

# COMPENSATING A PUBLIC BENEFIT CORPORATION

Sung Eun (Summer) Kim\*

## I. INTRODUCTION

At a time when more entrepreneurs desire to dedicate their time, talents, and resources to ventures that pursue social and environmental purpose alongside profit,<sup>1</sup> Professor Michael Dorff’s *Becoming a Public Benefit Corporation*, (“*Becoming a PBC*”) provides a timely, important, and comprehensive overview of two business forms that facilitate such pursuits in the United States—benefit corporations and public benefit corporations.<sup>2</sup> A company that is formed as a benefit corporation (BC) must specify in its charter the specific public benefit it seeks to advance, and a public benefit corporation (PBC) is the version of the BC that is offered in the state of Delaware (BCs and PBCs are collectively referred to here as “BC/PBCs”).

Professor Dorff provides a balanced view on both the promises as well as the limitations of BC/PBCs. To begin with their strengths, BC/PBCs are subject to legal duties and requirements that can be used to signal an entity’s legal commitment to consider the interests of stakeholders other than shareholders. Furthermore, the BC/PBC form ensures that these commitments are preserved even if the ownership of a BC/PBC changes hands.<sup>3</sup> In addition, BC/PBCs are excellent purpose *reinforcement* tools.<sup>4</sup> BC/PBC statutes create an opportunity for boards of directors to identify,

---

\* Professor of Law, University of California, Irvine, School of Law. I am grateful to Cassidy Hunt (Harvard Law School, Class of 2026) and Piper Hinson (*Editor-in-Chief*, Southwestern Law Review 2024-25) for their outstanding research and editorial assistance and to Professor Michael Dorff and the other contributors to this symposium issue for inspiring new ideas on how our legal system can keep up with corporations’ desires to serve the public benefit.

1. WORLD ECON. F., *The State of Social Enterprise: A Review of Global Data 2013–2023* 4 (2024), [https://www3.weforum.org/docs/WEF\\_The\\_State\\_of\\_Social\\_Enterprise\\_2024.pdf](https://www3.weforum.org/docs/WEF_The_State_of_Social_Enterprise_2024.pdf) (reporting an estimated 10 million social enterprises globally, collectively generating around \$2 trillion in annual revenue and creating nearly 200 million jobs).

2. MICHAEL B. DORFF, *BECOMING A PUBLIC BENEFIT CORPORATION* (2024) [hereinafter *BECOMING A PBC*].

3. *Id.* at 2-3.

4. *Id.* at 5, 125 (“[A]lthough the statutory mechanisms are imperfect enforcement tools . . . they are excellent reinforcement tools.”).

articulate, and reflect upon the specific public benefit their company seeks to pursue,<sup>5</sup> and this allows the entity's stakeholders to better understand and evaluate the company.<sup>6</sup>

However, as Professor Dorff also notes, BC/PBCs are not particularly effective *enforcement* tools, at least in their current form. This is because while BC/PBC statutory mechanisms encourage and facilitate decisions that are not otherwise available to traditional business forms, they do not require any particular outcomes.<sup>7</sup>

Furthermore, as with any legal innovation, the BC/PBC form creates an opportunity for actors to misuse the form. Indeed, the main concern with the BC/PBC form that is addressed in *Becoming a PBC* is purpose washing, which is defined as “appearing purpose-driven without bearing the costs of actually pursuing a social purpose.”<sup>8</sup> *Becoming a PBC* offers practical guidance and useful insights on how litigation, disclosure, third-party certification, non-profit governance, charter amendments, appointing benefit directors (and benefit officers) and going public can mitigate,<sup>9</sup> but not necessarily eradicate,<sup>10</sup> purpose washing. In this essay, I offer compensation structures as yet another governance mechanism that can be used to counteract purpose washing.

## II. EVALUATING COMPENSATION PRACTICES IN PUBLIC BENEFIT CORPORATIONS

This essay examines the relationship between executive compensation and purpose washing, focusing on a recent trend that has emerged among BC/PBCs. Referred to here as “ESG/CSR-based performance pay,” this type of compensation looks to environmental, social, and governance (ESG) and corporate social responsibility (CSR) metrics (e.g., employee wellbeing, CO<sub>2</sub> emissions, and improved board diversity) as benchmarks for executive pay. ESG/CSR-based performance pay is a relatively recent practice that has

---

5. *Id.* at 82 (“[T]he act of self-consciously identifying the specific public benefit . . . may encourage self-reflection that can lead to positive changes . . . by the board.”).

6. *See id.* (explaining how the requirement to specify a BC/PBC’s public benefit also helps stakeholders evaluate the company).

7. *Id.* at 57.

8. *Id.* at 100-01.

9. *See id.* at 192 (“The public nature of [publicly-traded PBCs] . . . may reduce PBCs’ ability to purpose wash.”).

10. *Id.* at 112 (“Neither lawsuits to enforce boards’ balancing duty nor the disclosure requirements seem likely to prevent purpose washing.”); *id.* at 124 (“BC and PBC statutes do not provide adequate enforcement tools to ensure that these entities actively pursue their social goals.”); *id.* at 181 (“Although the statutes require transparency and a degree of measurability, they do not provide for rigorous enforcement[.]”).

become prevalent among certain companies, including BC/PBCs. Adam Badawi and Robert Bartlett reviewed the extent to which S&P 500 firms linked executive compensation to ESG performance during the 2023 proxy season and found that 63% (315 firms) of the firms they reviewed had an ESG component in their executive compensation.<sup>11</sup>

This trend is a departure from the conventional compensation practice of looking solely to stock price movement and other financial metrics as benchmarks for executive pay (which is referred to here as “stock-based performance pay”). In this essay, I evaluate how ESG/CSR-based performance pay is an important, yet incomplete, alternative for stock-based performance pay, relying on a conceptual framework developed by Professor Michael Dorff. I also examine the ways in which ESG/CSR-based performance pay can, with appropriate disclosures, mitigate purpose washing.

An evaluation of executive pay must draw upon another one of Professor Dorff’s influential books, *Indispensable and Other Myths: Why the CEO Pay Experiment Failed and How to Fix It*, (“*Indispensable*”).<sup>12</sup> In *Indispensable*, Professor Dorff explains how stock-based performance pay started to emerge in the late 1970s and took hold in the 1980s.<sup>13</sup> Interestingly, despite widespread criticism of stock-based performance pay and the lack of empirical evidence showing that such compensation practices lead to higher stock prices, stock-based performance pay is still the dominant form of compensation for chief executive officers (CEOs) in the United States today.<sup>14</sup>

Professor Dorff offers a behavioral theory to explain this disconnect between evidence and reality. He finds that CEO performance tends to be difficult to measure, and the perceived ease of measuring performance using stock price provides an illusion of validity, clarity, and control.<sup>15</sup> However, Professor Dorff warns that these benefits are only illusory, and instead calls for reforms to compensation structures that can lead to actual, tangible benefits. In *Indispensable*, Professor Dorff argues that to be effective, compensation practices must be tied to factors that are: (1) within an officer’s

---

11. Adam B. Badawi & Robert P. Bartlett, *ESG Overperformance? Assessing the Use of ESG Targets in Executive Compensation Plans* (Stanford L. & Econ. Olin Working Paper No. 592, 2024), [https://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=4941016](https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4941016).

12. MICHAEL B. DORFF, *INDISPENSABLE AND OTHER MYTHS: WHY THE CEO PAY EXPERIMENT FAILED AND HOW TO FIX IT* (2014) [hereinafter *INDISPENSABLE*].

13. *Id.* at 6-7.

14. *See id.* at 9 (“[E]quity-based pay . . . is highly unlikely to result in higher stock prices . . .”).

15. *Id.* at 10.

control, (2) difficult to manipulate, (3) easy to measure, and (4) important to a corporation's long-term goals.<sup>16</sup>

In the balance of this part, I evaluate ESG/CSR-based performance pay through this four-factor framework from *Indispensable*. This analysis reveals that while ESG/CSR-based performance pay meets only some (but not all) of *Indispensable*'s best practices criteria, it does comparatively better than stock-based performance pay in some important respects.

***Indispensable* Factor 1: Is ESG/CSR-based performance pay tied to factors within an officer's control?** The answer to this question depends on the particular factors that are used to determine ESG/CSR-based performance pay. For example, imagine a PBC that would like to award its CEO based on the company's successful implementation of ESG policies. One method to measure and reward success might be to award the CEO a bonus if a committee of ESG experts rates the company's ESG policies as better than its peers for three consecutive years. Another method to measure and reward success might be to award the CEO a bonus if the company has a designated ESG officer on the management team for three consecutive years. Between these two methods, it could be said that the second method is more within an officer's control than the first method.

In the context of stock-based performance pay, stock prices are contingent on a range of factors, many of which are outside an officer's control. In this regard, it can be said that ESG/CSR-based performance pay practices are superior to stock-based performance pay when it comes to the ease of designing the compensation structure to be tied to factors that are within the compensated officer's control.

***Indispensable* Factor 2: Is ESG/CSR-based performance pay tied to factors that are difficult to manipulate?** The goal of tying one's pay to specified metrics is to incentivize desired outcomes.<sup>17</sup> An unfortunate byproduct of incentive pay is that it can motivate the compensated individual to exaggerate or manipulate metrics without achieving the desired outcome. The options backdating scandal of the mid-2000s, which revealed that thousands of American companies had backdated their stock options to inflate executive pay, is an example of such manipulation in the context of stock-based performance pay.<sup>18</sup>

---

16. *Id.* at 12-13.

17. JERRY Z. MULLER, *THE TYRANNY OF METRICS* 17 (2018) (citing management guru Tom Peters: "What gets measured gets done.").

18. See, e.g., Jesse M. Fried, *Option Backdating and Its Implications*, 65 WASH. & LEE L. REV. 853 (2008).

In *The Tyranny of Metrics*, Jerry Muller explains how our reliance on metrics necessarily creates a culture of gaming and manipulation.<sup>19</sup> This includes tendencies to distort information by relying on inputs that are most easily measurable and disregarding caveats, ambiguities and uncertainties.<sup>20</sup> The results can have deleterious effects on both the individual being evaluated and the people and mission that the individual serves.<sup>21</sup> Furthermore, forcing or incentivizing people to conform their work to numerical goals can stifle innovation and creativity.<sup>22</sup> Indeed, in *Indispensable*, Professor Dorff points to how stock-based performance pay erodes intrinsic motivation.<sup>23</sup>

As ESG/CSR-based performance pay also looks to measurable indicators to determine executive pay, it is similarly susceptible to these pernicious effects of metrics fixation. To avoid some of these pitfalls, ESG/CSR-based performance pay practices must be accompanied by a periodic evaluation of whether what is being measured is a reasonable proxy for desired outcomes.

Returning to our earlier example of the PBC that seeks to align some aspects of executive pay with the company's implementation of ESG policies, the manipulability of the relevant inputs will depend on how they are defined and measured. If the pay formula is tied to whether a committee of ESG experts rates the company's ESG policies as better than its peers, the compensation committee (or other body that is responsible for designing and implementing ESG/CSR-based performance pay) should evaluate the competence of this committee and its independence from the compensated individual.

***Indispensable Factor 3: Is ESG/CSR-based performance pay tied to factors that are easy to measure?*** It is notoriously difficult to measure impact. Even as calls to move toward stakeholder capitalism have grown louder, the indeterminacy of stakeholder value relative to shareholder value has been a barrier to implementing these shifts.<sup>24</sup> In particular, one obvious

---

19. MULLER, *supra* note 17, at 126.

20. *Id.* at 23.

21. *Id.* at 24-25.

22. *Id.* at 20.

23. INDISPENSABLE, *supra* note 12, at 10.

24. See Caroline Flammer, Bryan Hong & Dylan Minor, *Corporate Governance and the Rise of Integrating Corporate Social Responsibility Criteria in Executive Compensation: Effectiveness and Implications for Firm Outcomes*, 40 STRATEGIC MGMT. J. 1097, 1101 (2019); Sung Eun ("Summer") Kim, *The Duality of Variance Among ESG Assessments*, 88 MO. L. REV. 409, 448 (2023).

criticism of ESG/CSR-based performance pay is that these compensation policies lack substance and can be merely symbolic.<sup>25</sup>

Fortunately, new efforts and innovations are emerging in this area, especially among impact funds, which are private equity funds that seek to generate social and/or environmental impact alongside financial returns.<sup>26</sup> For example, SWEN Capital Partners, which announced a fund that aims to accelerate investments in renewable gas, has developed a bespoke impact methodology, referred to as the Net Environmental Contribution (NEC) metric, to calculate its progress toward its carbon footprint targets.<sup>27</sup> The NEC metric is an open-source measurement system developed to track the environmental impact of economic initiatives on climate, water resources, waste, air quality, and biodiversity.<sup>28</sup>

These efforts underscore the value and importance of industry-wide collaborations, impact consultants, independent assurance auditors, and third-party compensation experts who can improve how companies formulate, validate, and enforce their impact methodologies and related ESG/CSR-based performance pay outcomes. While measurability is one dimension on which ESG/CSR-based performance pay lags behind stock-based performance pay, measurability can be improved in this regard over time and with more practice.

**Indispensable Factor 4: Is ESG/CSR-based performance pay tied to factors that are important to a corporation's long-term goals?** ESG/CSR-based performance pay is praised for its ability to align managerial performance with a corporation's long-term goals. Caroline Flammer and her co-authors found that ESG/CSR-based performance pay shifts managers' attention toward longer-term efforts across longer-term horizons and also leads to an increase in firm value, an increase in social and environmental initiatives, a reduction in emissions, and an increase in green innovations.<sup>29</sup>

25. See, e.g., Flammer et al., *supra* note 24, at 1101.

26. The industry standard for compensation of private equity fund managers has been “two and twenty”: a management fee of two percent of the capital investors have committed and a performance fee (also referred to as the “carry”) of twenty percent of the profits of the fund. As managers of impact funds are expected to generate social and/or environmental impact alongside financial returns, some impact funds are tying a portion of the general partner's carry to social and/or environmental impact (also referred to as the “impact carry”). GLOB. IMPACT INVESTING NETWORK, *Impact-Based Incentive Structures: Aligning Fund Manager Compensation with Social and Environmental Performance* 1 (2011), [www.thegiin.org](http://www.thegiin.org).

27. Preeti Singh, *Metrics Play Key Role as Private-Equity Firms Link Profits to Impact*, WALL ST. J., (Dec. 8, 2021), <https://www.wsj.com/articles/metrics-play-key-role-as-private-equity-firms-link-profits-toimpact-11639000607>.

28. SYCOMORE AM, *A Responsible and Engaged Asset Manager*, <https://en.sycomore-am.com/responsible-approach> (last visited Sept. 18, 2024).

29. Flammer et al., *supra* note 24, at 1101.

In this regard, the emergence of ESG/CSR-based performance pay offers a promising alternative to overcome some of the short-termism associated with stock-based performance pay.

Another innovative aspect of ESG/CSR-based performance pay is that some entities have chosen to redistribute any unearned ESG/CSR-based performance pay to organizations that are aligned with their long-term goals. For example, Core Innovation Capital, a \$50 million fund that seeks to provide low and moderate-income consumers with access to financial services, has committed to distribute the share of compensation that could have been, but is not, ultimately paid to its general partner to a nonprofit organization dedicated to achieving social impact (this practice is referred to as an “impact hedge”).<sup>30</sup> The impact hedge contrasts with other funds’ common practice of returning any unearned compensation to its investors.<sup>31</sup>

One limitation of current practices in ESG/CSR-based performance pay is that they make up too small a piece of the entire compensation picture to make a meaningful difference. As ESG/CSR-based performance pay practices evolve and improve, however, these new compensation practices are expected to become a more significant part of executive compensation, especially among BC/PBCs. This will, in turn, require additional guidance on how companies should collect and report data on these compensation practices. The balance of this essay examines how BC/PBC compensation disclosure policies can be improved to advance the three core values emphasized throughout *Becoming a PBC*—transparency,<sup>32</sup> credibility,<sup>33</sup> and measurability.<sup>34</sup>

### III. DISCLOSING COMPENSATION PRACTICES IN PUBLIC BENEFIT CORPORATIONS

As Professor Dorff explains in *Becoming a PBC*, there are several shortcomings to the current BC/PBC disclosure regime.<sup>35</sup> For one, the rules that govern benefit reports are quite loose,<sup>36</sup> and more concerningly, even

---

30. GLOB. IMPACT INVESTING NETWORK, *supra* note 26, at 4, 8.

31. *Id.* at 6.

32. BECOMING A PBC, *supra* note 2, at 175.

33. *Id.* at 176.

34. *Id.* at 177.

35. *Id.* at 111.

36. *Id.* at 109-12 (explaining that both the Model Act and Delaware law require BC/PBCs to report periodically on how the company is performing its social purpose).

these rules are not being adequately enforced.<sup>37</sup> In reality, benefit reports have been used more as a marketing tool, rather than a disclosure tool.<sup>38</sup>

When it comes to compensation, the Model Benefit Corporation Legislation (the Model Act) requires companies to report the compensation paid to each director for her services as director.<sup>39</sup> Neither the Model Act nor the B Lab, which developed the Model Act, specify the details or best practices of compensation-related disclosures. In fact, the B Lab only recommends but does not require the identification of compensation to directors and benefit directors.<sup>40</sup> Even the states that require the disclosure of compensation for benefit corporations do not require compensation-related information to be included in the publicly available version of their benefit reports.<sup>41</sup>

BC/PBCs should be required to describe both the substance as well as the process of the compensation of benefit directors and benefit officers (if any) and other executive employees who are compensated with ESG/CSR-based compensation pay.

Substantively, a BC/PBC should explain how its compensation policies align with its articulated purpose. While compensation is not a silver bullet, it has important implications for how corporate strategies are set and implemented. Hanna Basra reports that executive compensation practices at several PBCs do not align with the PBC's articulated purpose,<sup>42</sup> which may be evidence of purpose washing.<sup>43</sup> Going further, evidence of misalignment could be the basis of benefit enforcement proceedings, which are a purpose-enforcement mechanism that allows shareholders to sue to require disclosure of the company's advancement toward its social mission and to enforce the

37. *Id.* at 111 (“[T]he rules that govern these reports’ content are quite loose, and . . . states are not adequately enforcing the rules . . .”).

38. *Id.* at 195.

39. MODEL BENEFIT CORP. LEGIS. § 401(a)(3)–(6) (BENEFIT CORP. 2017).

40. Kathleen Wilburn & Ralph Wilburn, *Benefit Corporations: An Analysis of Social Benefit Reporting*, 38 BUS. & PRO. ETHICS J. 223, 230 (2019) (“[B Lab] recommends identifying compensation to directors and benefit directors . . .”).

41. Brent J. Horton, *Rising to Their Full Potential: How a Uniform Disclosure Regime Will Empower Benefit Corporations*, 9 HARV. BUS. L. REV. 101, 134 (2019) (“While benefit corporation legislation does generally require that information regarding executive compensation be included in the version of the benefit report that goes to investors, it is not required to be included in the version that goes to the broader public.”).

42. Hanna Basra, *Delaware Public Benefit Corporations Through the Lens of Executive Compensation*, COLUM. BUS. L. REV. ONLINE (Nov 9, 2021), <https://journals.library.columbia.edu/index.php/CBLR/announcement/view/447>.

43. *Id.* (“An aspect that could shed light on whether PBC’s are social-responsibility-washing or acting in alignment with all their stakeholders is executive compensation.”).

board's duty to balance the company's social mission with its pursuit of profits.<sup>44</sup>

In terms of process, a BC/PBC should provide a description of: (i) the governing body that approves the compensation and administers the compensation policy, including the composition of this entity and the scope of its authority, (ii) how conflicts of interests among members of this entity are managed, and (iii) if comparables analysis is used (for example, by referring to the compensation policies of similarly situated BC/PBCs for functionally comparable positions or by relying on industry compensation surveys), how the referenced data was obtained and verified, and how it is used.

#### IV. CONCLUSION

As a company's fundamental objective evolves, so must its governance structure, including how its directors and officers are selected, evaluated, and compensated. *Becoming a PBC* provides a comprehensive overview of the governance changes and enforcement mechanisms available to companies that choose to or wish to organize as BC/PBCs. This essay takes a closer look at evolving compensation practices of BC/PBCs and other entities that seek to pursue social and/or environmental impact alongside financial performance and how these practices can better accommodate evolving corporate objectives.

While stock-based performance pay is entirely consistent with a shareholder profit maximization objective, it is less suitable for companies that seek to pursue social and/or environmental impact beyond financial performance. ESG/CSR-based performance pay is an effective way to align executive compensation with these emerging expectations and also forces a more precise articulation of impact and how it will be measured and rewarded.

At the end of the day, whether ESG/CSR-based performance pay motivates social or environmental impact is a question that requires an empirical investigation. The changes to compensation-related disclosures that are suggested in this essay are expected to not only improve the quality of compensation practices in BC/PBCs but also facilitate these empirical investigations.

---

44. *BECOMING A PBC*, *supra* note 2, at 102-09.