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JEFFREY GUTERMAN

A Rent-Seekers Tax?

BY RYAN MURPHY

In the last 35 years, states, counties, and cities have enacted 240 "megadeals"—amounting to at least $75 million apiece—that dole out corporate welfare in hopes of spurring "economic development." If you take naive calculations at face value, those subsidies have spent $456,000 per job ostensibly created. Of course, the economics behind subsidies creating *any* jobs at all are shaky at best. Yet these sorts of policies persist, using the same economic rationales, whether they are tax credits for biotech or cities giving sweetheart deals to local sports teams.

Judith Grant Long, in an extensive study on the historical realities of "partnerships" between governments and major sports teams, has found that the public on average bears 87 percent of the cost for new stadiums. Stadium deals are among the most flagrant examples of giving money to rich people in hopes of "creating jobs." As shown by John Siegfried and Andrew Zimbalist in a 2000 issue of the *Journal of Economic Perspectives* and Dennis Coates and Brad Humphreys in a 2008 issue of *Econ Journal Watch*, economists as a profession are as united against subsidies for sports stadiums as they are united on any issue. Yet, despite the constant pushback from the economics profession, stadium proponents are winning the war.

Activism by economists, libertarians, and the informed public has delayed many proposed stadiums, but most of them ultimately wind up getting built at great public expense. In other words, we have won some battles, but not the wars. After years of fighting for subsidies, the Miami Marlins got them and in 2012 built a gaudy stadium, in part financed by $91 million in bonds issued by Miami-Dade County. The financing was handled so poorly that the $91 million in bonds will eventually become a $1.2 *billion* obligation. While the anti-public-financing activism has been a clear public good, government officials will continue to view themselves as being trapped in a prisoner's dilemma, fighting for a finite number of teams.

Taxing local subsidies / There is a policy proposal already on the table that would stop this behavior in its tracks. But it is counterintuitive to the ears of many free market proponents because the solution involves a tax. In principle, the Internal Revenue Service could count money contributed by the state, county, and city toward the building of a stadium as imputed rent for the team owner—because that is exactly what it is. It could tax that income at the same rate it taxes other income. In effect, the federal government simply grabs back some of the corporate welfare that the other levels of government tried to give the team owner.

The IRS could even tax the income at 100 percent. Marginal tax rates that high have predictable consequences. When the marginal tax rate on income is 100 percent, we expect there to be approximately zero income. Likewise, when the marginal tax rate on rent-seeking is 100 percent, we should expect there to be approximately zero rent-seeking. The tax in practice would raise no revenue whatsoever and

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there would be no reason why team owners would even ask governments for money. We would be on the "wrong" side of the Laffer Curve, and that would be a good thing.

This type of proposal isn't a new idea. Arthur Rolnick, the longtime director of research at the Federal Reserve Bank of Minneapolis, has made this case for many years, most recently in 2007 congressional testimony. Yet, awareness of this proposal among free market advocates apparently is minimal. It is exactly the type of proposal that skeptics of government intervention *should* advocate for, or at least they should carefully weigh its merits. This is a "new tax," but it is a tax that will raise little or no revenue while reducing or even eliminating a huge source of graft and waste. On balance, that seems like a real win, even if it uses the "t" word.

One counterargument to this idea is that it is unlikely to gain passage because politicians at the federal level are no wiser or more angelic than their counterparts at lower levels of government. That is true, but federal politicians do not face the same incentives as a state or local politician. Local politicians perceive it to be the case—whether or not it is true—that they must fund corporate welfare to keep jobs from getting stolen by some other jurisdiction. Since federal politicians as a group do not have this concern for the industries in question, they may be better incentivized to implement this reform.

Those still skeptical of the positive ability of the federal government to do much of anything beneficial should heed Rolnick's apt analogy of this proposal to the dormant Commerce Clause. Just as the dormant Commerce Clause has successfully stopped states from erecting trade barriers on one another, it is reasonable to believe the federal government may be able to stop states from engaging in other ruinous negative-sum games that purport to create jobs. In terms of positive actions possibly undertaken by the federal government, that is about as free market as it can get.

Stadiums are merely the most concrete example of this idea. The tax could govern all forms of "economic development" legislation that are little more than corporate welfare. State legislators thus would no longer get to play central planner by handing out tax breaks to manufacturers or biotech firms.

Should we expect this solution to work perfectly? Clearly, no. This is a political solution. Inevitably, as the proposal goes through the political process, various exemptions will get tacked on. And states will try to get around it in other ways, for example by spending more than they should to upgrade infrastructure serving otherwise privately financed stadiums. But even an imperfect solution significantly reduces the benefits of rent-seeking—and that is what matters. *R*

Why Regulatory Reform?

BY STUART SHAPIRO AND DEBRA BORIE-HOLTZ

Regulatory reform is all the rage. Congress is currently considering more than 20 bills to change the regulatory process. State governments have joined in, passing reforms of many different shapes and sizes in recent years.

On its surface, this is an easy phenomenon to understand. Regulations impose significant economic costs (while also delivering significant benefits). They are promulgated largely by unelected officials in executive branch agencies. Regulatory reforms are intended to increase democratic oversight over an important policymaking tool.

But there is a problem with that explanation: it is contingent on the supposition that regulatory reforms actually have an effect on the regulations they are designed to affect. Most academic studies of the role that reforms have played in regulatory decisionmaking have found that this role is limited.

Many of those studies have looked at reform at the federal level. Requirements for public participation in the regulatory process often lead to many public comments on agency proposals, but few proposals are changed significantly in response to the comments. Requirements for economic analysis have done little to improve the efficiency of regulations. Other efforts, such as requiring negotiation, analysis of impacts on small businesses, and regulatory "look-backs" to gauge rule efficiency and effectiveness have had similarly limited effects.

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At the state level, we looked at 28 states in an aggregate analysis and one state—New Jersey—in detail (see "Lessons from New Jersey," Spring 2011) and our findings echoed the studies of the federal government. The best predictor of the volume of regulation in a state had nothing to do with the presence or absence of reforms. It was instead the political preferences of state legislatures. If legislatures were controlled by Democrats, state agencies issued more regulations. The reason for this is simple: Democrat-controlled legislatures were more likely to pass laws that required regulatory action by agencies. No changes to the regulatory process can outweigh that factor.

Politics and 'reform' / We have had more than 30 years of experience on the federal level of continuous changes to the regulatory process. You would think that, by now, legislators and executives would have learned that procedural changes aren't going to have a significant influence on agency regulatory decisions. So why do lawmakers keep implementing such changes?

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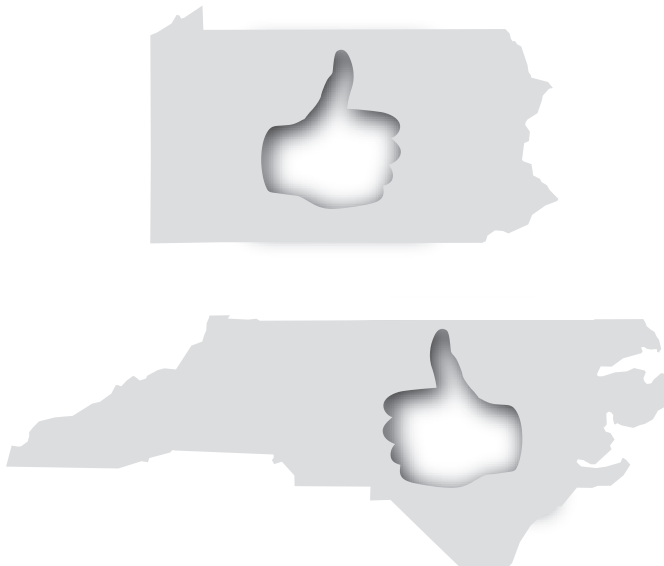

In our recent book, *The Politics of Regulatory Reform*, we sought to answer that question.

After examining a number of possible explanations for regulatory reform and finding them wanting, we turned to a detailed case study of two states where regulatory reform has been the norm over the past three decades. Arguably, the regulatory processes in Pennsylvania and North Carolina are more complex and have more veto points than even the federal process. Both states have examples of legislative review of regulations, executive review of regulations, and requirements for economic analysis. Both states also have quasi-independent regulatory review bodies: the Rules Review Commission (RRC) in North Carolina and the Independent Regulatory Review Commission (IRRC) in Pennsylvania.

Both states share another important property: they have experienced three roughly simultaneous "surges" of regulatory reform. In the early 1980s, Pennsylvania set up regulatory review procedures within the executive branch, in both the Attorney General's Office and the Office of General Council (OGC). Pennsylvania also created the IRRC. Meanwhile, in North Carolina, the RRC was created after an aborted attempt to house regulatory review in the legislature.

The early to mid-1990s saw the next surge of regulatory reform. In Pennsylvania, that took the form of establishing review in the Governor's Office via executive order. In North Carolina, a legislative review process was created and the first requirements for economic analysis of regulation were instituted. Both states then remained relatively quiet until the late 2000s, when numerous regulatory reform proposals were brought before the two state legislatures. Gov. Bev Perdue (D) strengthened executive branch review in North Carolina and the legislature followed in its current session by enacting a series of new requirements for regulatory agencies. In Pennsylvania, the latest wave of regulatory reforms resulted in an increase in the number of impact statements required, and a number of regulatory reform bills are still being considered.

The first thing to notice about the pattern of regulatory reform in the two states is that all three waves took place during economic downturns. That roughly mirrors the enthusiasm for regulatory reform at the federal level. We hypothesized that this timing is far from coincidental. Incumbent political officeholders know that one of the most important factors that voters use to judge them is the state of the economy (and, relatedly, the voters' own economic well-being). However, the number of steps that most incumbents can take to affect the economy is limited. So they need to convince their constituents that they are doing something.

As a result, many politicians look for a scapegoat for poor economic conditions and many settle on regulation. One might ask, if regulation is to blame for poor economic conditions, then why don't legislators work on *repealing* regulations? While some take that step, it is a politically risky strategy. Removing regulations designed to protect public health or the environment exposes an incumbent to attacks from advocates for those causes. Furthermore, existing regulations may actually have support in the incumbent business community because they serve as a barrier to entry for new firms.

But regulatory reform is a way to seemingly respond to poor economic conditions by attacking regulation without bearing the political costs of doing so. By the time anyone can judge whether or not the reforms are effective, the sponsors of the reforms have been taking credit for them for years (and hopefully the economy has improved!). In addition to the timing of regulatory reform in the two states, interviews with former and current legislators and executive branch employees helped corroborate this hypothesis. Repeatedly, they referred to poor economic conditions at the time of enactment and the "need to do something."

But there is more to the desire to enact regulatory reforms than this form of "credit claiming." Regulatory reforms also provide an innovative way for political officeholders to perform constituent service. The evidence for this argument comes not so much from stories about the enactment of the regulatory reforms in Pennsylvania and North Carolina, but from the ways the reforms were used once they were in place. In both states, politicians used the institutions created by regulatory reforms to intervene on behalf of constituents during particular regulatory proceedings.

One story from Pennsylvania is particularly instructive: An IRRC commissioner told us that the agency "absolutely can be a shelter for the legislature. By writing a letter to the IRRC, it is a great way of showing a constituent 'I am fighting for you.' It makes the constituent happy." He then shared this encounter:

> I once got a letter from a legislator and I happened to run into him at an event and mentioned that I had received his letter and was taking his concerns very seriously. He then told me: 'Don't worry

about what's in the [letter]. I don't care what you do.' He was actually surprised I was taking it seriously.

All the legislator cared about was the appearance that the letter conveyed to his constituent.

Interest group representatives confirmed this notion. They readily disclosed how, upon being faced with failure at the agency level to get their concerns heard, they would contact sympathetic legislators and ask them to assist by filing a comment or appealing to the independent rule review authorities. Those authorities often had "legislative intent" as one of the concerns they were statutorily bound to evaluate, and therefore a letter from a legislator was very useful.

Revenge of the political scientists / As we started out this research, we had few prior beliefs about the motivations for regulatory reform. But as we studied the futility of many of the reforms and talked to the legislators and executive branch officials responsible for their enactment, we thought back to classic political science works we read in graduate school. In particular, two works from the 1970s—David Mayhew's *Congress: The Electoral Connection* and Morris Fiorina's *Congress: Keystone of the Washington Establishment*—seemed to do more to explain regulatory reform than many of the explanations given by advocates on either side of the issue.

Mayhew argued that politicians (he focused on Congress, but the conclusions are broadly applicable) pursue reelection in three ways: The first is "credit-claiming," and Mayhew offers an excellent summary of how proponents of legislation use their advocacy to buttress their credentials for improving the economy during economic downturns. The recent wave of more than 20 regulatory reform measures before Congress provides additional evidence for this motivation.

The second way politicians pursue reelection is through constituent service. Fiorina expanded upon this idea in his book, arguing that Congress created bureaucracies that would naturally, on some occasions, frustrate their constituents. When those frustrations occurred, constituents would then turn to their elected representatives, who could secure the voters' undying gratitude by intervening on their behalf. Fiorina was describing the social welfare bureaucracies that allocate benefits, but his logic applies equally to regulatory bureaucracies. Regulatory reforms, as seen in Pennsylvania and North Carolina, are used by incumbent politicians to help (or to give the appearance of helping) constituents and potential donors who voice complaints about regulatory proposals.

We want to emphasize that playing a political role is not necessarily a bad thing. In a democracy, facilitating involvement by elected officials in decisions made by unelected officials has clear benefits. But regulatory reforms need to be understood in this way, not as improving efficiency, reducing burden, or the many other rhetorical flourishes that often accompany their proposal. The politics of regulatory reform is far more about politics than about regulation. *R*

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The Obamacare Regulatory Rush

BY SAM BATKINS AND IKE BRANNON

There is plenty of evidence that rushing through the rulemaking process results in poor analysis and shoddy policy outcomes. Nowhere is that more clearly manifested than in the Patient Protection and Affordable Care Act (PPACA, also known as Obamacare), the Obama administration's signature policy achievement.

Since its passage in early 2010, the administration has rushed PPACA regulations through the Office of Information and Regulatory Analysis (OIRA)—the entity tasked with reviewing regulations for soundness—at a breakneck pace, often with merely perfunctory analysis. The result of those pell-mell efforts is displayed almost daily before the public with corrections, delays, and botched rollouts.

When the administration began implementing PPACA, it issued a set of interim final rules that sailed through OIRA, which typically serves the White House by anticipating costly or problematic details in proposed regulations. However, when it came to PPACA, OIRA review apparently was perfunctory. Mercatus Center scholars Christopher Conover and Jerry Ellig documented in their 2012 paper "The Poor Quality of Affordable Care Act Regulations" how six prescriptive ACA regulations fared poorly on critical analytical metrics compared to other health care and Homeland Security regulations. Conover and Ellig suggested that the poor PPACA analysis was rooted in presidential priorities: the administration wanted the

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regulations out the door, and there was little OIRA—considered a minor agency in the Executive Office of the President—could do to ensure proper analysis. Now the administration is paying the price for that lax oversight.

PPACA's rollout has had more than its share of flubs and failures: a dysfunctional website, broken regulations, higher premiums, and cancelled plans. It has led some commentators to wonder how so many mistakes could pile up. The answer to that lies in the OIRA review data, which indicate that White House fast-tracked many PPACA regulations, including rushing through 27 rules without any formal review.

Table 1

AVERAGE REVIEW TIME FOR PPACA REGULATIONS

2010–2013

Type	Average Review Time	Average Time for Significant Rules
All Rules	74	70
EPA Rules	95	63
PPACA Proposed Rules	33	30
PPACA Final Rules	29	20
PPACA Corrected Proposals	8	N/A
PPACA Corrected Rules	4	N/A

Since 2010, the average OIRA review time for a typical rule has been 74 days. But the average review time for a PPACA final rule was just 29 days. "Economically significant" PPACA final rules (those with an annual compliance cost of $100 million or more) got even less scrutiny—just 20 days.

No other executive branch agency has review times anywhere near that brief. For example, Environmental Protection Agency proposed and final rules averaged 95 days of review; even Department of Education final rules averaged 47 days (the second fastest of all the sets of rules, behind the PPACA rules). Put bluntly, the administration—as a matter of course—spent noticeably less time scrutinizing PPACA regulations than other rules.

Perhaps more worrisome, the disparity in review times between PPACA regulations and all others has widened in the last several months. Since 2012, the average rule was under OIRA review for 110 days, and 97 days for those deemed economically significant. Yet PPACA reviews took on average between 20 and 33 days. It is clear the administration greased the tracks for many health care regulations.

White House inattention / The PPACA rollout has resulted in numerous missteps. For example, approximately one-third of all PPACA regulations contained errors, forcing the administration to issue corrective documents. Some of the errors that have come to light so far have been typographical in nature, but others have been substantive. In total, 286 errors in original PPACA regulations have been identified, requiring 140 pages of amended rulemakings solely devoted to correcting rushed regulations.

It is easy to see how those errors occurred. The White House appears to have given little if any oversight of the rulemakings. The average review time for an erroneous proposed health care rule was just eight days; the median time was zero days. Some 18 proposed rules and 16 final rules that subsequently needed fixing received no official White House review.

There have been more than 100 PPACA regulations issued since the law's passage, so perhaps we can cut the administration some slack. However, the data reveal the administration failed to review seven *significant* PPACA proposals, including measures to amend Medicare Advantage and to implement Medical Loss Ratios. The administration also failed to review six significant PPACA final rules, including amendments to the Medicare Prescription Drug Benefit Program.

The troubled health care exchange rollout bears special scrutiny. The Department of Health and Human Services submitted for review four significant proposed rules concerning exchanges. OIRA review of those proposed rules averaged a mere 16 days. (Final exchange rules averaged 36 days of OIRA review, which is better than 16 but still much shorter than average.) For an example of the poor exchange analysis, the administration initially estimated that individuals navigating the federal health care exchange would spend less than 30 minutes on the website. Obviously, that estimate hasn't fared well.

The White House has also failed to release any documents suggesting changes or material alterations to the exchange regulations. Under Executive Orders 12866 and 13563 (the latter issued by President Obama himself), agencies must "Identify for the public those changes in the regulatory action that were made at the suggestion or recommendation of OIRA." In all instances, OIRA listed exchange regulations as "Consistent with Change," indicating that OIRA did make suggestions or recommendations. Yet the White House and HHS have failed to release redline documents of any amendments to exchange regulations. For a White House that criticized its predecessor for a lack of regulatory transparency, such behavior is disappointing.

Conclusion / Passing a law does not conclude the policymaking process. For legislation as complex as PPACA, there are literally hundreds of regulations that an administration must issue in order to ensure that the law does what it is intended to do. It can be tedious, unexciting work, but an administration must give it full attention in order for the law to operate.

Concerning its signature policy achievement, the Obama administration has been surprisingly careless in that work, at least until the full magnitude of the exchange failure came to light and a political price had to be paid for the inattention. We expect that more regulatory failures will emerge as PPACA continues to be implemented. R

The Benefit Corporation: Statutory Barriers to Adoption

BY THOMAS A. HEMPHILL AND FRANCINE CULLARI

Since 2010, several state legislatures have enacted laws recognizing the "benefit corporation," a variant of the traditional legal form of the American public corporation. Advocates of the benefit corporate form argue that it protects "social entrepreneurs" from shareholder suits by legally permitting firm managers to consider "social benefits" beyond maximizing shareholder value when making business decisions. *Forbes* magazine, whose editors assembled its first "Impact 30" list of the world's top social entrepreneurs in 2011, offers a succinct definition of a for-profit social entrepreneur: "a person who uses business to solve social issues."

A state's benefit corporation statute is located within existing corporation law. However, the benefit corporation typically is given three explicit exceptions to that law:

- The firm has a corporate purpose to create a material positive impact on society or the environment.
- The firm's directors have expanded fiduciary duties that require consideration of nonfinancial interests.
- The corporation has an obligation to report on its overall social or environmental performance as assessed against a comprehensive, credible, independent, and transparent third-party standard.

As of February 2014, the Benefit Corporation Information Center (BCIC)—part of B Lab, a nonprofit organization whose purpose is to use "the power of business to solve social and environmental problems"—lists on its website 20 states and the District of Columbia as having adopted benefit corporation legislation. The BCIC adds that another 16 states are considering adoption.

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Benefit corporation statutes vary from state to state, depending on the individual characteristics of each state's business entity statutory scheme and input from legislators, state bar associations, practitioners, the business community, and other relevant stakeholders. However, the essential provisions are constant across jurisdictions.

Benefit corporations are required to have a purpose of creating "general public benefit" and are permitted to identify one or more "specific public benefit" purposes. Model legislation available from the BCIC lists seven nonexhaustive possibilities for specific public benefits: provide low-income or underserved individuals or communities with beneficial products or services; promote economic opportunity for individuals or communities beyond the creation of jobs in the ordinary course of business; preserve the environment; improve human health; promote the arts, sciences, or advancement of knowledge; increase the flow of capital to entities with a public benefit purpose; or accomplish any other particular benefit for society or the environment.

Motivation / According to William H. Clark and Larry Vranka, principal authors of an American Bar Association white paper evaluating the legal need for benefit corporation statutes, many social entrepreneurs of publicly traded companies who decide to expand their business operations face resistance from both executives and board members. The managers favor the fiduciary responsibility of shareholder primacy theory when considering investments, acquisitions, mergers, or liquidity options. The social entrepreneurs thus have an omnipresent fear of investor-driven pressure to alter business practices or strategy away from the social mission of the company. Allegedly, both the prevailing profit-maximization business culture and the advice of corporate counsel regarding the risk of shareholder litigation have created a "chilling" business environment for social entrepreneurs who wish to pursue a social mission as an integral component of a profit-driven enterprise. Besides the stories of investor-driven takeovers by boards dissatisfied with company financial performance, one vivid example of such fears is the forced sale of the mission-driven ice cream maker Ben & Jerry's a few years ago.

Interestingly, Cornell law professor Lynn Stout argued in a recent finance journal article:

> The business judgment rule ensures that, contrary to popular belief, the managers of public companies have no enforceable legal duty to maximize shareholder value. Certainly they can choose to maximize profits, but they can also choose to pursue any other objective that is not unlawful, including taking care of employees and suppliers, pleasing customers, benefiting the community and the broader society, and preserving and protecting the corporate entity itself. Shareholders primacy is a management choice—not a legal requirement.

Moreover, as Mark Underberg, a retired partner at the law firm of Paul, Weiss, Rifkind, Wharton & Garrison, noted a couple of years ago, "I am not aware of a single case holding directors liable for a routine business decision because they considered non-shareholder interests or that impose a general duty to maximize profits and short-term shareholder value." While the most recent legal exposition of shareholder primacy theory found in the complex 2010 case *eBay v. Newmark* from the Chancery Court of Delaware may have provided further legal support for the shareholder maximization perspective, the lack of evidence in the case law does not support the argument for benefit corporation statutes to be enacted. The statutes are apparently being enacted prophylactically, as a result of the perceived legal and marketing fears of mission-driven, for-profit social entrepreneurs.

Primary statutory provisions / According to the model legislation that is often used to draft benefit corporation acts, corporate directors may consider the interests of shareholders, employees, customers, suppliers, the community, and the local and global environment, as well as short- and long-term interests useful to accomplishing the firm's general benefit purpose and any specific public benefit purpose. Furthermore, the benefit corporation statutes allow directors to consider other pertinent factors or the interests of any other group that they deem appropriate. The model act legislation states that the consideration of all stakeholders will not constitute a violation of the general duties and responsibilities of directors, thus explicitly restricting corporate liability and the liability of directors and officers for monetary damages from shareholder suits. Benefit corporation directors are protected from litigation by beneficiaries of the corporation's public purpose. A shareholder, however, is expressly given the right to bring legal action against a director or officer who fails to pursue or create the stated general or specific public benefit purposes, fails to consider the interests of the various stakeholders listed in the statute, or fails to meet the transparency requirements in the statute.

A benefit corporation is required to issue an annual benefit report to shareholders. The report is to be posted on the firm's website and filed with the incorporating state. The report must contain a narrative describing how it pursued its general—and any specific—public benefit and include an assessment of its overall social and environmental performance against a third-party standard.

Adoption barriers / In spite of its recent popular appeal among state legislatures, the benefit corporation is potentially confronted by looming statutory barriers to widespread adoption by businesses contemplating this form of incorporation. One barrier is the statutory requirements to report on how the corporation has performed in meeting its overall social and environmental performance against a third-party standard. Such a reporting requirement will inevitably restrict both the board and management in executive decisionmaking when considering opportunities and responding to threats, because company resources need to be allocated among a variety of stakeholders and their attendant issues. Social entrepreneurs, like other entrepreneurs, need flexibility and adaptability in their managerial decisionmaking to meet traditional business goals and objectives, rather than being statutorily bound to meeting fixed financial or other business performance goals established in their benefit incorporation documents—say, for example, donating 20 percent of pretax annual earnings to nonprofit charities. Furthermore, the benefit corporation shareholders have the legal standing to bring a civil suit against board members and executives who do not meet the stated "public benefits" contained in the state's enabling statute. Also, state government regulators are charged with identifying a third-party standard for annual audit purposes. At this time, there appears to be no consensus as to which third-party standards are acceptable, nor which organizations are qualified to provide independent, third-party standard certification.

A second barrier concerns stakeholder credibility. If a legally designated benefit corporation is not meeting statutory requirements for maintaining benefit corporation status, will state governments rescind its legal status? If thousands of firms choose this designation, will state governments have regulatory systems in place to effectively enforce the maintenance of this legal status? What about due process for appealing the rescission of benefit corporation status? Will additional annual fees (above statutory audit requirements) need to be assessed by state governments against companies that choose this legal form? Because these companies are incorporated at the state level and there are differences in each state's incorporation laws, being a "benefit corporation" does not have the same meaning for all such legally designated corporations. Thus, from the standpoint of the consumer and other stakeholders, will there need to be a supplemental third-party certification designation to compare companies' performance on an "apples-to-apples" basis (i.e., as to the breadth and depth of their social and environmental commitment)? Those important accountability questions remain unresolved.

A third barrier is the potential for a "race to the bottom" by the states that do not have benefit corporation statutes. Critics of existing benefit statutes are already concerned that there is far too much leeway given to boards and management as to which business decisions must consider social and environmental effects. Concerning board responsibility for achieving social and environmental performance goals and objectives, some benefit statutes—such as those in Colorado and Massachusetts—do not require an independent benefit director to internally monitor company business practices. To attract state revenue from incorporations and appease legislative critics of the benefit statute concept who may delay or block such statutes from being successfully enacted, it is possible that fewer or more lenient accountability requirements will be incorporated into future state legislation. Nationwide, this can lead to even further confusion among consumers and other stakeholders about what constitutes a "benefit corporation." The scenario could also increasingly discourage startup firms from choosing the benefit corporation legal form, as the effort to distinguish themselves from benefit corporations in other states becomes increasingly problematic, not to mention costly.

Regulatory arbitrage misuse? / A few years ago, University of San Diego law professor Victor Fleischer defined regulatory arbitrage as an activity that "exploits the gap between the economic substance of a transaction and its legal or regulatory treatment, taking advantage of the legal system's intrinsically limited ability to attach formal labels that track the economics of transactions with sufficient provision." In the case of regulatory arbitrage related to company incorporation strategy, there has been no empirical evidence showing "misuse" of the incorporation choices offered to companies in the 20 states where benefit corporation statutes have been enacted. Could such misuse be occurring? Yes, but as mentioned above, the lower regulatory or legal costs of operation for a company are likely to rest with the traditional form of for-profit incorporation and not the benefit form of incorporation.

A point to consider when addressing regulatory arbitrage misuse is that a social entrepreneur (or existing nonprofit corporation) that chooses to form (or convert to) a benefit corporation is expected to have altruistic motives. If it does, the benefit corporation will not be looking to avoid a regulatory scheme or use it to an advantage other than that directed by statute. On the other hand, a corporation could elect the benefit form strictly for public relations purposes, with no intent to offer anything more than "lip service" to the stakeholders it chooses to benefit. Those stakeholders typically have no standing to sue under the benefit corporation statutes. They would have to rely on shareholders to defend their cause, or purchase enough shares to become significant shareholders themselves.

While the trend toward states adopting the benefit corporation appeared to have picked up momentum through 2013, there also appears to be some recent reluctance on the part of many state legislatures to expedite the process of enacting such statutes. As seen in the foregoing discussion, there are significant business and public policy issues that need to be resolved before the full potential for benefit corporation statutes can be accurately gauged by social entrepreneurs who may be interested in adopting this corporate form. R

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