

B Lab is Building a New Sector of the Economy: But Can We Trust Who is Behind the Wheel?

By: Stacy Magdaluyo

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Graduate School of International Relations and Pacific Studies
University of California, San Diego

Prepared for Professor Peter Gourevitch
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Introduction

Triple-bottom-line is a topic of increasing importance in public and private debate, yet the monitoring of businesses' performance in this regard remains unclear. For socially responsible investors and conscientious consumers, the challenge of differentiating between a good *company* and good *marketing* remains. B Lab, a nonprofit organization headquartered in Philadelphia, addresses the challenge of triple-bottom-line by rating companies on performance related to governance, workers, community and environment, and providing a certification. Launched in 2006, B Lab certifies B Corporations the same way Fair Trade USA certifies Fair Trade coffee or the U.S. Green Building Council certifies LEED buildings. To date, there are 517 Certified B Corporations in 60 industries, ranging from Patagonia in the apparel industry to Bamboo Sushi in the restaurant industry. Through its efforts, B Lab aims to build a new sector of the economy. This paper seeks to answer the following questions: *Is B Lab's certification method reliable for investors and consumers? What makes the organization credible?*

B Lab

Overview of Organization

B Lab is a nonprofit, 501(c)3 organization whose mission is to use the power of business to solve the world's most pressing challenges. B Lab began in 2006 when three long-time friends and college mates, Joey Coen Gilbert, Bart Houlahan and Andrew Kassoy, decided to create a foundation for businesses that wanted to do more than make money. According to Kassoy, "We realized that there is a huge marketplace of companies and their consumers and investors who are interested in creating value for all stakeholders, not just shareholders¹."

Developing this marketplace requires addressing systematic problems in the current one. These problems include: (a) a lack of standards to distinguish between good companies and good marketing, and (b) a bias in existing corporate law toward maximizing profit, and therefore, shareholder value. B Lab addresses these problems through their major initiatives: designing a rating system, certifying businesses as “Certified B Corporations” who pass the assessment, and promoting a new corporate form called the “B Corp” that takes into account stakeholders, not just shareholders.

It is important to distinguish between a “Certified B Corporation” and a “B Corp,” as these are not considered to be the same label. The former is a certification from B Lab granted to a for-profit business that voluntarily takes the B Lab assessment, receives a passing score, and changes its governing documents to reflect consideration of stakeholders. The latter is a legal status administered by the state granted to a for-profit business that changes its corporate charter and files the appropriate documents with the State Department of Assessments and Taxation. Benefit corporations, or B Corps, are required to have a corporate purpose to create a material positive impact on society and the environment; expand fiduciary duty to require consideration of the interests of workers, community and the environment; and publicly report annually on overall social and environmental performance against a comprehensive, credible, independent, and transparent third party standard². Though they share similar names, they are administered by entirely different entities. B Lab, however, plays a direct role in deeming companies as Certified B Corporations, yet also plays an indirect role in convincing states across the U.S. to adopt B Corp as a legal form. B Lab will not necessarily be the third party standard for the annual reports of benefit corporations.

Aside from providing certification, B Lab is determined to create a supportive community for Certified B Corporations. B Lab facilitates direct financial benefits, including product and service discounts with other Certified B Corporations and B Lab partners. They claim to save Certified B Corporations over \$1 million annually through discounts on Salesforce.com, B2B services and loan forgiveness programs. B Lab also promises growing attention from the media, but more interestingly, from impact investors. Certified B Corporations receive a free GIIRS rating—a measurement used by the impact investment industry to guide the flow of socially responsible capital.

Target Audience

B Lab appears to have many audiences, ranging from conscientious consumers to social investors to the social enterprises themselves. The certification signals to the conscientious consumers and investors that a company is worth supporting because it meets rigorous standards of social and environmental performance, accountability and transparency. In this regard, B Lab appears to affect the marketplace demand by making it easier for triple-bottom-line consumers and investors to assess where to put their money. B Lab also appears to affect the marketplace supply by encouraging social enterprises to acquire certification, by providing direct financial and professional benefits (see Appendix A). However the more prioritized target audience is actually the state legislators. B Lab strives for systematic change to the existing marketplace. They understand that a benefit corporation is the corporate structure that best affects change. Therefore, the consumers, investors and enterprises form the community of Certified B Corps, form the constituency through which B Lab can persuade states to adopt the new legislation.

Governance

B Lab is governed not only by a Board of Directors, but also by two independent Standards Advisory Councils that oversee the certification ratings and auditing requirements. The Board still has ultimate authority on recommendations coming from the Standards Advisory Councils. Current members of the Board include Debra Dunn, Director of the Skoll Foundation; Bart Houlahan, Co-Founder of B Lab; Lorene Arey, President of the Clara Fund; Dave Chen, Founder and Managing Director of Equilibrium Capital Group LLC; and Don Shaffer, President and CEO of RSF Social Finance. In their current endeavors, they support social ventures. The Skoll Foundation awards social entrepreneurs; the Clara Fund supports global organizations that grant economic opportunities for women; Equilibrium Capital Group invests across a platform of asset managers that focus on sustainability of water, distributed energy, agriculture, integrated land management, and low carbon transportation; and RSF Social Finance lends capital to social enterprises that focus on Food and Agriculture, Education and the Arts, and Ecological Stewardship. Across all members, they bring a long history of understanding and working with the types of businesses that B Lab aims to support.

The Standards Advisory Councils (SACs) are independent bodies that oversee the B Rating System. Nine members comprise the Developed Markets SAC, and ten members comprise the Emerging Markets SAC. Recommendations from the SACs can only be rejected with a 2/3-majority vote by the Board of Directors. Current members of the SACs include Rhonda Evans, Science Advisor for GoodGuide; Genevieve Edens, Impact Assessment Manager for Aspen Network of Development Entrepreneurs; Rafi Manachem, Metrics Manager for Grassroots Business Fund; and Hewson Baltzell, Head

of the Sustainable Solutions Team for Risk Metrics. Many of these members came from private sector backgrounds in which they focused on corporate accountability and sustainable behavior.

Funding

Providing the monetary support to B Lab are several foundations (Rockerfeller Foundation, Halloran Philanthropies, Prudential Foundation, Clara Fund, Good Energies Foundation, Annie E. Casey Foundation, and Calvert Foundation), board of directors (Debra Dunn and David Chen), wealthy individuals (Stuart Davidson and other anonymous donors), private sector companies (Deloitte LLP and RSF Social Finance), as well as the United States Agency for International Development (USAID). Each of these funders has expressed a belief in B Lab's mission and efforts, and seven of the major funders pledged a multi-year contribution (see Appendix B).

B Lab collects annual certification fees from its over 517 Certified B Corporations (see Appendix C). These fees are charged on a sliding scale based on the corporations' annual net sales. A smaller business making less than \$1 million in net annual sales will pay a \$500 annual certification fee, whereas a larger business making more than \$100 million will pay \$25,000.

B Lab Certification

Certification Process

Any business may take a free online B Impact Assessment, regardless of whether the business is looking to become certified. A business seeking certification must complete a series of steps: (1) earn a minimum score of 80 out of 200 possible points on the B Impact Assessment, (2) engage in a phone interview with a B Lab staff member, (3)

provide documentation as proof to eight to ten randomly selected questions from the assessment, (4) amend the bylaws to require consideration of stakeholders not just shareholders, and (5) sign the B Corp Declaration of Interdependence.

Monitoring Process

Any Certified B Corporation is eligible for an on-site review every two years. Specifically, B Lab randomly selects 20% of all Certified B Corporations, meaning all corporations have a one in five chance of being audited. The goal of the audit is for B Lab to verify the accuracy of each response to the B Impact Assessment.

The review process is quite transparent, with the steps and timeline available on the B Lab website. B Lab informs selected companies several months before the review, and provides guidelines for what will be required. If the on-site review results in their score going below an 80, the company has a 90-day “cure period” to bring its score back up. If the on-site review proves that the company misrepresented itself on the assessment, the company fails the review.

Three rounds of on-site reviews have taken place, with over 49 corporations visited. Of these, 43 corporations passed their review with two corporations still under review from the 2010 audit.

Analyzing Integrity of B Lab

Are They Pointless?

B Lab’s certification concept has received copious amounts of praise from private and public entities alike. According to Esquire magazine, “B Corps may be like civil rights for blacks or voting rights for women—eccentric, unpopular ideas that took hold and changed the world.” However, also in the limelight is the notion of passing

legislation to make B Corporations a legal form. According to the former president of the American Bar Association, the concept of the benefit corporation is “the first real, original, constructive thought anyone has had in the corporate governance world in about 25 years.” Co-founder Andrew Kassoy claims that “when we started, we decided we shouldn’t do anything that requires changing the law, so we should start with a certification⁵.” Such a statement raises the question of whether the certification is simply the means to an end, rather than the end itself. Contrary to Fair Trade USA or USGBC, which use certification to achieve their respective missions, B Lab also plans to affect legislation. Currently, the benefit corporation laws have been enacted in seven states. Provided that the legislation is passed by all states, the role of certifications becomes meaningless. At most, it offers businesses with a measurement tool prior to applying for benefit corporation legal status. However, a legal B Corp does not need to be a Certified B Corp. Certification seems to be a low-risk alternative for a business, given there are no legal implications and the certification is voluntary. In fact, Benchmark Asset Managers decertified in 2011 immediately after its on-site review. Decertification does not require much effort; it requires simply the removal of the certification seal from the website and other marketing materials.

The fact that 517 corporations have been certified by B Lab is impressive, but is overwhelmed by the 5,767,306 registered U.S. businesses that have not been assessed³. Additionally, the assessments seem more geared toward U.S. businesses as opposed to international ones, with just a handful of certified businesses in Canada and in the European Union. The relatively small and U.S.-based presence of Certified B

Corporations reinforces the use of certification as a tool for affecting legal change. B Lab is focusing on the U.S. as part of its strategy to target U.S. legislators.

Governance Issues

B Lab has overall strong governance, as seen by independence of the Standard Advisory Councils from the Board of Directors as well as the staff members carrying out the certification. However, as more social businesses become Certified B Corporations, there is the potential for a conflict of interest as the decision-makers also have "day jobs" in organizations linked with Certified B Corporations. RSF Social Finance owns a fund that invests with New Resource Bank, a Certified B Corporation. Equilibrium Group invests in asset managers whose focus is sustainable energy businesses. While their current portfolio does not contain Certified B Corporations, these businesses appear as good candidates for certification. If the assumed goal of B Lab is to increase the number of certified businesses, the potential for conflict of interest can be assumed to increase as well.

Funding Issues

The team of funders is transparent on the B Lab website, and a majority of the funders are philanthropic foundations concerned with defining standards and accountability. They are not concerned with the performance of individual businesses, therefore are less likely to influence the board or standard-setting councils toward lenient standards. The reputation of the funders also aids B Lab's credibility, with key names such as the Rockefeller Foundation and USAID.

Although many of the funders have made multi-year contributions, B Lab plans to sustain itself through annual certification fees. While this may present an incentive for B

Lab to ease its standards in order to attract and retain businesses, it is common practice among certification authorities such as Fair Trade USA and USGBC to charge a registration or annual fee.

Certification Issues

One red flag arises in the first step of the certification process. A business must earn a minimum score of 80 out of 200 possible points on the B Impact Assessment. However a passing score of 40% seems low by most grading standards. It means that a Certified B Corporation must earn less than half of the possible points. A low standard could signify that B Lab hopes to encourage businesses to become certified, possibly to broaden their constituency in order to pass legislation.

Another red flag appears in the second step of the certification process. A business must pass a phone interview with a member of the B Lab standards team. The interview ranges from one hour to longer, depending on the size of the company. The questions are meant to clarify the responses on the initial assessment. However there is little transparency as far as who is asking the questions—volunteer interns or full-time experts—as well what are the rigor, quality and consistency of the questions.

Looking at the list of certified companies is one way to judge the rigor of the certification process. 72% of the certified companies are in the service or retail industry, 16% are in manufacturing, and 12% are in wholesale. A majority of the certified companies provide information services, with only a small percentage involved in manufacturing or wholesale. Therefore they are likely to do well on the environment component of the assessment, by nature of their operations. Additionally, the certified companies are mainly small, start-up businesses that are little known to the public. Large,

household name businesses such as Wal-Mart or McDonalds⁴ are not found on the list. The likelihood of these businesses applying for certification is very low, given they do not need a certification to differentiate themselves in the marketplace. Therefore, it appears that the certification exists as a way for small businesses to compete against larger competitors.

Monitoring Issues

Although companies are selected randomly for on-site review, the selected companies are informed in advance. Not only that, B Lab provides them with guidelines for what is expected during the on-site review. Companies have two to three months to prepare. This amount of time and preparation seems to favor the company in review. Additionally, if the company's on-site review results in a score lower than 80, the company has 90 days to redeem itself. Of the three on-site reviews conducted in 2008, 2009 and 2010, nearly all of the companies passed the review. Rather than claim that two companies failed the review, B Lab states that they are still under review. This is far beyond the 90-day cure period, and detracts from the credibility of the monitoring process.

Incentives to Mislead

B Lab has more incentives to certify companies than to reject them. First, they aim to build a community of Certified B Corporations. Without such a community, they cannot pursue their other services, such as creating a network for social entrepreneurs, or leading the way in passing legislation. Their 2012 Annual Report includes a section for B Lab's progress, and their key indicators include number of states that signed benefit corporation laws, the number of Certified B Corporations, the number of businesses

completing the assessment, and the number of articles featuring Certified B Corporations. By setting these metrics, it appears that it is in B Lab's best interest to assess and certify as many businesses as possible.

They have little to no costs of being wrong; in fact, two of the companies that went through an on-site review were not deemed to have failed, but rather it appears B Lab engages in a year-long process of helping the company reach a passing score. Even the term "being wrong" is hard to define, since B Lab is the first and only organization to develop a rating system for companies. Because they deal with many companies across over 60 industries, they tailor their assessment and interviews to whatever the industry may be—construction, apparel, or financial services. B Lab has power over its definition of a good company; therefore it is difficult for an outside observer to know when B Lab is wrongly certifying a company.

B Lab has three approaches in its push for the adoption of benefit corporation laws. First, B Lab partners with the American Sustainable Business Council to obtain petition support from individual businesses and business associations. Second, B Lab approaches individual citizens to write letters of support to their elected officials through www.care2.com. Third, B Lab has its most well-known or "marquee" supporters such as Patagonia, Method and RSF Social Finance testify at the hearings. Therefore, it makes sense for B Lab to spread awareness of the legislation by introducing a certification. Once a company gets certified, it wants to share its success, thereby generating media press about Certified B Corporations and the underlying fight toward legislation.

The biggest concern is what will happen to B Lab once the legislation is passed and each state within the U.S. has adopted the benefit corporation as a legal form. B Lab

will continue to offer a professional network and discounts for these social businesses, thereby still fulfilling its initiative of supporting entrepreneurs that want to use their business for good. They will continue to provide certification for new start-ups who wish to register as benefit corporations, but are not certain of how they measure up; as well as for existing businesses who wish to re-incorporate, but want to test the feasibility of doing so. They can also provide the B Impact Assessment for benefit corporations who are required by law to publish their performance as measured by third party standards. However, the benefit corporation is free to choose among a list of approved third party standards, such as Good Guide, Green Seal Business Certification, and the Ceres Roadmap to Sustainability. If a company already has its Certified B Corporation status, then it will likely continue to use B Lab for future annual reports.

Conclusion

After examining the organizational structure and certification process of B Lab, it is time to return to the initial questions: *Is B Lab's certification method reliable for investors and consumers? What makes the organization credible?*

B Lab's certification process is not easy. A business must do more than simply pay a registration fee. The business must engage with B Lab through a series of steps, including amending its governing documents. B Lab has also made an effort to make its standard-setters independent of the certifiers. Moreover, the rating system used in the B Impact Assessment has been built upon to form GIIRS, which is used widely throughout the impact investing industry. However, when it comes strictly to B Lab's certification process, there are many flaws to its reliability. The passing score is a meager 40%, the phone interview process is not transparent, and it is easy for information companies to

pass the environment component, but difficult for manufacturing and wholesale companies. Additionally the monitoring process is quite transparent, benefitting the companies coming under review; as well as lenient, offering a three-month cure period to companies that do not pass the review. That said, it is still difficult to measure whether investors or consumers will change their behavior based on the certification. Investors would rather see the GIIRS ratings when making their decisions, as this has become standard in practice. Consumers may not be familiar with the certified companies, as they are so new to the market.

The organization is, for the most part, credible. Its funders are reputable organizations known for their stringent criteria, and its governance practices are mostly free of conflicts of interest. But is B Lab credible as a certifier? The answer is no. The certification, from B Lab's perspective, is a means to an end. B Lab's goal is to affect meaningful, structural change to support businesses that want to do good. Even once that goal is achieved, in the form of each state adopting the benefit corporation laws, B Lab is setting itself up for continued revenue. By associating itself with the legislation movement, and certifying as many companies as possible, it is in the best position to continue to be the third party standard for companies that legally become benefit corporations.

B Lab has proven itself as a pioneer in making triple-bottom-line a more measurable concept. Its accomplishments in bringing accountability and standards to otherwise "good marketing" concepts are worth the praise it has received. However, as a certifier, it lacks credibility because of the incentive to certify more and more companies to fulfill its other organizational goals. It claims to certify companies in the same way that

Fair Trade USA and the U.S. Green Building Council certify coffee and LEED buildings, respectively. Yet forming an independent organization focused on certification, and isolating the organization that seeks to drive policy changes would better serve its credibility.

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Appendix A: Top 12 Reasons to Become a B Corp

(Source: Brochure from B Lab presentation in San Diego on March 6, 2012)

- 12) Be recognized as a leader
- 11) Differentiate your business
- 10) Participate in national ad campaign
- 9) Protect your mission
- 8) Make employees proud
- 7) Access technology, talent and expertise
- 6) Benchmark company performance
- 5) Save money, increase profits
- 4) Partner with like-minded leaders
- 3) Pass legislation to advance sustainable business
- 2) Access mission aligned capital
- 1) Lead a movement

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Appendix B: List of Funders

(Source: <http://www.bcorporation.net/funders>)

‡ Multi-year Contribution † Program Related Investment

\$5,000,000 - \$2,500,000

- The Rockefeller Foundation

\$2,499,999 – \$1,000,000

- B Lab Co-Founders † ‡
- Deloitte LLP
- Halloran Philanthropies ‡
- The Prudential Foundation †
- United States Agency for International Development (USAID)

\$999,999 – \$100,000

- The Clara Fund
- Good Energies Foundation
- Panta Rhea Foundation
- Pioneer Portfolio of the Robert Wood Johnson Foundation
- RSF Social Finance ‡
- Tom Bird Charitable Trust ‡ †

\$99,999 – \$25,000

- Anonymous
- The Annie E. Casey Foundation
- Calvert Foundation † ‡
- Flora Foundation
- Armonia LLC
- Ruth Fuchs Charitable Trust ‡
- Debra Dunn ‡

\$24,999 – \$10,000

- Anonymous
- Linklaters
- Stuart Davidson
- The John P. and Anne Welsh McNulty Foundation

\$9,999-1,000

- Anonymous
- David Chen
- John Fullerton
- Solidago Foundation
- Vertex

Appendix C: Annual Certification Fees

(Source: <http://www.bcorporation.net/become/official>)

Annual Net Sales	Annual Fee
\$0 - \$1,999,999	\$500
\$2 M - \$4,999,999	\$1,000
\$5 M - \$9,999,999	\$2,500
\$10 M - \$19,999,999	\$5,000
\$20 M - \$99,999,999	\$10,000
\$100 M +	\$25,000

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Appendix D: Sample B Impact Assessment

(Source: <http://www.bcorporation.net/index.cfm/fuseaction/company.report/ID/3c0b54a8-a988-46ea-ad59-c1557afe725b>)

2012

2012 Rating: 107.1		
<i>Rating Details</i>	Points Earned	% Points Available
Governance <i>Area of Excellence*</i>	14.8	87.1 %
Corporate Accountability	11.6	88.6 %
Transparency	3.2	80 %
Workers <i>Area of Excellence*</i>	25.1	62.8 %
Compensation, Benefits & Training	17	83 %
Worker Ownership	2.2	31.4 %
Work Environment	5.9	88.3 %
Community	19.8	44 %
Community Products & Services	0	0 %
Community Practices	19.8	44 %
Suppliers & Distributors	8.6	77.3 %
Local Involvement	1.3	18.3 %
Diversity	2.8	32.6 %
Job Creation	1.1	13.8 %
Civic Engagement & Giving	8.3	83 %
Environment <i>Area of Excellence*</i>	47.4	71 %
Environmental Products & Services	3.8	12.7 %
Environmental Practices	43.4	89.6 %
Land, Office, Plant	6.8	77.6 %
Inputs	18.8	77.1 %
Outputs	1.8	38 %
Suppliers & Transportation	8.8	37.8 %
Total	107.1	

Date Founded: July 1972

Location: Ventura, California

Sector: Wholesale

Industry: Apparel & Footwear

Products/Services: Outdoor Apparel

Corporate Structure: C Corporation

Ownership: Private

Website: <http://www.patagonia.com>

Highlights:

Governance: Board includes independent members to represent interests of Community and Environment; work within industry to develop social & environmental standards; 5 financials with employees

Workers: Extend health benefits to part-time retail, warehouse staff; 50% full time employ participate in external professional development; conduct annual employee satisfaction survey >80% report 'satisfied' or 'engaged'; part-time and flex-time work schedules available; subsidized child care and counseling service offered

Community: 100% of significant suppliers made transparent on website; code of conduct enforced on all primary suppliers; >40% of management are women or ethnic minorities >25% of employees took time off for community service; 1% of sales donated to environmental NGOs

Environment: 75% of materials used are environmentally preferred (organic, recycled etc); company conducts life cycle studies on most common materials; 30% of suppliers meet bluesign® standards for environmentally advanced apparel manufacturing; Some facilities LEED Certified; 5-10% of energy use is generated on-site

