invites us to consider the ways in which the unique nature of the form is molded over time, shapes the community around it, and constitutes a valuable end in and of itself.\textsuperscript{172} Akin to the enterprise model of the corporation, the channelling theory of the corporation appreciates not only the commitments made by entrepreneurs and shareholders, but also the commitments made by employees, business partners, lenders, and the community.\textsuperscript{173}

2. Persistent values and generally applicable rules

For the same reason, the channelling function of law would suggest that the distinctiveness of the benefit corporation should not be abandoned during times of financial distress. Denying creditor primacy in insolvency would make the benefit corporation more distinctive, not less so. It would tend to


\textsuperscript{171}See supra note 18 (discussing Ben & Jerry’s unique arrangement within Unilever); EDMONDS, supra note 15, at 156 (noting that Unilever management realized that the value of their target would be “greatly reduced if [they] could not gain the support of its charismatic cofounders”).

\textsuperscript{172}In this way, the channelling function of law is also akin to virtue ethics, which focuses on the development of ethical character, a tradition of moral philosophy traced back to such luminaries as Aristotle and Jesus.

\textsuperscript{173}Ryan Honeyman and Tiffany Jana describe some of the benefits of incorporating as a benefit corporation as becoming part of “a global community of leaders,” and “attracting talent and engaging employees.” HONEYMAN & JANA, supra note 94, at 39–40, 46–47. The distinctiveness of the corporate form is perhaps most important to employees, who typically dedicate an overwhelming percentage of their waking hours to the purposes of the corporation and whose commitment to its values and character should not therefore be underestimated. See, e.g., HARMER & HERING, supra note 21, at 15–20 (describing Millennials as the most “cause-driven generation in history”).
make creditors to a benefit corporation more conscientious of the identity of their business partner. By contrast, allowing creditor primacy would make the distinctiveness of the benefit corporation vanish once it goes into financial distress.

Duty-based and utility-based approaches do not provide conclusive answers, but they can set forth helpful frameworks (for entrepreneurs, investors, partners, or judges) for thinking about the issues. By contrast, a character- or virtue-based approach provides at least a strong answer in favor of the benefit corporation’s distinctiveness persisting into times of financial distress. Since legislatures have already decided that an additional corporate form is desirable as part of the suite of options available to individuals seeking to launch an enterprise, the distinctive features of that form should persist into financial distress. In this respect, the choice to incorporate or re-incorporate as a benefit corporation is analogous to the choice to incorporate as a nonprofit corporation: it establishes the character of the business enterprise — for life.

At the same time, none of these approaches suggests that the innovation of the benefit corporation should override otherwise applicable creditor-debtor or bankruptcy law. While the normative arguments are not conclusive, I argue that they counsel in favor of a multi-layered approach: persistent values subject to generally applicable law. The innovations of the benefit corporation are innovations in the corporate governance of the benefit corporation, not adjustments to the more fundamental laws of insolvency and bankruptcy. A benefit corporation experiencing financial distress is still at risk of the creditor actions described in Section III and, if it files for bankruptcy, it must still navigate the reticulated net of rules and standards that apply in bankruptcy court. The corporate governance legislation does not automatically override all other generally applicable rules. None of the approaches discussed above counsel in favor of giving benefit corporations a free pass from generally applicable law.

One advantage to this conclusion is that it does not require further legislation. The results come from the straightforward application of corporate governance law, read alongside the rules and procedures of the Bankruptcy Code. The hybrid approach proposed here seems adequately to capture the balancing act created by state legislatures that enacted the benefit corporation legislation in the first place.174

174 Some commentators think that the benefit enforcement proceeding is too weak an enforcement mechanism and suggest that the legislation be amended to allow the attorney general of the state of incorporation to bring such a proceeding. See Brakman Reiser, supra note 142, at 240-45 (discussing a possible role of state attorneys general in enforcing the pursuit of public benefit for a number of different forms of social enterprise, including the public benefit corporation); see also Michael A. Hacker, “Profit, People, Planet” Perverted: Holding Benefit Corporations Accountable to Intended Beneficiaries, 57 B.C. L.
III. PITFALLS OF INSOLVENCY AND BANKRUPTCY

As foreshadowed in Section II, even if the benefit corporation’s innovation to fiduciary duties should persist into insolvency, benefit corporations in financial distress face other pitfalls that are not altered by the benefit corporation legislation. This Section maps out some of those pitfalls in the contexts of insolvency and bankruptcy.

A. INSOLVENCY

Both fiduciary duty and liability take on a new dimension when a corporation is insolvent. As an initial matter, an insolvent corporation may default under its debt facilities, which gives both secured and unsecured creditors significant control over the company’s future. That is particularly true of secured creditors, who have access to state remedies like foreclosure and forced sales. In addition to that, the residual ownership interest of the shareholders approaches zero and creditors become the beneficial owners of the company.

1. Creditors as enforcers of fiduciary duty

When a corporation becomes insolvent, the nature of the fiduciary duty owed by the corporation (and its directors and officers) changes. Economically, the shareholders’ ownership stake has zeroed out, and the creditors now have the most to gain from any increase in the value of the corporation, and the most to lose from any decrease.

Courts recognize this reality in one of two ways. Under the “trust fund”

Rev. 1747, 1772-79 (arguing that existing powers of state attorneys generals with regard to the oversight of charitable institutions could be extended to public benefit corporations). Such a proposal would bring benefit corporations a step closer to nonprofit corporations, where the state attorneys general are responsible for enforcing the charitable mission. This step could help but may be unnecessary. The shareholders already have the ability and incentive to enforce the benefit mandate and if further loosening is needed, state legislatures could simply lower the threshold of stock ownership for doing so.

The law sets forth three prevailing definitions of “insolvent” for purposes of this analysis: First, balance-sheet insolvency is when the corporation’s liabilities outweigh its assets, a snapshot of the corporation’s financial picture at a single moment in time. See, e.g., 11 U.S.C. § 548(a)(1)(B)(ii)(I). Second, cash-flow insolvency is when a corporation does not have sufficient liquidity to pay its debts as they come due. See, e.g., id. § 548(a)(1)(B)(ii)(III). Third, capital insolvency is when a corporation does not have reasonably sufficient capital to engage in its ongoing business. See, e.g., id. § 548(a)(1)(B)(ii)(II). Insolvency under any one of the three is sufficient for a company to be deemed insolvent.

Indeed, if the directors and officers continued to prioritize the best interests of shareholders, it could cause the corporation to engage in risky behavior in the hopes of climbing out of insolvency. At the same time, courts have split over whether claims against the board for “deepening insolvency” are cognizable. Compare In re Troll Commc’ns, LLC, 385 B.R. 110, 122 (Bankr. D. Del. 2008) (“[D]eepening insolvency has been rejected as a valid cause of action or a theory of damages under Delaware law.”), with In re Eugenia VI Venture Holdings, Ltd. Litig., 649 F. Supp. 2d 105, 125 (S.D.N.Y. 2008), aff’d sub nom. Eugenia VI Venture Holdings, Ltd. v. Glaser, 370 F. App’x 197 (2d Cir. 2010) (“New York courts have recognized ‘deepening insolvency’ as a theory of damages that may result from the commission of a separate tort.”).
doctrine, the corporation owes fiduciary duties to creditors, who may enforce them directly. By contrast, under the Delaware Supreme Court case of North American Catholic Educational Programming Foundation, Inc. v. Gheewalla, creditors are not owed fiduciary duties directly, but they gain derivative standing to sue for breach of fiduciary duty, as the parties-in-interest with the best economic stake in enforcing them.

Either way, the content of the directors' and officers' fiduciary duties remains the same: the duty of loyalty and the duty of care. The only difference is to whom the duty is owed, or who may enforce it. The circumstances calling for enhanced scrutiny under Unocal or Revlon may coincide with financial distress, but financial distress by itself does not alter the tripartite framework under which board decisions will be reviewed.

What this shift means practically for a struggling company like Big Idea is that the board will have the creditors' interests in mind — a big part of why the board felt compelled to hand the company over to the bidder preferred by Big Idea's biggest creditor. As will be seen in Section IV, this dynamic is complicated in the case of a benefit corporation.

2. Avoidance actions and involuntary bankruptcy

But even apart from fiduciary duty, insolvency also presents a heightened risk of liability. The corporation (whether it is a benefit corporation or not) may now face causes of action that tend to accompany financial distress, but also certain creditor causes of action that become available only when a corporation is insolvent. State legislatures amended none of these rules for benefit corporations.

First, the corporation is at risk of creditor actions. Due to its insolvency, the corporation is at a heightened risk of triggering defaults under its credit agreements or otherwise failing to meet its obligations. Such defaults can be particularly perilous when the corporation has granted a security interest in its property, because the secured creditor can commence execution actions, such as foreclosure or a forced sale.

Second, the corporation becomes susceptible to two different types of "avoidance actions" under state or bankruptcy law. The first avoidance action is a fraudulent transfer or fraudulent conveyance, where a debtor intends

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177 See, e.g., N.Y. Credit Men's Adjustment Bureau, Inc. v. Weiss, 110 N.E.2d 397, 398 (N.Y. 1953) ("If the corporation was insolvent at that time it is clear that defendants, as officers and directors thereof, were to be considered as though trustees of the property for the corporate creditor-beneficiaries.").

178 930 A.2d 92 (Del. 2007).

179 Id. at 101 ("When a corporation is insolvent... its creditors take the place of the shareholders as the residual beneficiaries of any increase in value. Consequently, the creditors of an insolvent corporation have standing to maintain derivative claims against directors on behalf of the corporation for breaches of fiduciary duties.").

180 See, e.g., U.C.C. § 9-601.
to "hinder, delay, or defraud" its creditors by transferring property away for less than reasonably equivalent value.\textsuperscript{181} The policy behind fraudulent transfer litigation is that an insolvent debtor should not be permitted to spin off its assets — whether intentionally or not — at a sharply reduced price.\textsuperscript{182} The second avoidance action is a preference, where the debtor pays one creditor more than that creditor's pro rata share among the pool of similarly situated creditors.\textsuperscript{183} The policy behind preference litigation is that an insolvent debtor, who cannot pay all its debts in full, should pay all similarly situated creditors a pro rata share of their debts, instead of preferring one to another.\textsuperscript{184}

Finally, the corporation is at risk of an involuntary bankruptcy filing. Section 303 of the Bankruptcy Code allows certain creditors or a qualifying group of creditors to band together and place a corporation into bankruptcy.\textsuperscript{185}

B. Bankruptcy

Just as state legislatures left creditor-debtor law untouched when forming the benefit corporation, Congress also left the Bankruptcy Code untouched. But the landscape of fiduciary duty and liability changes dramatically upon the filing of a petition in bankruptcy, whether voluntary or involuntary.\textsuperscript{186}


\textsuperscript{182}See generally Jack F. Williams, Revisiting the Proper Limits of Fraudulent Transfer Law, 8 BANKR. DEv. J. 55 (1995) (discussing common law history of and policy rationales behind prohibitions on fraudulent transfers).

\textsuperscript{183}See 11 U.S.C. § 547.


\textsuperscript{185}11 U.S.C. § 303(b). To do so, those creditors must be owed, in the aggregate, a certain amount more than the value of any security interest on the debtor's property. The petitioning creditors must also hold claims that are not "contingent as to liability or the subject of a bona fide dispute as to liability or amount." Id. § 303(b)(1). Where there is such a bona fide dispute, the petitioning creditors should reach a final adjudication under state law prior to commencing an involuntary bankruptcy case. Because secured creditors are paid first in any bankruptcy case, this rule ensures that the petitioning creditors actually stand to gain something from commencing a bankruptcy case. And because secured creditors have special enforcement remedies under state law, as described above, they have no need for a special entrance to the Bankruptcy Code. To the contrary, it is precisely when secured creditors begin seizing collateral under state law that the policies of the Bankruptcy Code spring into effect, and the unsecured creditors — concerned about their ability to recover value from the company if it is sold for scraps — should commence an involuntary bankruptcy case, assuming that the debtor does not do so voluntarily first. An involuntary bankruptcy case may not be commenced against "a farmer, family farmer, or a corporation that is not a moneyed, business, or commercial corporation." Id. § 303(a).

\textsuperscript{186}Contrary to the public imagination, bankruptcy is not the state of being insolvent: it is a formal court case that proceeds under standards and rules set forth the Judicial Code, the Bankruptcy Code and the Federal Rules of Bankruptcy Procedure. A bankruptcy case is commenced by the filing of a petition in
1. Fiduciary duties of the debtor in bankruptcy

The filing of a petition in bankruptcy creates an estate, managed by a trustee, though in most cases the bankruptcy court will allow the debtor’s management to continue to run the company as the “debtor-in-possession.” Under 28 U.S.C. § 959, the debtor is required to “manage and operate” the estate according to state law. The Supreme Court has held that the debtor has a duty to maximize the value of the estate, but has never sketched out that duty with much precision. What does it mean to maximize the “value” of the estate in a chapter 11 case? What kind of value did the Supreme Court have in mind? Or, put differently, value in whose eyes: secured creditors, unsecured creditors, other stakeholders? These questions take on particular importance for companies — like nonprofits and benefit corporations — who have a distinct approach to their understanding of value, and they introduce an unwelcome uncertainty for a social enterprise facing financial distress.

2. Creditors and committees

The fiduciary duty of the debtor is not the only source of uncertainty in bankruptcy: a bankruptcy case is a collaborative process that involves not only the debtor and the court, but also the U.S. Trustee, secured creditors, unsecured creditors, and other parties-in-interest. These other entities can disrupt the debtor’s blueprint for how the case might proceed: whether by

bankruptcy. 11 U.S.C. § 301(a). The filing of a petition in bankruptcy creates an estate, comprised of all the property of the debtor. Id. § 541(a). The bankruptcy trustee is the representative of the estate, id. § 323(a); see also 28 U.S.C. § 959, and in a chapter 11 case may operate the business unless the court orders otherwise, 11 U.S.C. § 1108. In a typical chapter 11 reorganization case, the management of the company serves as the “debtor-in-possession.”

For purposes of this Article, I will refer to both a chapter 11 trustee and a debtor-in-possession as the “debtor,” but as a formal doctrinal matter, the debtor-in-possession is wearing the hat of the bankruptcy trustee.

Commodity Futures Trading Comm’n v. Weintraub, 471 U.S. 343 (1985); see also Ostrow, supra note 23, at 88–89 (explaining the judicial creation of the doctrine of value maximization in a chapter 11 reorganization). Bankruptcy courts have applied this principle to resist the suggestion that state law could do away with the fiduciary obligation of the bankruptcy trustee in its entirety. See In re Houston Reg’l Sports Network, L.P., 505 B.R. 468, 481–82 (Bankr. S.D. Tex. 2014).

The duties of the trustee in a chapter 7 liquidation seem clearer. In a chapter 7 liquidation, the trustee has a duty to “collect and reduce to money the property of the estate for which such trustee serves, and close such estate as expeditiously as is compatible with the best interests of parties in interest.” 11 U.S.C. § 704. Those duties are noticeably absent from the duties of the trustee or debtor in bankruptcy under a chapter 11 reorganization. See id. §§ 1106, 1107(a) (outlining duties of trustees and debtors-in-possession).

See Schildhorn & Keilson, supra note 23, at 59.

The U.S. Trustee’s Office, which monitors bankruptcy cases across the United States, appoints a committee of unsecured creditors. 11 U.S.C. § 1102. That committee serves as the voice for unsecured creditors throughout the case. The U.S. Trustee’s Office can also appoint an equity committee. The Bankruptcy Administrator performs functions similar to the U.S. Trustee in bankruptcy cases filed in Alabama and North Carolina.
forcing the debtor to stick to its commitment to public benefit, or by forcing
the debtor to abandon it.

Most importantly, secured creditors' interest in the collateral of the
debtor is protected in bankruptcy, such that a debtor whose assets are
pledged will find it difficult to use those assets to advance the bankruptcy
case without the consent of the secured creditor.192

As another example, debtors have the exclusive right to propose a plan
for the first 120 days of the bankruptcy case.193 But where a debtor is unable
to sell the company or restructure its debt within that time period, it may
lose the exclusive right to propose a plan, opening the floodgates to plans put
forward by other constituencies.194 And while a benefit corporation has a
statutory duty to consider general and specific public benefit, creditors who
propose a plan do not have the same fiduciary duty and might propose a plan
that does not take public benefit into account at all.195

Similarly, a debtor can lose control of a chapter 11 case when creditors
start to believe that a liquidation would better protect their interests than a
chapter 11 reorganization. Creditors can move the court to convert the case
when they can show "cause" for doing so, which includes "substantial or con-
tinuing loss to or diminution of the estate and the absence of a reasonable
likelihood of rehabilitation."196 In a chapter 7 case, a new trustee is ap-
pointed (not the debtor-in-possession), and the chapter 7 trustee has a more
strictly defined mandate to "reduce to money the property of the estate," a
mandate that the trustee (or a reviewing court) might be more likely to inter-
pret as overriding the mandate to consider public benefit.197

A benefit corporation that enters chapter 11 proceedings without a strat-
egy for the bankruptcy risks losing control of the case, and with it the future
of the company.

3. The watchful eye of the bankruptcy court

Against this backdrop, voluntary debtors in bankruptcy typically (though
not always) file their bankruptcy cases with a plan in mind for the trajectory
of the case. In a chapter 11 reorganization, debtors are usually aiming toward
either an asset sale of the company or a confirmed plan of reorganization.

Asset sales in bankruptcy can take place either under § 363 or as part of

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192 A debtor-in-possession cannot even use cash collateral in the ordinary course of business without
either the consent of the secured creditor or the court's permission. See 11 U.S.C. § 363(c)(2).
193 Id. § 1121. Courts frequently extend this period in complex chapter 11 cases.
194 Id. § 1121(b)-(c). To be sure, the court may extend these periods of time (within limits). See id.
§ 1121(d).
195 See Brown, supra note 25, at 71 & n.228.
197 See supra at note 189.
a plan of reorganization under § 1129.\textsuperscript{198} Big Idea, for example, knew that it needed to find a buyer for the company, and conducted the auction as an asset sale under § 363.\textsuperscript{199} An asset sale requires court approval,\textsuperscript{200} and if the debtor is a nonprofit corporation, the sale must comply with state law, which often requires approval from the attorney general.\textsuperscript{201} Where there is a lien on the debtor's assets (as in almost all cases), the debtor may only sell property free and clear of the lien if state law allows it and the secured creditor consents.\textsuperscript{202}

Plans of reorganization must be confirmed by the bankruptcy court under § 1129 of the Bankruptcy Code. Section 1129 contains several requirements, most importantly that a plan must (a) respect absolute priority among creditors, especially by giving secured creditors the value of the collateral securing their debt; and (b) otherwise treat equally situated creditors equally.\textsuperscript{203}

In comparison to a company operating outside of bankruptcy, a debtor operating within bankruptcy must continue its business under the watchful eye of the bankruptcy court. The company may continue in the ordinary course of business without court authorization,\textsuperscript{204} but virtually every decision outside the ordinary course of business will require bankruptcy court authorization and approval.\textsuperscript{205}

Other decisions require the blessing of the bankruptcy court and have ad hoc standards, generally a little higher than outside bankruptcy, something like a "good business reason."\textsuperscript{206} Bankruptcy courts are less deferential to debtors than a reviewing court would be outside bankruptcy, but these standards do provide some leeway for a debtor to manage the company in line with its business judgment. As discussed further in Section IV, directors

\textsuperscript{199}See supra notes 10–12 and accompanying text.
\textsuperscript{200}11 U.S.C. § 363(b)(1).
\textsuperscript{201}Id. § 363(d)(1).
\textsuperscript{202}See id. § 363(f).
\textsuperscript{203}Id. § 1129. Among other things, a chapter 11 plan must be preferable to a liquidation, i.e., provide more value to holders of claims or equity interests than they would receive in a chapter 7 liquidation. See id. § 1129(a)(7)(A)(i)–(ii). If the plan "impairs" any class of creditors, i.e., gives them anything less than what they would be entitled to under nonbankruptcy law, at least one impaired class must accept the plan. Id. § 1129(a)(10). The plan must be proposed in good faith and not be likely to be followed by a liquidation or further reorganization (unless the plan proposes a follow-up liquidation or reorganization). Id. § 1129(a)(3), (a)(11). Where a class of claims or interests is impaired and has not accepted the plan, the court may still confirm the plan if the proponent of the plan meets the "cramdown" requirements of § 1129, which include that the plan provides equal treatment to all members of the same class and respects absolute priority across classes. See id. § 1129(b)(1)–(2).
\textsuperscript{204}Id. § 363(c)(1).
\textsuperscript{205}See, e.g., id. § 363.
\textsuperscript{206}See, e.g., Isley M. Gostin, Craig Goldblatt & George W. Shuster, Jr., WILMERHALE, Insolvency at Its Limits: What Management and Creditors of Insolvent LLCs and LPs Should Know About Fiduciary Duties Waivers and Standing, Inside and Outside of Bankruptcy, at p. 3 (June 8, 2017).
who wish to run the company in a socially responsible way may have some additional discretion under this standard. When a debtor is incorporated as a nonprofit or as a benefit corporation, a reviewing court may be more likely to authorize decisions that are consistent with the nonprofit's mission or the benefit corporation's consideration of public benefit — even over creditor objections.

From the foregoing discussion, one can see that the benefit corporation's innovations to fiduciary duty are but a small piece of the puzzle. Creditor actions, avoidance actions, involuntary bankruptcies, and the reticulated provisions of the Bankruptcy Code all operate in full force on benefit corporations, just as they do on business corporations. But this multi-layered approach, I argue, strikes just the right balance.

IV. CHARTING A PATH FORWARD

While Section III laid out a number of the pitfalls facing an insolvent benefit corporation, this Section tries to provide a path forward through the course of creditor-debtor litigation and formal bankruptcy proceedings, teasing apart fiduciary duty from other forms of liability. To do so, I draw from bedrock principles of procedure and federalism in bankruptcy law to argue that bankruptcy is a little less mysterious (and a little less inhospitable to benefit corporations) than some seem to think.

A. Benefit Corporation Status as a Shield

To start, imagine the board of a benefit corporation that seeks to stay the course and continue to emphasize general and specific public benefit in the face of financial distress and creditor pressure. The benefit corporation legislation alters the fiduciary duties of the board in a way that carries over into insolvency and bankruptcy. The board can use the statutory mandate to consider public benefit as a shield to protect its decision-making from certain forms of challenge.

207 See infra Section IV.A.

208 The bankruptcy court's supervision largely insulates the debtor from claims for breach of fiduciary duty for its management of the estate for the duration of the case. Debtors enjoy quasi-judicial immunity for full-disclosure decisions, except for the duty of loyalty. See Gostin et al., supra note 206, at p.3. In practice, where a bankruptcy case results in a confirmed plan in chapter 11, such plans commonly include formal releases of the directors and officers for their management of the debtor during the bankruptcy. To be sure, though, litigation over prepetition claims against the corporation and its officers and directors may well be preserved, and litigation over them can persist long after the action in the main bankruptcy case has died down.

209 Small business debtors proceeding under subchapter V have more control over the proceedings. Creditors' committees are not formed as a matter of course, 11 U.S.C. §§ 1102(3), 1181(b), only the debtor may file a plan, id. § 1189(a), and a plan is easier to confirm over creditor objection, id. § 1191(b).
1. In insolvency

First, as previously discussed, when a benefit corporation is insolvent, under Gheewalla and similar cases, creditors assume the position of shareholders. But the benefit corporation legislation requires the directors and officers to balance the interests of shareholders against general and specific public benefit. Therefore, just as a shareholder could not sue the board of a benefit corporation for not prioritizing her interests over all else during good times, a creditor may not do so during bad times. The liability shield prevents it.

The benefit corporation’s innovations to Unocal and Revlon should also persist into insolvency, consistent with legislative intent. In a hostile takeover situation, the board of a benefit corporation may resist the takeover consistent with its statutory requirement to consider general and specific public benefit. In a sale, which previously would operate under Revlon rules, the board of a benefit corporation is protected. Just as the board need not sell to the highest bidder under Revlon when the duty is focused on shareholders, so too here the board need not do so when the duty is focused on creditors.

At the same time, the benefit corporation’s innovations in the law of corporate governance do not alter the more fundamental law of liability that the corporation can incur as it moves into financial distress. As discussed above in Section III, an insolvent corporation remains at risk of creditor actions. Similarly, unpaid creditors of a benefit corporation could commence an involuntary bankruptcy against it if they met the statutory requirements, or creditor remedies under state law, such as foreclosure.

2. In bankruptcy

Second, the statutory mandate and liability shield should persist into formal bankruptcy proceedings, not only as a matter of normative argument, as seen in Section II, but also as a matter of positive law. This result finds deep theoretical support in the foundational bankruptcy principle of Butner, which counsels that bankruptcy courts should apply state law unless there is a clear federal (bankruptcy) interest to the contrary. Bankruptcy courts, like fed-

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2022) BANKRUPTCY & THE BENEFIT CORP. 135

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210 See supra note 179 and accompanying text.

211 See supra notes 130–131 and accompanying text (describing how the benefit corporation statute deems the standards of Unocal and Revlon to have been met).

212 See supra Section III.A.2.

213 As the Supreme Court explained in Butner, “[p]roperty interests are created and defined by state law” and “[u]nless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding.” Butner v. United States, 440 U.S. 48, 55 (1979); see also In re Central Ice Cream Co., 836 F.2d 1068, 1072 (7th Cir. 1987) (“The bankruptcy court should try to implement, rather than alter, non-bankruptcy entitlements.”); THOMAS H. JACKSON, THE LOGIC AND LIMITS OF BANKRUPTCY LAW 7–67 (1986).
eral courts generally, strive to avoid finding that the federal law preempts state law. No federal statute or interest (of which I am aware) is strong enough to override the state benefit corporation legislation.

Indeed, § 959(b) of the Judicial Code requires the debtor to “manage and operate the property” of the estate “according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof.” This statute makes the statutory mandate of the benefit corporation legislation applicable to benefit corporations in bankruptcy. While courts have not yet ruled on this specific issue, at least one court has held that § 959(b) requires a receiver to act in accordance with state law governing fiduciary duty.

To be sure, the Supreme Court suggested in Commodity Futures Trading Commission v. Weintraub that the debtor’s duty to maximize the value of the estate is governed by federal common law. But that is not inconsistent with the benefit corporation’s distinct twist on value. Moreover, federal common law looks to state law for its content, and absent any strong federal policy should adopt the emerging consensus on the duties of the board of benefit corporations.

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21528 U.S.C. § 959(b). Section 959(a) authorizes suit of trustees in bankruptcy court with respect to “acts or transactions in carrying on business connected with such property.” Id. § 959(a); see McNulta v. Lochridge, 141 U.S. 327 (1891) (noting that § 959(a) creates official liability only and therefore does not open trustees to suit in state court). Some courts have found that breach of fiduciary duty does not meet the requirements for a no-leave suit. See, e.g., In re McKenzie, 476 B.R. 515, 529 (E.D. Tenn. 2012), aff’d, 716 F.3d 404 (6th Cir. 2013). Nevertheless, a suit for breach of fiduciary duty that is “premised on an act or transaction of the fiduciary in carrying on the Debtors’ business operation” might qualify. In re Kashani, 190 B.R. 875, 884 (B.A.P. 9th Cir. 1995).

216Russell C. Silberglied, a prominent Delaware restructuring attorney, has also concluded that § 959(b) incorporates the benefit corporation legislation into the duties of the chapter 11 trustee. See Russell C. Silberglied, Can a Lower Bid for a Debtor’s Assets Be Approved as “Better” Because It Saves More Jobs than the Higher Bid?, 76 Bus. Law. 817, 837-38 (2021). Given the lack of caselaw on § 959(b), one could argue that the relatively mundane nature of the surrounding provisions suggests that Congress did not intend to hide such a meaningful provision in that section. 28 U.S.C. § 959. But § 959 is quite clear, and Congressional deference to state law on a matter that Congress did not elsewhere sketch out in detail is rather exceptional. Id. The legislative history of the provision is unilluminating; the text was amended once, in 1978, and only then to add a carve-out for railroad bankruptcies. See PL 95-598, 92 Stat. 2549.


219Congress “has repeatedly expressed its legislative determination that the trustee is not to have carte
If that is right, then a benefit corporation in bankruptcy is required to (and should) consider general and specific public benefit throughout the duration of the case, and perhaps especially at key junctures, such as settlements under Rule 9019, an asset sale under § 363, or plan confirmation under § 1129.

To be fair, fiduciary duties are typically not enforced directly in bankruptcy court: they are practically displaced by the ad hoc standards in bankruptcy, and usually released at the confirmation of a plan. As a formal matter, though, a debtor should be required to comply with its fiduciary duties and the ad hoc standards for whatever action it wishes to take.

At the same time, the benefit corporation’s innovations to fiduciary duty do not alter other rules expressly set forth in the Bankruptcy Code. Some of those rules set high protection for secured creditors and strict rules about the order in which creditors can be paid. For example, the court must “prohibit or condition” an asset sale under § 363 in order to protect any liens on the property, and the sale price must exceed the “aggregate value of all liens” on the property in order for the property to be sold “free and clear” of any blanche to ignore nonbankruptcy law.” Midatlantic Nat. Bank v. New Jersey Dep’t of Envt’l Prot., 474 U.S. 494, 502 (1986).

Rule 9019 of the Bankruptcy Rules allows the court to “approve a compromise or settlement” on motion and after notice and a hearing. The rule does not provide any further details on the standard for approving a settlement, but courts have read into the rule a general requirement that the settlement be “fair and equitable” and in the best interests of the estate. See, e.g., In re Lehman Bros. Holdings Inc., 435 B.R. 122 (S.D.N.Y.), aff’d sub nom. Suncal Communities I LLC v. Lehman Com. Paper, Inc., 402 F. App’x 634 (2d Cir. 2010).

The academic literature is split on the correct result here, and caselaw is absent so far. See Silberglie, supra note 216, at 834. That said, the language of 11 U.S.C. § 363 provides enough flexibility for a socially conscious trustee or debtor-in-possession to sell property only to other benefit corporations or non-profits. Correspondingly, state law requires the buyer of a non-profit to carry out its mission, and such requirements must be respected in a sale of a non-profit in bankruptcy. See Schildhorn & Keilson, supra note 23, at 59 (“[D]irectors of a nonprofit corporation had a fiduciary obligation to further the hospital’s healthcare mission and that the decision regarding the appropriate sale transaction should not be based solely on price.”) (citing In re United Healthcare Sys. Inc., No. CIV. A. 97-1159 (NHP), 1997 U.S. Dist. LEXIS 5090 (D.N.J. Mar. 26, 1997)).

A court might come out differently for a chapter 7 (liquidation) trustee. Unlike the chapter 11 trustee, the chapter 7 trustee has an express, statutory duty to “collect and reduce to money the property of the estate for which such trustee serves, and close such estate as expeditiously as it is compatible with the best interests of parties in interest.” 11 U.S.C. § 704(a)(1). Even if the chapter 7 trustee were inclined to pursue a socially conscious mission, courts might consider the express statutory provision to “reduce to money the property of the estate” to override the specific benefit corporation legislation and require the chapter 7 trustee to seek the highest monetary value of the property, without regard to general or specific public benefit. And, indeed, some courts have found that 28 U.S.C. § 959 does not apply to a chapter 7 trustee. A trustee under subchapter V performs some, but not all, of the § 704 duties and would provide an even more interesting study in statutory interpretation. See 11 U.S.C. § 1183(b).

This may be simply because the ad hoc standards are harder to meet than the basic fiduciary duties owed to corporations, and so litigants have not pressed the issue.

A benefit corporation in bankruptcy cannot evade those provisions by virtue of its corporate status.

B. BENEFIT CORPORATION STATUS AS A SWORD

Now flip the scenario around: imagine that the board of the benefit corporation, in the face of financial headwinds, begins to waver in its commitment to public benefit. The board plans to "sell out." Can shareholders or creditors use the benefit enforcement proceeding to hold its feet to the fire? Although courts have not yet adjudicated the issue, the answer should be yes. As above, that result is both normatively desirable (see Section II) but also, I argue, the correct result as a matter of positive law. The general rules applicable to derivative suits would suggest that creditors of the benefit corporation could obtain derivative standing to bring benefit enforcement proceedings once the corporation is insolvent.

The same principle holds true in bankruptcy. Bankruptcy courts apply similar standards for derivative standing when granting creditor constituencies standing to pursue claims belonging to the debtor in bankruptcy. Indeed, the United States Trustee's office, the statutory watchdog of the bankruptcy courts, must call for the appointment of an unsecured creditors' committee in a chapter 11 case, a committee that could lead the charge in a benefit enforcement proceeding. And in the bankruptcy of a benefit corporation, the U.S. Trustee might be particularly attuned to whether the benefit corporation is in financial distress. 

225 Id. § 363(f)(3).

226 Derivative lawsuits for breach of fiduciary duty, as in Gheewalla, see supra notes 177-179 and accompanying text, are among the most common kinds of derivative lawsuits, but as a formal matter, a shareholder could seek derivative standing to file a derivative lawsuit of any kind, if the board is not inclined to pursue it. See, e.g., Aronson v. Lewis, 473 A.2d 805, 809 (Del. 1984) (plaintiff sought derivative standing for non-fiduciary claims), overruled on other grounds by Brehm v. Eisner, 746 A.2d 244, 254 (Del. 2000). The policy behind derivative standing maps onto the benefit corporation neatly: insolvency "makes the creditors the principal constituency injured by any fiduciary breaches that diminish the firm's value." Prod. Res. Grp., L.L.C. v. NCT Grp., Inc., 863 A.2d 772, 794 n.67 (Del. Ch. 2004). Indeed, financial distress might widen the circle of individuals able to challenge the benefit corporation's focus on its mission: creditors of a distressed company are likely to include lenders, trade vendors, and employees. What remains unclear is how a court would apply the stock ownership thresholds to a creditor asserting derivative standing. See supra note 123.

227 See, e.g., Commodore Int'l Ltd. v. Gould (In re Commodore Intern. Ltd.), 262 F.3d 96, 100 (2d Cir. 2001) (holding that a "creditors' committee may acquire standing to pursue the debtor's claims if (1) the committee has the consent of the debtor in possession or trustee, and (2) the court finds that suit by the committee is (a) in the best interest of the bankruptcy estate, and (b) is 'necessary and beneficial' to the fair and efficient resolution of the bankruptcy proceedings") (quoting Liberty Mut. Ins. Co. v. Official Unsecured Creditors' Comm. of Spaulding Composites Co. (In re Spaulding Composites Co.), 207 B.R. 899, 904 (B.A.P. 9th Cir. 1997)); see also Off. Comm. of Unsecured Creditors of Cybergenics Corp. ex rel. Cybergenics Corp. v. Chinery, 330 F.3d 548, 568 (3d Cir. 2003).


229 11 U.S.C. § 1103 (laying out the powers and duties of committees appointed in chapter 11 cases).
corporation seemed inclined to give up on its mission — and bring it to the attention of the bankruptcy court. 230

Practically, however, a formal benefit enforcement proceeding is unlikely to force a debtor in bankruptcy to change course. As a reminder, the benefit enforcement proceeding is not monetary, but injunctive and forward-looking, unlike most derivative suits in bankruptcy. 231 The debtor’s going-forward plans, such as an asset sale under § 363 or plan confirmation under § 1129, will likely be governed by one of bankruptcy’s many ad hoc standards.

That said, the substantive requirement that the trustee or debtor-in-possession consider public benefit would likely carry over into bankruptcy via § 959 or even through bankruptcy’s ad hoc standards. 232 For example, where creditors could have brought a benefit enforcement proceeding to enjoin a sale, the bankruptcy court might hear the same arguments as part of the sale objection. 233 And § 1129 of the Bankruptcy Code requires that any chapter 11 plan be “proposed in good faith and not by any means forbidden by law.” 234

C. IMAGINING THE TRAJECTORY OF A CHAPTER 11 CASE

With these two sides of the coin in mind, we can make sense of the potential trajectory of a chapter 11 case of a benefit corporation.

1. Setting the pace: the benefit debtor

Given the thicket of statutory rules that apply to debtors in bankruptcy cases, it might seem that a socially conscious debtor would have limited discretion to carry out its mission. Yet the debtor does retain substantial control over the pace and purpose of a bankruptcy case. A benefit corporation in bankruptcy can therefore plot its trajectory along a route consistent with its mission and purpose. Indeed, the socially conscious debtor should expressly consider the statutory mandate of the benefit corporation when making key decisions throughout the course of the bankruptcy, as argued above.

The debtor generally retains control over the shape, location, and pace of the bankruptcy process. A benefit corporation in bankruptcy should ap-

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230 Under § 307, the bankruptcy court is required to hear the U.S. trustee “on any issue in any case or proceeding.” 11 U.S.C. § 307.

231 See supra Section I.D.3. It is this same, forward-looking feature that explains why a benefit enforcement proceeding brought in bankruptcy court would not violate the automatic stay; it would be a postpetition action to enforce the trustee’s fiduciary duty during the course of the bankruptcy itself, not an attempt to enforce a right that arose prior to the commencement of the case.

232 See supra Section III.B.3. Of course, the success or failure of such arguments turns on whether the bankruptcy court agrees that the trustee (or debtor-in-possession) must abide by the statutory mandate in the benefit corporation legislation.

233 As a threshold matter, the bankruptcy court must hear any “party in interest . . . on any issue in a case under this chapter.” 11 U.S.C. § 1109.

234 Id. § 1129(a)(3).
proach such decisions — such as where to file, how quickly to seek emergence or whether to convert the case to a chapter 7 liquidation — consistently with its statutory mandate to consider general and specific public benefit. Depending on the nature of the request, courts may be receptive to dramatic alterations in the general pace of a bankruptcy case.

2. Asset sales under § 363

Socially conscious debtors should anticipate challenges and try to seek court approval in advance. For example, imagine a debtor (like Big Idea) who plans to sell the company and wants to sell to a purchaser whose vision aligns with the benefit corporation’s purpose — but who may not have submitted the highest bid. Schildhorn and Keilson propose that the debtor build the considerations of the benefit corporation into its proposed bidding procedures and seek court approval for them in advance. Indeed, the debtor could argue that the obligation to consider public benefit has an ineluctable quality: much like a lien, a sale cannot simply cast that obligation aside. The bidding procedures would specify that so long as a bid for the property exceeds the aggregate value of all liens on the property, the debtor will consider the bidder’s proposed use of the property and whether it is consistent with the benefit corporation’s statutory duty to consider specific and general public benefit. In this way, bidders would be on notice of the debtor’s deliberative process, and the court can bless that procedure in advance of the auction process.

235 For example, at the onset of the COVID-19 crisis in the United States, courts in several major retail bankruptcy cases agreed to stay (or “mothball”) the cases for a limited time during lockdown or to partially freeze the cases, so that online sales could continue. See George W. Shuster, Jr., Paul Jakubowski, Benjamin W. Loveland and Christopher D. Hampson, How ‘Mothballed’ Ch. 11 Cases Will Affect Vendors, Landlords, Law360 (Apr. 16, 2020), https://www.law360.com/articles/1263480/how-mothballed-ch-11-cases-will-affect-vendors-landlords.

236 See Schildhorn & Keilson, supra note 23, at 86; see also Steve A. Peirce, Adding “Public Benefit” to the Bankruptcy Mix Raises Thorny Issues, Fed. Law., May/June 2014, at 10, 18 (agreeing with potential usefulness of sale procedures which include consideration of the public benefit).

237 Id. The debtor might also want to propose that the bid meet or exceed 75% of the fair market value of the property, a threshold identified by some courts as the minimum requirement for court approval of a bankruptcy sale as fair. See, e.g., In re WK Land Holdings, LLC, No. 13-11934, 2013 WL 6579172, at *1 (Bankr. D. Kan. 2013).

The notion that the debtor must select the highest bidder in a § 363 sale is flatly incorrect, and not only in this context. Antitrust law applies to § 363 sales, see 11 U.S.C. § 363(b)(2)(B), and one can readily imagine a monopolistic or anticompetitive purchaser offering the best dollar price. Yet, where the highest dollar-value offer would comprise a merger or acquisition that violates antitrust law, the bankruptcy court will not approve the sale — and the debtor may be required to accept a slightly lower offer from a different buyer. To be sure, while the purchase of a failing company does not violate antitrust law under the “failing firm defense,” that defense does not apply where the failing firm has received any offer above liquidation value — even if the offer is less than the offer of the proposed buyer. See U.S. DEPT. OF JUSTICE & FED. TRADE COMM’N, HORIZONTAL MERGER GUIDELINES § 11 & n.16 (Aug. 19, 2010), https://www.justice.gov/atr/horizontal-merger-guidelines-08192010#foot16.
In practical terms, however, the insight raised by Schildhorn and Keilson simply needs to be executed much sooner — before the bankruptcy case even begins. Many companies facing chapter 11 bankruptcy do not have enough unencumbered cash to fund an orderly chapter 11 case, and so must seek debtor-in-possession financing, commonly known as “DIP” financing. The most common source for DIP financing is the secured creditor, who may choose to protect its position by funding a bankruptcy case. In fact, this is what happened to Big Idea, who borrowed several million dollars from LaSalle Bank to fund its bankruptcy case. Where the plan for the bankruptcy involves a sale of the company, secured creditors may negotiate the terms of a sale order and bidding procedures with the debtor before the bankruptcy petition is even filed. And indeed, the benefit corporation legislation does not displace the protections granted to secured creditors and the substantial bargaining power that they enjoy as a result.

The board of a benefit corporation therefore needs to procure the approval not only of the bankruptcy court, but also of the DIP lender. While this may seem unlikely, the benefit corporation may credibly argue that it is required to consider public benefit during the bankruptcy, or risk challenges from activist creditors. Further, the secured creditor has less incentive to contest the consideration of public benefit if the sale or plan provides ade-

238 See In re Big Idea Prods., Inc., No. 03 B 35893, Dkt. 132, Agreed Final Order Authorizing Debtor-in-Possession to Obtain Post-Petition Financing, at 9–10.

239 In an insightful body of empirical research, Professor Pamela Foohey has observed that the leadership of churches who file for bankruptcy are often “pushed” to think about their financial troubles as legal problems by creditors. See Pamela Foohey, When Faith Falls Short: Bankruptcy Decisions of Churches, 76 OHIO ST. L.J. 1319, 1348–49 (2015). That said, negotiations over bankruptcy provisions are unlikely to be successful before default. Brown, for example, proposed that a borrower “negotiat[e] for stakeholder-friendly protections in its credit documents.” Brown, supra note 25, at 56 n.159. A benefit corporation could, for example, ask creditors to represent that they understand the nature of the borrower’s corporate purpose and state that the corporate purposes should not be contravened or altered even if profitable to do so or necessary to pay creditors. But designing such commitments to be enforceable presents two challenges: first, on the eve of bankruptcy, the borrower has likely defaulted under those credit documents (or is about to) and may therefore be unable to enforce its provisions; and second, the borrower will likely need additional cash to fund a bankruptcy case and therefore has limited bargaining power.

240 See BRAKMAN REISER & DEAN, supra note 16, at 239. In an insightful article, Professors David Skeel and George Triantis point out that contemporary bankruptcy practice routinely involves pre-bankruptcy agreements, such as intercreditor agreement, restructuring support agreements, and debtor-in-possession financing agreements — a phenomenon they call the “new contract paradigm.” David A. Skeel, Jr. & George Triantis, Bankruptcy’s Uneasy Shift for a Contract Paradigm, 166 U. PA. L. REV. 1777 (2018). This development alters the standard theory of bankruptcy developed by Thomas Jackson, along with Douglas Baird, of bankruptcy as reflecting the hypothetical bargain that creditors would strike if negotiation were possible. See id. at 1779–80; see also Thomas H. Jackson, Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors’ Bargain, 91 YALE L.J. 857, 858 (1982). For a thoughtful discussion of recent developments in chapter 11 practice, see David A. Skeel, Jr., Taking Stock of Chapter 11, 71 SYRACUSE L. REV. 531 (2021).

241 After all, a company with a lien on substantially all its assets would be subject to a forced sale under state law.
quate protection for the value of its liens. This kind of negotiation tactic may have changed the story of Big Idea, especially since Wet Cement's bid was more than sufficient to pay off LaSalle Bank.242

3. Reorganization plans under § 1129

Winning bankruptcy court approval for § 363 asset sales is much easier than confirming a plan of reorganization under § 1129. For this reason alone, benefit corporations who enter bankruptcy with the goal of selling the company should consider running a § 363 asset sale first and then — once the sale is approved by the bankruptcy court — filing a plan to dispose of the rest of the estate's assets.

But even under the requirements of § 1129, a benefit corporation in bankruptcy should not lose sight of the ways in which its unique structure could enable it to meet the reticulated requirements of the Bankruptcy Code. To be sure, benefit corporation status will not shift the bedrock principles of the absolute priority rule (senior creditors must be paid before junior creditors) and the requirement that plans be “fair and equitable” (like creditors must be treated alike).243 Similarly, a bankruptcy plan must meet the “best interests of creditors” test under § 1129(a)(7), which requires that each holder of an impaired claim or interest either accepts the plan or will receive at least as much value under the plan that it would under a chapter 7 liquidation.244

But confirming a plan is, in the first instance, a matter of garnering votes and building a coalition.245 If the benefit corporation seeks a plan rooted in its purpose and mission, and has truly built support among its stakeholders, many of whom will also be creditors, that process should be facilitated by the coalition-building work and credibility that the benefit corporation has already done.246

CONCLUSION

Corporate law contains various means by which a socially responsible organization can be formed and managed. The benefit corporation is just the latest innovation, yet perhaps one of the most important ones, because it creates a truly hybrid form. Despite that, as with many corporate law concepts, the true test of the idea will come during the hard times. That is the

242See supra note 11 and accompanying text.
244See id. § 1129(a)(7). Indeed, if the focus on public benefit in a chapter 11 reorganization does not result in go-forward value that outstrips what would be available in a liquidation, creditors may well press for conversion to chapter 7.
246Notably, benefit corporation status may help a debtor comply with the rule that if the plan impairs any class of creditors, at least one impaired class must accept the plan. See 11 U.S.C. § 1129(a)(10).
crucible that will reveal whether the existence of the benefit corporation can change the future for the next Ben & Jerry’s or the next Big Idea.

This Article has tried to provide a doctrinal roadmap, a path forward, and a theoretical underpinning to support the notion that the benefit corporation’s key innovations should persist into financial distress.

In the end, the purpose of the benefit corporate legislation was to invite into our world a new kind of entity, one that would be committed to socially beneficial purposes in the pursuit of profit. Fortunately, bankruptcy law, properly understood, does not undermine that basic commitment. Instead, bankruptcy principles should safeguard it in the moment of greatest need.