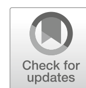
Social Enterprises, Benefit Corporations and Community Interest Companies: The UK Landscape



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1 Introduction

During the past two decades, the newspaper headlines and the media have been flooded by stories of corporate scandals and misdeeds, such as Enron, WorldCom, Tyco, Adelphia, Parmalat, Satyam Computer Services, Lehman Brothers, AIG, Massey, Olympus, and MF Global. The impact of these scandals on the stability and the reputation of the global financial markets was tremendously negative and has led governments and the business community to revisit the concept of the traditional corporation. In the context of the required transformation of the corporate purpose, reference was made to terms such as social enterprises,[1] social purpose, public

[1] The term 'social enterprise' refers to public benefit organisations that pursue the satisfaction of social needs through the imposition of at least a partial non-profit constraint and by devoting the majority of their positive residuals and patrimony to socially oriented activities. See Borzaga et al. (2009). In the United States, the term has a broader meaning and social enterprise are those using traditional business methods to accomplish charitable or socially beneficial objectives or companies with a significant mission-driven motive, regardless of whether profit is the primary objective. See

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interest and blended value.[2] As a result, both the United States and several European Union Member States have introduced special legal frameworks for social enterprises.

According to the European Commission, the social economy is dynamic and constantly growing. It employs more than 14.5 million people in the EU, corresponding to 6.5% of the active workforce.[3] The development of the social economy is not only seen in the EU but also globally, not least in the US, where there has been a wave of initiatives to promote social enterprises.[4] The solutions range from amendments to the existing company legislation through to certification schemes and to new corporate forms, such as benefit corporations, community interest corporations (CIC), limited liability companies (L3C), benefit limited liability companies (BLLC), flexible purpose corporations (FPC), social purpose corporations (SPC) and, lastly, the certified B corporations. All these initiatives reflect a fundamental change to the traditional business model implemented in both sides of the Atlantic Ocean and are all part of a movement towards greater transparency and commitment to pursuing social and environmental objectives in addition to profits.

The present chapter will focus on the social enterprises' landscape in the United Kingdom, with emphasis on certified B corps, benefit corporations and the CICs. Section 1 discusses the background to the introduction of special rules for social enterprises. This is followed by Section 2, where an overview of the benefit corporations and B corps will be provided using evidence for the United States and the United Kingdom. Section 3 looks at the formation and the operation of CICs and an attempt is made to reflect on the experience from their operation in the United Kingdom so far. Section 4 concludes.

2 The Shift Towards Social Enterprises

Before we discuss the gradual, but steady, shift towards social enterprises and delve into the regulatory framework currently in place in the UK, it is essential to offer an overview of this concept and its basic characteristics. Social enterprise is defined as 'the use of market-based strategies to promote the public good'.[5] Another commonly used definition provides that it is 'an organisation or venture that achieves its primary social or environmental mission using business methods, typically by operating a

Brewer (2011), p. 679; Lane (2012), p. 3. There are also narrower definitions put forward, according to which social enterprises must directly address social needs through their products and services or through the numbers of disadvantaged people they employ. See Boschee et al. (2010), p. 1.

[2]Bugg-Levine and Emerson (2011), pp. 10–11, where blended value is used to describe the mix of economic, social, and environmental value that social enterprises produce.

[3]European Commission (2013), p. 45.

[4]Defourny and Nyssens (2008), p. 4; Doeringer (2010).

[5]See Cummings (2012), p. 578.

revenue-generating business'.[6] As it becomes apparent from these definitions, the main feature of social enterprises is that they combine the performance of a commercial activity with a social one and there is no exclusive emphasis on profit-maximisation. The European Commission has defined a social enterprise as 'an operator in the social economy whose main objective is to have a social impact rather than make a profit for their owners or shareholders'.[7] This definition signals that it concerns companies that have a social agenda and demonstrate a commitment for the achievement of this agenda. Social enterprises are expected not only to give priority to social considerations than profits, but to actually use part of their profit for social purposes.

A careful consideration of the current status quo in the United Kingdom reveals we are still far away from being able to talk about a social economy and stakeholder-focused businesses. In fact, company directors, guided by a commercial and legal system that was designed to prioritise shareholder welfare, never had any strong incentives to consider pursuing any other purpose. This idea, known as the principle of shareholder primacy, came to prominence in the United States and the United Kingdom throughout the 19th and 20th century on the basis that maximising shareholder returns would maximise total social welfare, and that corporate resources should be diverted toward social goods, such as environmental welfare. Although not explicitly enshrined in statute, a substantial body of case law held that the interests of a company are the interests of its shareholders and that company resources could not be diverted for any purpose that would not benefit them.[8] Milton Friedman has been famously quoted as a justification for the prevalence of a sheer profit-maximisation corporate paradigm and it has become a slogan that the 'There is one and only one social responsibility of business—to use its resources and engage in activities designed to increase its profits',[9] same as the judgement in *Dodge v Ford*, where it was stated that 'a business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end. The discretion of directors is to be exercised in the choice of means to attain that end, and does not extend to a change in the end itself, to the reduction of profits, or to the non-distribution of profits among stockholders in order to devote them to other purposes...'.[10] There have been several other quotes that

[6] See Katz and Page (2010), p. 85.

[7] European Commission (2011), p. 2; in the UK, the Department of Trade and Industry (DTI) has adopted a very similar definition: a social enterprise is a business with primarily social objectives whose surpluses are principally reinvested for that purpose in the business or in the community, rather than being driven by the need to maximise profit for shareholders and owners'; see DTI (2002), p. 7.

[8] *Greenhalgh v Arderne Cinemas Ltd* [1951] Ch 286; *Winthrop Investments Ltd v Winns Ltd* [1975] 2 NSWLR 666, 690; *Residues Treatment & Trading Co Ltd v Southern Resources Ltd* [No 4] (1988) 14 ACLR 569, 577; *Parke v Daily News* [1962] Ch 927; *Ngurli Ltd v McCann* (1953) 90 CLR 425.

[9] Friedman (1970).

[10] *Dodge v Ford Motor Company*, 204 Mich. 459, 170 N.W. 668 (Mich. 1919), para 684.

could have been used for slogans, such as Henry Ford's statement that, instead of boosting dividends, he would rather use the money to build better cars and pay better wages[11] or Johnson & Johnson's credo, written by General Robert Wood Johnson in 1943, that the company's first responsibility was not to investors but to doctors, nurses, and patients, but shareholder primacy was so deeply embedded in the Anglo-Saxon corporate world that it was extremely difficult to deviate from it.[12]

The late 20th century saw a relaxation of this position, which was accompanied by greater corporate involvement in the wider community through corporate social responsibility (CSR) initiatives. The introduction of the UK Companies Act 2006 and the adoption of the Enlightened Shareholder Value theory through section 172 was hailed as the end of short-termism and the beginning of a new era in corporate behaviour. We have to accept that section 172 did not bring the expected change of culture in corporate boardrooms and it has been argued that it has not lived up the expectations and in effect shareholder primacy remains at the core of the UK company law system.[13] However, it became apparent that blind short-termism can only have a negative effect on modern corporations and stakeholders' interests should not be ignored or overlooked in favour of those of shareholders.

Having regard to the interests of stakeholders is not a legally enforceable duty and falls short in disincentivising any investment that would detract from profit maximisation; nevertheless, companies can no longer afford to be disengaged from the society within which they operate, ignoring their social responsibilities. The financial crisis has highlighted this need to focus on the responsibilities, including social ones, of companies, investors, consumers and public authorities in relation to the challenges of climate change, the limits to natural resources and respect for human rights.[14] There is no expectation that companies solve the problems that our society experiences on their own, while at the same time are struggling to remain competitive and profitable, although the market though will react positively to the fact that a company is actively seeking to be socially responsible and sustainable.[15] For instance, it can give companies a competitive advantage in attracting new investors and trading partners, while it will boost sales and increase customer loyalty. At the same time, socially responsible companies can attract better qualified staff, who share the same values and aspirations, and increase the productivity and commitment of their existing employees, who will feel that they are being part of a larger cause.[16]

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[11] Ibid.

[12] https://www.jnj.com/_document/our-credo-english?id=00000159-6a64-dba3-afdb-7aef76350000.

[13] Collison et al. (2011), p. 44; Fettiplace and Addis (2010), pp. 61–62; Linklater (2007), p. 129; Greier (2014), p. 108; Grant (2015), p. 256.

[14] Taylor (2009/2010), p. 743.

[15] See, for instance, Sjafjell (2012) and Zrilic (2012). Many have expressed doubts about such a requirement, see, for instance, Yan (2013), Deva (2011) and Dine and Shields (2008).

[16] See von Arx and Zeigler (2008); Salzmann et al. (2005), p. 27. See also European Commission (2009), pp. 106–121.

Without strong and clear incentives, it is hard for companies to initiate a radical transformation of their business operations; not only the costs associated with this transition are likely to be high, but also without legal enforcement companies are unlikely to be convinced to take the risk, especially during the current times of uncertainty.[17] As Liao notes, it is the board of directors, who should step up and be the drivers for change.[18] This is why there have been introduced provisions allowing companies to adopt a legal structure that deviates from the traditional shareholder value paradigm and expands the corporate purpose beyond the narrow limits of the pecuniary interests of its shareholders. The next section will examine two of the most popular initiatives that have attracted the attention of entrepreneurs and serve as evidence that a shift towards more pluralistic corporate forms is actually taking place.

3 Benefit Corporations and B Corps

Starting with the benefit corporation,[19] this is a legal structure for a business, which exists in several countries across the globe, including the USA, Italy and Colombia. In the US, the 'benefit corporation' form was introduced in 2010 and so far, it has been adopted in 38 states as well as the District of Columbia, while more than 40 state jurisdictions across the country have enacted at least one social enterprise statute. It is designed for 'for profit' undertakings that also wish to take account of social and environmental considerations.[20] Their purpose must be to 'create general public benefit', which is defined as having 'a material positive impact on society and the environment'. There is no obligation to reinvest profits, nor are there limits to the distribution of profits, as the legal requirement for creating a 'general public benefit' can be met through the normal operation of the company, by having regard to its stakeholders and trying to combine profit maximisation with positive stakeholder impact.[21] From a first glance, it seems that there are similarities with the enlightened shareholder value theory that the UK government has tried to implement through section 172 of the Companies Act 2006 (CA 2006). One could not help but wonder whether the benefit corporations has been another attempt to deviate from the shareholder value paradigm with an element of flexibility, considering that the adoption of this corporate vehicle is optional. Although there is no evidence that the introduction of the rules regarding the benefit corporation has any connection with ESV, it can still be argued that the swift towards a different type of corporations

[17] Wessing (2010), p. 20. See also Stout (2012), p. 60.

[18] Liao (2015), p. 318.

[19] Hemphill and Cullari (2014), pp. 7–9. See also Koehn (2016); Murray (2014); Nass (2014); Brakman Reiser (2011); Cummings (2012).

[20] Blount and Offei-Danso (2013), p. 617; Brakman Reiser (2011), p. 591.

[21] See Clark Jr and Babson (2012); Clark Jr and Vranka (2013).

and a more pluralistic mode of governance is gradually becoming a reality. Is this the result of a process of enlightenment or just of the pressure exercised by the market and stakeholder groups? It does not really matter, because the two main supporters of shareholder primacy, the United States and the United Kingdom, have been actively exploring different options. What is also extremely important is that these options have the potential to introduce a different culture in the boardrooms and ultimately to drive corporate management away from short-termism towards a more long-run perspective.

Benefit corporations are often confused with certified B corporations. The main difference is that B corp is a certification, while benefit corporation is a legal form. The B corp certification of social and environmental performance is a third-party certification administered by the non-profit B Lab, based in part on a company's verified performance on the B Impact Assessment. B Lab was founded in 2006 by Stanford University alumni and businessmen Jay Coen Gilbert and Bart Houlahan, and former investment banker and Stanford colleague, Andrew Kassoy. The companies that have obtained this certification can designate themselves as 'Certified B Corporations'. Some companies are both certified B corporations and benefit corporations, and the benefit corporation as a corporate structure fulfils the legal accountability requirement of B corp certification. The certification is a prima facie indication for a company's environmental performance, employee relationships, diversity, involvement in the local community, and the impact a company's product or service has on those it serves. The rationale behind the establishment of this certification system was that there was uncertainty about the scope for a company's management to take account of social purposes.[22] Therefore, it was considered necessary to help these new entities organise their affairs in such a way that they will be able to pursue their dual purpose within the existing regulatory framework. To obtain certification as a 'Certified B Corporation', an impact assessment is conducted, during which the company goes under the microscope as a whole, i.e. its management, suppliers, employees, social and environmental impact, so that it is determined whether it meets the requirements for certification. Particularly, the B Impact Assessment examines a company's impact on their workers, community, environment, and customers as well as its governance structure and accountability. Questions are split into two categories: Operations, which covers the day-to-day activities, and Impact Business Models, which awards additional points for business models designed to create additional positive impact. Companies have to score at least 80 out of a possible 200 marks to become certified, pay an annual fee of between £500 and £25,000 a year, depending on their size and structure, and undergo a regular reassessment every two years. The B Impact Assessment is updated every three years to ensure that companies maintain the required minimum standards and work towards their improvement through the feedback provided during the reassessment process.

[22] Clark Jr and Babson (2012), p. 842; Clark Jr and Vranka (2013).

Apart from the certification, a B corp constitution must provide that a managing member shall [. . .] give due consideration to [. . .] the long-term prospects and interests of the Company and its members, and the social, economic, legal, or other effects of any action on [. . .] the Stakeholders [. . .], together with the short-term, as well as long-term, interests of its members and the effect of the Company's operations [. . .] on the environment and the economy of the state, the region and the nation.[23] It is also required to incorporate in the Articles of Association commitments to standards of social and environmental performance, accountability and transparency; and B corps must sign a declaration that includes a commitment to 'aspire to do no harm'.[24]

B corps are illustrations of a commitment to a 'triple bottom line' approach to business,[25] an accounting framework that incorporates three dimensions of performance: social, environmental and financial, with emphasis on the 3Ps: people, planet and profits. This commitment should not only be mentioned in the company's objects clause, but the whole company should be organised in such a way that it actually has a positive impact on the society and the environment. To put it differently, the overall fulfilment of obligations to the community, the employees, the customers and the other stakeholders should be measured, audited and reported exactly in the same way as the financial performance of public companies.[26]

The scheme started in 2007 and, as of September 2020, there are over 3,522 certified B corporations across 150 industries in 74 countries. For a voluntary arrangement, its expansion has been remarkable and indicates that there is a growing interest amongst companies internationally for ways to diversify their operation and their business model. Any company of any size can get B corp certified, even sole traders, as there are no requirements for minimum size. It is important to highlight that B corporation certification, apart from being entirely voluntary, does not bring any legal significance to a company's shareholders, stakeholders or to its employees. As described above, the certification (B Impact Assessment) allows companies to benchmark themselves against some of the world's leading exponents of 'profit with purpose' business, while the scores of all certified B corps are publicly disclosed, so there is a very strong incentive to improve. The process highlights the areas of weakness, providing a clear roadmap for improvement and practices that should be implemented. It remains to be seen whether the certification will be applied in a consistent way, while the assessment criteria are flexible enough on the one hand to accommodate all different types of companies and, on the other hand, to reflect the best standards in the market.[27] Until then, the recognition that companies, such as Patagonia and Ben and Jerry's, have received shows that the certification brings

[23] B Corporation (2013).

[24] Woods (2016), pp. 89 and 93.

[25] Elkington (1998); Henriques and Richardson (2004); Willard (2002); Slaper and Hall (2011), p. 4.

[26] Norman and MacDonald (2004), p. 257.

[27] Bridgers Ventures (2015).

significant branding benefits to the corporation, including greater outreach, broader recognition and impact. The higher the level of trust that is established between the corporations and the stakeholders, the higher the valuation of the brand and the position in the market. The recent 'B the Change' marketing campaign aimed to encourage certified companies to make greater use of the B corp branding on their packaging and marketing materials, so that there is more visibility and the consumer body learns more about what the movement is all about and what these companies are trying to achieve.

While there is not much doubt that the B corps are based on a more pluralist model of governance, there are concerns expressed for the lack of a legislative framework that would monitor compliance with the required standards in a more robust way, due to the fact that within the period between the reassessments, directors have unlimited discretion to shape the company's strategy and operation in any way they deem appropriate without any oversight. Criticisms also focus on the possibility that the B corps movement undermine the existing social economy and the contribution that charities and charitable trusts have been making.[28] The other side of the coin is that B corps do not necessarily redirect resources away from the civil society into the private sector; quite the contrary, social enterprises can complement charities and help in the expansion of the notion of social purpose to all sectors of the economy. The fact that there is a swift towards companies being committed to have a positive impact through their operation can create a momentum for a 'new social contract developing between business and society, in which businesses engage with stakeholders beyond their current narrow remit to create benefits for employees, citizens and society at large'.[29]

B Corp UK, the organisation responsible for trying to implement B corporations in England and Wales, was hoping to sign up roughly 50 B corps in 2015 and there are currently 275 companies that are certified B corporations across many industries including legal services, advertising, accounting, telecommunications, even hairdressing! Some of the most notable companies that have achieved certification are the Jamie Oliver Group, Activia, Danone and Abel & Cole. Considering that the United Kingdom is widely recognised as having the most highly evolved social enterprise sector in the world,[30] it is rather surprising that on the one hand benefit corporation legislation does not exist in the United Kingdom, while on the other hand the B corps certification system has not really taken off. There can be two explanations for this: at first, that the UK Companies Act 2006 is a very flexible instrument, designed to enable businesses to have regard to different groups of stakeholders through the duty of directors to promote the success of the company. Despite the concerns as to the enforceability of this duty and the overall success of the Act to instil a more enlightened way of doing business in the UK, people are still sceptical regarding the extent to which B corps really have a different modus

[28] See LeClair (2014).

[29] Advisory Panel to the Mission-led Business Review (2016), p. 3.

[30] Regulator of Community Interest Companies (2013), p. 35.

operandi. The second justification is that there is the community interest company and, as it will be discussed in the next section, this form has managed to create strong supporters within the UK markets and business community in general.

4 Community Interest Companies (CIC)

'The CIC idea was initially hatched over a bottle of claret in Balls Brothers Wine Bar in Cheapside by myself and Roger Warren-Evans, a serial social entrepreneur'.[31] This is how Stephen Lloyd, the founding father of CICs, described the formation of the idea behind this *sui generis* corporate form. Their motivation was that they were dissatisfied by the reduced status and low profile of industrial and providence societies, and they agreed that there was room for a new legal form for social enterprises. The government endorsed their plans for creating public interest companies and shortly after the community interest company, a special form of social enterprise, was introduced in the United Kingdom under the Companies Audit Investigations and Community Enterprise Act 2004. The 2004 Companies Act became especially effective when given effect by two subsequent Regulations: the Community Interest Company Regulations of 2005 and the Community Interest Company (Amendment) Regulations of 2009. The first CIC incorporated in the United Kingdom on 11th August 2005 and 15 years later there are more than 15,700 CICs on the public register providing community benefit in all business types across the United Kingdom. The rapid growth and the fact that CICs quickly outnumbered both cooperatives and mutual, two quite old and traditional corporate structures, serves as evidence that the establishment of the CIC has been a very positive development and a successful addition to the business vehicles available in the UK business environment.

From the beginning, it became apparent that the whole concept of benefit corporations has been applied differently in the United Kingdom compared to the United States. For example, up until 2015 a close look at the companies that have applied to B Lab to become B corps in the United Kingdom, the majority were small and medium-sized businesses, not large or multinational companies that would try to get access to foreign markets and sell their products internationally.[32] The motivation has been different and, despite the fact that companies can significantly benefit from the B corp branding, increased awareness and wider profit margins at a global basis, CICs seem to be more focused on the local communities within their country of registration, such as nurseries, community groups, spin-outs from health, youth services and other public sector areas. It would not be an exaggeration to say that CICc bear greater resemblance to non-profit organisations rather than for-profit

[31] Fisher and Ormerod (2013), pp. 58 and 118.

[32] Williams-Grut (2015).

businesses.[33] This motivation can be seen in the UK government's website, where it is mentioned that CICs are effectively companies 'working for the benefit of the community',[34] providing services by and for communities. Another interesting fact is that a significant number of CICs, especially during the first years after the introduction of the CIC form, have been companies limited by guarantee, which in practice means that they can never pay out dividends, as they have no share capital and no shareholders. Of course, this can change as time goes by, depending on the nature of the CIC's business, because if private investors wish to invest in the company, they cannot get shares.

Under the 2005 Regulations, companies (both limited by shares and limited by guarantee) can be re-registered as CICs.[35] To be registered as a CIC, a company must declare how it will benefit society, providing information about the nature of the community interest that it will pursue. This statement of purpose is also being assessed through a 'community interest test', which stipulates that 'a reasonable person might consider that its activities are being carried on for the benefit of the community'.[36] For example, the pursuit of political aims, such as support for political campaigns, is not allowed.[37] Any benefits or advantages provided by the company in the context of its operation should favour the wider community. Thus, specific social groups are favoured, as long as this does not undermine the genuineness of the social purpose pursued.[38] Such examples are when a hospital is built, a museum is established, or clinical trials are supported.

Practically, companies limited by guarantee must either re-invest their profits in the company or use the profits for social purposes. Companies limited by shares must combine the pursuit of the stated social purpose with the promotion of their success, financial or of any other kind. The transformation into a benefit corporation requires a 75% majority of the shareholders and any minority shareholders, who wish to express their opposition to the conversion, can refer the matter to the courts within 28 days, to have the decision blocked.

CICs are regulated by the CIC Regulator, an independent statutory office holder, appointed by the Secretary of State. The Regulator is responsible to screen companies that seek registration as CICs and monitors their activities, since CICs are subject to restrictions on the payment of dividends, transfer of assets and capital investment. The Regulations governing CICs do not contain any special guidelines or any specific provisions on the duties of management, other than the implicit obligation to pursue social purposes.[39] All CICs must publicly file a 'CIC Report' within 21 months of incorporation (and subsequently, annually), describing the

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[33] Borzaga et al. (2020), pp. 30–31.

[34] Department for Business, Energy and Industrial Strategy (2016a), p. 5.

[35] DBEIS (2016c), Chapter 4.

[36] Companies (Audit, Investigations and Community Enterprise) Act 2004, section 35.

[37] DBEIS (2016c), Chapter 4, section 4.6.

[38] DBEIS (2016b), Chapter 2, section 2.3.

[39] DBEIS (2016e), Chapter 9, p. 4.

actions the CIC has taken to benefit the community in line with the company's initially stated community interest purpose.[40]

The Regulator is entrusted with the task of facilitating the formation of CICs. More specifically, the Regulator will not take an inflexible or bureaucratic approach towards new applications and an attempt will be made to resolve any problems informally and without undue delays. However, this does not imply any pro-active supervision of individual CICs or any pre-judgement by the Regulator.[41] For example, in 2009–2010, 1,572 applications were received, out of which 1,298 were accepted.[42] In 2016, the applications received were 4,007, but there was a 30% rejection rate.[43]These statistics indicate that the scrutiny can be quite robust, and a certain level of minimum standards needs to be met before certification is provided. In this way, there is a degree of certainty that all social enterprises that have received the certificate by the authorities are in compliance with the requirements of the law.

In the US, some states have introduced a requirement for benefit corporations to appoint a 'benefit director', who is responsible for monitoring, on a continuing basis, whether the company complies with its obligation to pursue or create public benefit or a specific public benefit. Although the respective laws do not provide for any liability to pay compensation in case this obligation is breached, there is an element of monitoring on a continuous basis after registration, which can be seen as an additional mechanism of checks and balances that ensures that the pursuit of the social purpose is not abandoned.[44] Equally, as it was discussed above, B corps also have to be re-certified every two years and since the assessment criteria are being updated regularly in response to the current best practices, it can be more difficult and demanding to reach the required score each time.

When a company's primary purpose is of a social nature, this inevitably raises the question of whether the stakeholders whose interests the company must serve should be able to sue the company if their interests are not promoted in line with the company's stated purpose. In the UK, stakeholders cannot sue a CIC, but they can complain to the Regulator, who can in turn examine the complaints, ask for additional information or evidence in to verify the validity of these complaints.[45] Moreover, the Regulator can appoint, suspend or dismiss members of the board of directors where: (a) there is misconduct or mismanagement; (b) it is necessary to

[40] See Regulator of Community Interest Companies (2015), p. 18. See also DBEIS (2016e), Chapter 9.

[41] DBEIS (2016g), Chapter 11, section 11.1.

[42] See Department for Business, Innovation and Skills (2011), p. 7. See also Ishkanian and Szreter (2012).

[43] Community Interest Companies Blog (2017).

[44] Benefit directors are mandatory in Hawaii, New Jersey and Vermont. Section 302 of the Model Legislation for benefit corporations made provision for there to be a mandatory benefit director for all publicly traded corporations. See also Brakman Reiser (2011), pp. 604–605 and Brakman Reiser (2013), pp. 38–39.

[45] DBEIS, Chapter 11, p. 11.4–5.

protect the assets of the company; (c) the company fails the 'community interest' test mentioned above; or (d) the company does not carry on any activities in pursuit of its social purpose.[46] The Regulator also has the power to institute proceedings to wind up the company.[47]

When a company has a very broad or generic statement of purpose and, in light of the fact that there are no guidelines about the actual fulfilment of the social purposes or strict rules about management liability, it would be extremely difficult to stipulate such a right for the stakeholders. Particularly, it would be really challenging to identify the stakeholders, who have a right of action,[48] there will be uncertainty about the risk of liability and stakeholders deciding to start proceedings would be sailing in uncharted waters, as it will be hard to prove to what extent a company's management has fulfilled its obligations towards them.[49] At this point, it is worth mentioning that in the US certified companies play the role of the watchdog themselves as to whether the other certified companies continue to fulfil the requirements for certification and it is thus not unheard for the B Lab to receive complaints from other certified undertakings.[50] This system of 'checks and balances' offers an effective solution to the problem of limited resources of the regulators or the supervisory authorities and can be characterised as self-monitoring, because it is the market participants themselves who are monitoring each other and are responsible to report any breaches that they may come across. The other side of the coin is that it is possible that complaints can be made without any support from evidence or based on rumours and suspicions or they can be driven by indecent motivations, such as to harm or eliminate the competition. Of course, such practices, apart from being unethical and unprofessional, do not fit with the whole purpose of social enterprises and should thus be avoided.

Reference needs to be made on the issue of how profits will be used and what proportion will be distributed to shareholders through dividends, the approach taken by the United Kingdom is that there should be restrictions on the shareholders' discretion on the transfer of assets, such as payment of dividends or asset disposal, especially in the event of winding up or reincorporation as an ordinary company. A CIC can only pay its shareholders a maximum dividend of 5% over the Bank of England base rate. Only 35% of a CIC's distributable profits in any one year can be paid out in private dividends to shareholders; the rest must be kept in support of the CIC's mission. Until the law changed in 2014, there was a double asset lock: in addition to the 35% restriction, dividends could total no more than 20% of the value

[46] Companies (Audit, Investigations and Community Enterprise) Act 2004, section 31.

[47] DBEIS (2016g), Chapter 11, section 11.4.2.6.

[48] In companies that have adopted a two-tier board system, it would be perhaps easier to monitor the conduct of directors and through employee or stakeholder representation open the avenue for directors' liability.

[49] Engsig Sørensen and Neville (2014), pp. 296–297.

[50] Engsig Sørensen and Neville (2014), p. 298.

of the shares held.[51] In case that dividends are not paid in one year, the amount payable can be carried forward and be used in the distribution of profits in the following year. In the context of the adoption of the rules related to CICs, there was a number of proposals about dividends and distribution of profits, but this model was supported as more compatible with the whole idea behind the creation of CICs.[52] An alternative solution could be to require that a payment be made for social purposes if it was decided that dividends would be paid to the company's shareholders. In this way, the company would in principle fulfil its dual purpose, as the company would in fact justify that it has sufficient financial resources to invest in the fulfilment of its social purpose as well as pay its shareholders without endangering the company's financial stability.[53]

In terms of other kinds of disbursements, it is worth mentioning the following rules:

(a) a CIC can only buy back shares at a price corresponding to what was paid for them;
(b) if a reduction of capital is decided, a CIC may not pay out on shares that have not been fully paid up, and the maximum that can be paid out is equal to a fully paid-up share;
(c) the maximum interest that can be paid on a loan where payment is dependent on the company's profits is 10% of the principal; the rationale behind this rule is to prevent owners from providing loans instead of buying shares to avoid the restrictions on the payment of dividends;
(d) the directors of a CIC only receive reasonable salaries or fees and the reasonableness of these is monitored as per the provisions of the 2005 Regulations.[54]

The imposition of all the restrictions (asset locks[55]) aims at preventing greenwashing[56] and protecting the social character of CICs. The wording of the rules reflects an attempt to limit the flexibility allowed to shareholders and prevent

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[51] Community Interest Company Regulations 2005, section 17 ff. Under Section 30 of the Companies (Audit, Investigations and Community Enterprise) Act 2004, the Regulator has authority to determine the limits for dividend payments and other disbursements. See also DBEIS (2016d), Chapter 6, section 6.3.

[52] Cross (2004), p. 312. See also Neville (2013), pp. 179–217.

[53] Engsig Sørensen and Neville (2014), p. 300.

[54] Community Interest Company Regulations 2005, section 30.

[55] An asset lock is a commitment by CICs and those who set them up to lock profits and assets into the company irrevocably, through the implementation of the following two measures: (a) prohibit or impose limits on the distribution of assets by community interest companies to their members, and (b) impose limits on the payment of interests on debentures issued by, or debts of, community interest companies.

[56] The flipside of this trend towards increased transparency is the risk of 'green washing' or 'purpose-washing' where large businesses present a social or environmental front that is not backed up by realised social or environmental impact. It can be hard to distinguish between a company that is genuinely creating value for society and the environment, from one that is good at marketing. Amongst others, see Ramus and Montiel (2005), Laufer (2003) and Bowen (2014).

practices whereby the profits are paid back to the shareholders instead of being used for the pursuit of the company's social purpose. For instance, in relation to the directors' salaries, there are no criteria as to what constitutes a reasonable salary or a formula that would allow the authorities to set minimum or maximum standards for the companies to adhere to. The restriction is clearly aimed to prevent the manipulation of the companies' financial statements and the undue setting of the levels of the executive pay.[57]

A more important set of restrictions is related to the CICs' de-registration and conversion. A CIC is not allowed to convert into an ordinary company.[58] It is not possible for a CIC to simply denounce their social purpose and decide to become a normal 'for profit' company, because there would be room for fraudulent activities through companies opting in and out of the CIC scheme. If the conversion of a CIC into a normal company would be allowed, the shareholders would be able to take control of all the assets created during the period that the company was operating as a CIC without any obligation to account for them to the stakeholders. Therefore, it is decided that a CIC is wound up, its assets cannot be distributed to the shareholders. Shareholders may only be paid an amount corresponding to their original capital investment in the company, while the remaining assets must be allocated to other CICs. If the articles of association of the CIC in question does not specify which CIC (s) should receive the assets in the event of its winding up, then the Regulator will decide.[59] The only conversion that is allowed is the conversion of a CIC into a charitable trust or an Industrial and Provident Society, and the company's assets will be entirely devoted to social purposes.[60] Interestingly, in benefit corporations a conversion into a normal corporation is allowed without any restriction related to the use of the assets as long as the decision has the support of the two thirds of the shareholders.[61]

The restrictions described above are supplemented by reporting requirements, which promote transparency, so that the company's stakeholders as well as the authorities are informed about the CICs' performance, especially in relation to the fulfilment of the social purposes. This is why the 2005 Regulations specifically mention that the reporting obligations must cover how the company has served the community interest, how the company has consulted the interest groups affected by the company's activities (and the results of these consultations), information about payments to directors, information about dividends, information about payments of interest on loans which are dependent on the company's profitability and a review of activities carried out by the company without charging a full fee.[62] These reporting

[57] DBEIS (2016d), Chapter 6, section 9.3.6.

[58] DBEIS (2016f), Chapter 10, section 10.5.

[59] DBEIS (2016f), Chapter 10, section 10.4.4. See also Community Interest Company Regulations 2005, section 23.

[60] See DBEIS (2016f), Chapter 10, section 10.2 and 3.

[61] Model Benefit Corporation Legislation 2017, section 105(a).

[62] Community Interest Company Regulations 2005, section 26ff.

requirements cannot be considered as excessive compared to the information that public companies are required to disclose. In addition, the social purpose that these companies pursue make the content of such disclosures significant not only for its own shareholders, but also for competitors, investors interested in investing and the interest groups which are to benefit from the social purpose pursued.[63]

Before concluding, it is essential to engage with the criticism that the CIC form has received and the drawbacks that have been identified so far by academics and practitioners.

One quite commonly argued criticism in relation to CICs is that this corporate form can easily be used by 'weasely people who want to hide behind a veneer of social benefit without the same level of accountability'.[64] This line of thought is based on the premise that charities can be used if the aim of the business is to have social impact, instead of using CICs, which offer 'the simplicity of company structure without the extra level of governance' and 'a less intense regulatory regime', considering that the Office of the Regulator is a rather 'light-touch and rarely goes public when following up [with] complaints'.[65] It is true that the Regulator openly acknowledges that its role is intended to be light-touch, but this does not mean that it will allow abuses or it will not apply the Complaints Procedure Protocol in the event that complaints are received. Particularly, the fact that CICs seem to work closely with the local communities is indicative of their intention to be more transparent and directly accountable to the same local communities that they intend to work for. The pressure from such communities can be substantially the same as the reputational damage if the CICs fail to live up to the expectations created by their purpose statement. Phil Horrell, the Office Manager at the CIC Regulator, argued that a CIC 'theoretically offers greater potential for rapid expansion and diversification, not only because of the looser financial regulation but also because of the greater opportunities for raising capital'.[66] However, he emphasised that the choice between a charity and a CIC is an important one, same as the distinction between these two forms. Particularly, CICs and charities are two separate entities because they cover two distinct degrees of benefit: benefit to the community and general public benefit.[67] Therefore, a company should decide to become a CIC over a charity mainly to 'be branded as a social business' that the public will view 'like [a] charit[y]' while still operating under the 'dynamism' of for-profit businesses.[68] Perhaps, the UK government and the Regulator should try to draw some inspiration from the United States and promote more the CIC brand and its value as a business

[63] See Nicholls (2010), p. 384. See also Brakman Reiser (2011), p. 613.

[64] Senscot (2015). See also Cho (2017), p. 167.

[65] See Third Sector (2015).

[66] Jump (2007).

[67] See Edmonds (2014), p. 4 (Although the community interest test to become a CIC is whether the CIC's activities would benefit the community, charities must pass a different test, the charitable test of public benefit.). See also Borzaga et al. (2020).

[68] Jump (2007).

vehicle for global expansion even under demanding market circumstances, as the ones that currently exist.[69]

Another issue that has attracted criticism is the lack of any provisions granting tax relief for the CICs, as it is the case for charities. A CIC is not entitled to any specific corporation tax exemptions and its profits are fully taxable unless it can be shown that the terms of the contract are such that, in tax law, the organisation does not amount to a taxable trade. In most cases, a CIC will enter into a contract with a third party to provide goods or services and it is difficult to see the contract as anything other than a commercial arrangement freely entered into. This leaves the question of whether the services are provided for reward or, perhaps more meaningfully, for profit.[70] A CIC is, of course, required under its articles of association to apply any profits for the benefit of the community. However, this not-for-profit motive does not affect the corporation tax position on earning profits; it merely directs how those profits are to be applied. A CIC's not-for-profit motive does not, therefore, affect its corporation tax status.[71] Until now, there is no evidence to support that there will be a change of approach in relation to tax reliefs or lower corporate tax rates for CIC any time soon, so it is unlikely that this concern will be addressed by the government in the short-run.

5 Conclusion

In the early years of the development of the CICs in the UK, it was noted that this corporate form 'assumes [there is] a pool of investors with an appetite for wedding financial and social return and sufficient brand awareness and confidence to appeal to them . . . [It also], however, requires these investors to be especially devoted to the blended enterprise concept by substantially limiting the upside of their investments'.[72] While it seems that this has not been a deterring factor for entrepreneurs and investors, at least looking at the number of CICs registered so far, time will show whether the CIC form will stand the test of time and to what extent it can play a central role in the UK's corporate sector. It is also very difficult to predict whether it will expand to all industries and sectors of the economy and it will be of critical importance whether multinational corporations will be tempted to become CICs or use this form for their subsidiaries.[73] Equally, it has to be seen how well CICs will cope with the competition that B corps and benefit corporations will create in the next few years. Even if the CIC model becomes a credible complementary model to the traditional/mainstream corporate models, it will be a huge success, because it will

[69] Cho (2017), pp. 169–170.

[70] See *BBC v Johns* [1964] 1 All ER 923.

[71] Batty (2015), pp. 25–26.

[72] Brakman Reiser (2010), p. 649.

[73] Liao (2015), pp. 311–312.

definitely challenge them and it will oblige corporate executives to re-think the purpose and mission of their companies.

This conclusion is based on the fact that increasing jurisdictions have been introducing or are seriously considering introducing new or hybrid structures with a more social orientation. All these new initiatives, such as B corps and CICs, are voluntary and still represent a trend, not an integral part of the international business landscape. They need to evolve, improve and become more attractive. One of the major challenges in regulating social enterprises is to find a solution that is both flexible and credible. On the one hand, it is necessary to ensure that companies that are designated 'social enterprises' do indeed pursue social goals. This may call for specific requirements for qualification as a social enterprise, as well as restrictions on what companies may do as long as they are classified as social enterprises. On the other hand, the regulations should be sufficiently flexible, so that the social enterprise regime is not solely for those whose activities have a purely charitable aim. It is not easy to balance the interests of those who are profit-driven and those who wish to pursue social purposes.[74] However, what should not be overlooked is the fact that the topics of social economy, social enterprises and corporate pluralism are now part of the agenda of discussion at all international political, economic and business forums. Even if the discussion takes a long time to mature and lead to any resolutions or initiatives, at least an exchange of views has been initiated and, as long this exchange does not halt to a stop, this is a positive development.

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[74] Engsig Sørensen and Neville (2014), pp. 268–269.

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