

Benefit Corporations - A New Type Of Corporation - Are Now Authorized In Pennsylvania

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On January 23, 2013, the Pennsylvania Benefit Corporation Act (the Act) became effective. The Act authorizes a new type of for-profit business corporation known as a benefit corporation. Pennsylvania is now one of 12 states that have passed laws creating benefit corporations.

A. Benefit Corporations under the Pennsylvania Act.

A fundamental difference between benefit corporations and standard business corporations is that directors of benefit corporations are required to consider the effects of corporate actions on the interests of a number of different groups, as referred to in Section B.3 below, in addition to shareholders. In return, benefit corporations may receive greater protection to pursue sustainable business goals and to maintain their business purpose over time, as well as a way to differentiate their business and transparently report on their social and environmental performance. However, unlike the corporation laws of many other states, under Section 1715 of the Pennsylvania Business Corporation Law the directors of standard business corporations, in determining the best interests of a corporation, may consider, to the extent they deem appropriate, the effects of any corporate action on any groups affected by such action, including shareholders, employees, suppliers, customers, creditors and the communities in which there are establishments of the corporation, as well as considering "all other pertinent factors." Additionally, directors of Pennsylvania standard business corporations are not required to regard the interests of any particular group affected by such action as a dominant or controlling interest or factor. As a result, persons who might consider establishing a benefit corporation should, as set forth in Section D.3 below, determine whether the goals they seek to achieve might also be accomplished by using a standard Pennsylvania business corporation, with more flexibility and fewer restrictions.

B. Differences between Pennsylvania Benefit Corporations and Standard Business Corporations.

Under the Act, benefit corporations have many of the same features of standard business corporations, but with the following special requirements, among others:

- 1. Corporate Purposes.** A benefit corporation must have as one of its purposes the creation of a "general public benefit." This term is defined as a material, positive impact on society and the environment, taken as a whole, assessed against a third-party standard. The Articles of Incorporation of a benefit corporation may also identify one or more specific public benefits which the corporation may wish to achieve. These include, among other things, promoting economic opportunity for individuals or communities, preserving the environment, improving human health, and promoting the arts, sciences or advancement of knowledge.
- 2. Transparency.** Benefit corporations must provide a greater level of transparency than standard business corporations. This transparency is aimed at preventing benefit corporations from engaging in "greenwashing," or portraying themselves as "responsible" or "sustainable" companies to attract consumers without following through on their commitment to sustainable business practices. The Act requires a benefit corporation to publish an annual benefit report to inform its shareholders and the public about its success in meeting its public benefit purposes. In evaluating its success, a benefit corporation must assess its overall social and environmental performance against a comprehensive, credible, independent, and transparent third-party standard. The term "third-party standard" is defined as a recognized standard for defining, reporting and assessing corporate social and environmental

performance that is (a) developed by an organization that is independent (as that term is defined in the Act) of the benefit corporation and meets certain other requirements, and (b) transparent because certain information about the standard is publicly available. A number of organizations have developed such third party standards. The names of some of these organizations can be found on the website of B Lab Company (benefitcorp.net), a nonprofit corporation based in Berwyn, Pa., which was the original progenitor of the benefit corporation concept. The assessment does not need to be audited or certified by a third-party standards provider.

In addition to the assessment described above, the annual benefit report must contain several other disclosures, including: a description of the ways in which the corporation pursued its public benefits during the year; the extent to which such benefit was created; any circumstances that hindered in the creation of such benefit; the compensation paid during the year to each director; the name of each person that owns 5 percent or more of the benefit corporation; the opinion of the “benefit director” regarding whether the corporation acted in accordance with its general and specific public benefit purpose and whether the directors and officers complied with their respective duties and standards of conduct under the Act; and a statement of any connection between the organization that established the third-party standard and the benefit corporation. The annual benefit report must be delivered to each shareholder, and must also be posted on the public portion of the corporation’s website or, if the corporation does not have a website, filed with the Pennsylvania Department of State and provided without charge to anyone who requests the report.

3. Accountability of Directors and Officers. The Act specifies standards of conduct for directors and officers that differ in a number of respects from those relating to the directors and officers of standard business corporations. Benefit corporation directors are required to consider the long- and short-term effects of their decisions on various stakeholders. Each officer is required to take such interests into account when the officer has discretion to act with respect to a matter and it reasonably appears to the officer that the matter may have a material effect on the creation by the corporation of its general public benefit or any specific public benefit

identified in its Articles of Incorporation. The interests that must be considered by the directors and officers of benefit corporations are: (a) the shareholders of the corporation; (b) the employees and work force of the corporation and its subsidiaries and suppliers; (c) the interests of customers as beneficiaries of the general public benefit or specific public benefit purposes of the corporation; (d) community and societal considerations, including those of any community in which the corporation or its subsidiaries or suppliers are located; (e) the local and global environment; (f) the short-term and long-term interests of the corporation; and (g) the ability of the corporation to accomplish its general public benefit purpose and any specific public benefit purpose. No priority is required to be given to the interests of shareholders or of any other particular group over the interests of any other person or group, unless the benefit corporation has stated in its Articles of Incorporation its intention to give priority to certain interests related to the accomplishment of its general public benefit purpose or of a specific public benefit purpose identified in its Articles of Incorporation.

The shareholders and directors of a benefit corporation have the exclusive right to bring an action called a “benefit enforcement proceeding” against the corporation or its directors for failing to pursue or create a general or specific public benefit or for a violation of a duty or standard of conduct under the Act. Although subject to greater accountability, the directors and officers, and the corporation itself, are not liable for monetary damages for any of the above actions; instead, injunctive relief or similar equitable remedies are available. As is the case with directors of standard business corporations, directors of benefit corporations may be released from personal liability for their actions (unless the director breached or failed to perform the duties of his or her office, and such breach or failure constituted self-dealing, willful misconduct or recklessness; however, such limitation does not apply to the liability of a director under any criminal statute or the liability of a director for the payment of taxes under any applicable law), if such limitation is included in a bylaw adopted by the shareholders. The Act also specifies that directors and officers of a benefit corporation do not have a fiduciary duty to the beneficiaries of any of the public benefit purposes of the corporation.

A benefit corporation must designate one of its directors as a benefit director. In addition to having the duties and rights of the other directors, such director is responsible for preparing a statement to be included in the corporation's annual benefit report as to whether, in such director's opinion, the corporation acted in accordance with its public benefit purposes in all material respects. If, in such director's opinion, the corporation or its officers or directors failed so to act, then the statement must include a description of the ways in which they failed to so act. The benefit corporation may also elect a benefit officer who is responsible for preparing the corporation's annual benefit reports.

C. How to Become a Benefit Corporation. There are three ways to become a benefit corporation under the Act:

1. A new business can form as a benefit corporation under the Business Corporation Law by stating it is a benefit corporation in its Articles of Incorporation.
2. An existing corporation may amend its Articles of Incorporation to include a statement that it is a benefit corporation, if approved by a two-thirds vote of each class or series of shareholders, regardless of any limitation in its Articles of Incorporation or by-laws relating to such vote.
3. A business seeking to become a benefit corporation through a merger, consolidation, division or share exchange must approve the transaction by a two-thirds vote of each class or series of shareholders, regardless of any limitation in its Articles of Incorporation or bylaws relating to such vote.

D. Certain Considerations To Be Taken into Account.

1. By Potential Directors and Officers. Although directors and (to the extent set forth in Section B.3 above) officers of benefit corporations are required to take interests other than those of the shareholders into account in making decisions, and are not (except as set forth in its Articles of Incorporation) required to give priority to any particular interest, the Act does not completely negate the fiduciary and other duties of directors and officers. The standards imposed on directors and officers are subjective, and it will likely be difficult to determine how to best weigh

the various interests that must be taken into account in determining whether or not to take a particular action. Consequently, as with standard business corporations, it is important from the perspective of a director or officer of a benefit corporation to confirm its bylaws have indemnification provisions that are as broad as possible, consistent with the Business Corporation Law, as there are no special provisions in the Act limiting such indemnification, and to confirm that the corporation has obtained adequate directors and officers liability insurance.

2. By Potential Investors. Benefit corporations provide a vehicle for socially conscious investors to invest in companies they believe can achieve a public purpose but still make profits, resulting in potential monetary gains for the investor. On the other hand, since benefit corporations are for-profit corporations, payments to such corporations will not be deductible for tax purposes. In addition, investors must keep in mind that the directors and officers of a benefit corporation are permitted to take actions that would benefit constituencies other than shareholders, and are not required to give priority to shareholders' interests.

3. Less-Restrictive Alternative to Benefit Corporations. Businesses that want to pursue socially or environmentally conscious goals can attain some of the goals of benefit corporations without locking themselves into the Act's requirements and restrictions. As described in Section A above, Pennsylvania's Business Corporation Law already permits (but does not require) directors to consider all "pertinent" factors when making corporate decisions, including the interests of constituencies in addition to the shareholders. Furthermore, although consideration of these factors is not mandatory under the Business Corporation Law, such a requirement may be written into the Articles of Incorporation or bylaws of a Pennsylvania standard business corporation, as can a "public benefit purpose."

However, the "optics" advantage of benefit corporations may be significant in some cases. That is, the positive perception of some potential investors that may arise from benefit corporation status may, in some people's view, be valuable enough to make organizing as a benefit corporation an appropriate course of action.

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