On Inventing the Purpose-Driven Enterprise

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Research Note

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Abstract

In this article we present the main lineaments for a reform of the business corporation introducing the purpose of the firm. In France, a report commissioned by the government recommends that two new concepts should be introduced in law: the raison d'être of the firm and "purpose-driven enterprises." This reform partly originated in a research program carried out in France after 2009. The legal articulation of a so-called "purpose-driven enterprise" has now taken off, first in the US and now in France and elsewhere. It paves the way to introducing sustainability issues and new valuations processes in corporate governance.

Key words: Profit-with-purpose corporations; mission; corporate law; corporate governance

Is the for-profit corporation compatible with a social or environmental purpose? Are the values and valuations that control for-profit business structurally at odds with other objectives, despite the conciliatory hopes put forward by numerous investors and entrepreneurs? Today, it is mostly acknowledged that financial value doesn't contradict the aim of creating other types of social, cultural, scientific or environmental values. If new technology is able to capture carbon in an efficient way, it should bring both environmental and economic value. Yet, the value the business corporation is willing and likely to develop heavily

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depends on the governance mechanisms that distribute control rights over corporate strategy. And in practice, for-profit enterprises do indeed often lack the means to protect "extra-financial" missions when the dominant view among their shareholders is to expect financial and short-term return on investment. Corporate social responsibility (CSR) measures and doctrines, despite notable achievements, have fallen short of altering the dominant business rationale. In practice, any determination in that direction at managerial or executive levels can be countered at the level of the shareholders. Inventiveness is still possible, and we have witnessed in recent years the augmentation of managerial, economic and legal innovations that focus on how to frame the purpose of business beyond profit maximization. In France, a report commissioned by the government, and strongly influencing the current writing of the law, recommends that two new concepts should be introduced in law: the *raison d'être* of the firm and "purpose-driven enterprises" (Notat and Sénard 2018).[1]

Our research has attempted to contribute to that discussion. The development of a model for a "purpose-driven enterprise" – *"entreprise à mission"* – constitutes the prime outcome of this research program. A crucial – and at the time surprising – legal innovation in this area is the development in the early 2010s in the United States of the "social purpose corporation" and of the "benefit corporation": these two particular legally defined types of for-profit corporations detail in their corporate charters explicit social or environmental purposes, different from profit maximization (Levillain 2017). Our research suggests that in order to make such initiatives robust and tractable, the key emphasis is on the commitment demanded of shareholders on a public and transparent formulation of the purpose of the corporation, augmented with precise assessment and accountability protocols. Actually, existing – or still emerging – profit-with-purpose corporations commit for example to the development of pharmaceutical R&D strategies preserving nature and living systems through simulation; to the invention of innovative renewable energy production methods for energy transition; or to the development of novel forms of social business.

What such innovations need to confront is the so-called "deformation" of the idea of the enterprise (Lyon-Caen and Urban 2012; Favereau 2014). Focalization from the 1970s onwards on

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[1] The report recommends that:

• The board of the corporation should formulate the *raison d'être* of the company, which sets its purpose and can differ from the interests of shareholders.

• The law should recognize a new corporate status – mission-led corporation. It could be obtained by any company, irrespective of its legal form, if the company makes its *raison d'être* legally binding for its directors by integrating it into its charter, undergoes external evaluation of its respect for the mission expressed in its *raison d'être,* and reports on it.

profitability criteria and financial metrics on the framing and design of corporate governance translated into the processes of financialization that are now well documented. While shareholders have increasingly contrasted profiles and strategies (hedge funds, assets managers, impact investors, etc.), a series of economic and managerial doctrines has played a crucial role in the evolution of corporate governance, agency theory being among the most notable. The control of shareholders ("principal") over chief executives ("agents") allows reduced focalization of business strategies on financial returns, at the expense of social or environmental values. Although this is not a uniform trend, corporate governance has widely propagated a biased representation of the enterprise, which the law has not countered. Indeed, if the law does not require that management run the company in the interests of shareowners, neither does it protect social or environmental ambitions if shareholders happen not to support them. This explains abundant observations on how the so-called "shareholder value maximization" criteria lead in shifting risks from the activity of firms to other parties, causing major social and environmental tort (Margolis and Walsh 2003). In addition, this trend also threatens the very economic sustainability of the firm, together with its capacity to innovate (Lazonick 2007, 2014).

A critique of the rule of the maximization of shareholder value is inevitably suggested in the research that observes such processes of "deformation." But more fundamentally, this deformation, which threatens recursively the stability of any business enterprise, reveals a theoretical confusion between the corporation, which is a legal entity, and the enterprise being left devoid of legal consideration (Robé 1999; Greenfield 2008).

Research in management and law has also insistently observed a crucial flaw in shareholder-oriented governance: based on the idea that because shareholders take more risks they should be paid first, it ignores the fact that risks are in fact jointly assumed by a number of parties, starting with employees who in a sense do invest in the firm. The view of the corporation as a legal fiction, a mere nexus of contracts, and the concomitant development of the idea that shareholders do own the firm (when they in fact own only shares emitted by such a legal person) do also contribute to the construction of the "interest of the corporation" as the aggregate financial interests of shareholders, which can run, sometimes blatantly, against the manifest interest of the "enterprise" as a value creating collective.

An alternative to this is precisely to conceive the corporation itself as a legal entity, independent from the shareholders but integrating the purposes of the multiple stakeholders whose contribution is necessary for the value creation process (Blair and Stout 1999; Robé 1999; Lan and Heracleous 2010). Decision makers within the firm, the board of directors in particular, ought then to consider the interests of this legal

entity in a neutral, balanced manner. The law, however, does not have much at hand for defense of an ideal of "corporation's interest" that would fall beyond the shareholders' monopoly: shareholders are for example, still responsible for appointing and removing directors, who act as spokespersons of the corporation. A number of interesting proposals are nonetheless available for progress in that direction: the introduction of constituency statutes in the United States, or the recent modification of the Companies Act in the United Kingdom, was meant to allow directors to take into account the impact of their decisions on all stakeholders. Yet their effective impact is debatable today (Keay 2011).

The business "enterprise", in addition, is a quite recent notion. Unlike the business corporation which settled in law during the first half of the nineteenth century, the enterprise emerged in the late nineteenth century with the development of labor contracts and professional management, prompted by the dynamics of science and technology. Many authors have put forward the radical implications not only for an economic model, industrial relationships, but also for a law for this shift from a regime of production to a regime of generation of products and new production means (Fayol 1917; Rathenau 1918; Commons [1924] 2017; Follett 1924). Following these pioneering authors, we conceptualize the enterprise's potential as a form of "collective creation" (Segrestin and Hatchuel 2012; Segrestin et al. 2014; Favereau and Roger 2015). The modern enterprise was constituted in order to develop new communication systems, to invent new therapies, to explore unknown territories. Therefore, the mandate given to managers can often be expressed as a "desirable future" more than as a defined value. But if the enterprise is formed to shape the future and to transform our environment, a normative stance obviously goes with this conceptualization. How can this collective creation be best oriented toward the collective interest? Today's innovative and global business enterprise cannot be thought of as a private actor pursuing its own interests. As an engine for the production of society, its governance should certainly match the requirement of general welfare.

Multiple possibilities have been considered – and even experimented with – with the purpose of countering the "deformation" of the enterprise and restoring the notion of a collective purpose. As mentioned above, CSR stands as perhaps the most documented of these. It has undoubtedly produced new, interesting managerial norms and dialogues. But the credibility of CSR initiatives fails to a large extent the shareholder test – especially in cases of economic stress. Political solutions consisting of opening governance to the representation of stakeholders are certainly promising. But they often raise the question of the distribution of power and the erosion of management. In the face of this mixed achievement, allowing

enterprises to define their own mission offers a new productive path (Mac Cormac and Haney 2012; Segrestin et al. 2015; Levillain 2017). First, the stipulation of a "desirable future" at the very core of corporate charters restores in law the nature of the modern enterprise, and recognizes it as a different entity from the corporation. Second, it commits the corporation and implies that managers are accountable to shareholders but with a purpose not exclusively in the interests of shareholders. It stabilizes the strategic orientations and makes CSR initiatives credible. Finally, as the goal is to designate unknown but desirable innovation (such as new technologies for energy transition), it allows collective and sustainable engagement to address contemporary challenges. Thus, profit-with-purpose corporations preserve entrepreneurial leeway while fostering engagement in collective interests.

It is too early to assess the effective transformation of purpose-with-profit corporations. But for scholars, it raises new questions about the valuation process associated with a commitment into desirable futures and the related accountability devices. It also invites revisiting the legal foundations of contemporary capitalism (Commons [1924] 2017). While the law was up until now often considered to be aimed at social and management sciences, a comprehensive understanding of contemporary organizations and challenges may indeed contribute to a renewal in law toward more sustainable governance rules.

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