Benefit Corporation
FAQ

Frequently Asked Questions **for Investors**

www.benefitcorp.net

Benefit Corporation

Investor FAQ

Q: How does a benefit corporation differ from a traditional corporation?

A benefit corporation has a modified governance structure that promotes the creation of durable value for all stakeholders. The structure commits the corporation to higher levels of purpose, accountability and transparency:

Purpose: Benefit corporations are committed creating environmental and social value in addition to generating profit.
Accountability: Benefit corporation directors must consider the interests of all stakeholders, not just shareholders.
Transparency: Benefit corporations are required to regularly report on how the company is balancing these interests.

Q: Doesn't traditional corporate law already allow a board to pursue the interests of stakeholders?

Not if the stakeholder interest conflicts with shareholder value. This reality is particularly vivid when a company is sold. In a sale process, traditional corporate law requires the board to accept the highest bid, no matter how that bid affects other stakeholder interests. However, even outside of the sale context, shareholder value is the only measure of director performance under traditional corporate law.

Q: What specific advantages does benefit corporation status provide?

Long-Term value creation: Benefit corporations have protection and permission to make decisions based on the creation of long term value for all stakeholders. The benefit corporation's expanded duty combats short-termism, helping investors hold management accountable to long-term and sustainable value creation.

Positive brand association: Becoming a benefit corporation confirms brand association with positive social and environmental impact in the mind of consumers and in the industry more broadly. An increasing number of consumers, over 70 million today, purchase goods based on the morals or the mission of a business and, increasingly, a company's mission is a major factor influencing brand loyalty.

Brand trust: Benefit corporations provide an innovative model to hold a company accountable to its mission and, by committing to this higher purpose, create a network of trust with workers, customer and other important constituencies.

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Q: What specific advantages does benefit corporation status provide? *(Continued)*

Strong Governance and Effective Management: Benefit corporation governance promotes the long-term creation of durable value. CalPERS has stated that "strong governance, along with effective management of environmental and human capital factors, increases the likelihood that companies will perform over the long-term and manage risk effectively."

Transparency: Integrated environmental and social reporting is a trend throughout the capital markets, and benefit corporations report regularly on their social and environmental impact. Reporting against a third party standard, as required in the model legislation and in most states, can reduce due diligence costs and as well as risk for investors by allowing them to compare performance across companies.

Attraction and Retention of Employees: Benefit corporations attract and retain talent through increased employee engagement and their commitment to a higher purpose. 40% of businesses polled have found that involvement in sustainability was very important to employee retention. Millennials will grow to 75% of the workforce by 2025; 77% of current millennials indicated that their company's purpose was part of the reason they chose to work there.

Q: What kinds of investors are investing in benefit corporations?

Numerous benefit corporations have raised capital from both traditional and social impact funds. Investors in benefit corp include: Andreessen Horowitz, Founders Fund, First Round Capital, Forerunner Ventures, Foundry Group, Baseline Ventures, Benchmark, Sherbrooke, New Enterprise Associates, Brand Foundry, Collaborative Fund, DBL Investors, Emerson Collective, Freshtracks Capital, Generation Equity Investors, Golden Seeds Capital, Good Capital, Greycroft Partners, Harrison Metal, Ironwood Equity Fund, New School Ventures, Omidyar Network, Pacific Community Ventures, Peterson Ventures, and The Westly Group.

Q: How does this model protect the interests of investors?

Shareholders retain all the protections that they have in a traditional corporate model. First, they have all their corporate governance rights. They elect the directors and vote on major corporate transactions such as charter amendments or mergers. Conflict transactions will still be subject to a searching entire fairness analysis whenever challenged, so that directors cannot pursue their own interests ahead of the interest of shareholders. Shareholders will retain the ability to bring the same types of lawsuits they can bring against a traditional corporation, including demands to review the company's books and records, election review proceedings to make sure elections are being conducted fairly, and derivative suits to pursue corporate claims against directors for breach of fiduciary duty. The only change under the benefit corporation model is the value proposition: the idea that durable long-term value is built by aligning all stakeholder interests, including the interests of shareholders.

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Q: Is investing in a benefit corporation a viable alternative for an institution that has a duty to its investors, such as its LPs, to maximize value?

Absolutely. First, the commitment to stakeholder interests can create value for shareholders that does not exist outside of that status. By making such a commitment, a business may engage its employees, its customers and its business partners in a manner that creates more long-term value for its shareholders. Even if that were not the case, it may well be that any costs associated with a company's mission can simply be viewed as a cost in that entity's business model, and that model may still provide an opportunity to obtain an acceptable return.

It may be helpful to consider a simplified hypothetical: imagine an investor considering an investment in a corporation whose successful execution of its business plan would yield a $100 profit to the investor. Then imagine another investment in a similar entity that, by pledging to contribute 10% of its profits to charitable causes, could yield a profit of $120 for the same investment by engaging its employees and customers through publicizing its charitable commitment. At that point, $120 less the 10% pledge would yield $108 profit, an 8% increase in profitability. While this is obviously simplified, it illustrates that there is no conceptual contradiction between maximizing stockholder value and committing to a mission.

More importantly, shareholders do not own just one company: most investors are diversified, and have broad shareholdings across the entire market. (This is particularly true when one focuses on the ultimate beneficiaries of the institutional asset owners that dominate the market. These pensions, mutual funds, insurance companies, endowments and foundations all have as ultimate beneficiaries a broad swath of the population that is diversified through such asset owners.) These "universal owners" earn most of their return not by successfully picking stocks that "beat the market," but by being invested in a healthy market: generally, about 80% of an investor's return comes from the behavior of the market. Accordingly, investors are actually hurt when a company in which they are invested tries to improve the return to its shareholders by externalizing costs in a manner that hurts the market. For example, universal owners who owned shares in financial companies were hurt by the "value-maximizing" activities of those companies that created the market crash in 2008

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Q: This all sounds good, but is there any legal precedent to back it up? Isn’t it risky for a business to adopt this new form?

All business plans have some risk, but the benefit corporation legislation is structured to reduce risk. The precedent that applies to traditional corporations, such as the eBay case, validates lawsuits against companies that treat stakeholders on par with shareholders. While there is no guarantee that a benefit corporation will not be sued for pursuing stakeholder values, the adoption of the benefit corporation model should decrease that risk. In addition, the benefit corporation model provides several protections from frivolous lawsuits challenging directors for not protecting stakeholders. First, only shareholders (and not stakeholders) may bring lawsuits challenging board decisions. In addition, in order to bring a derivative lawsuit challenging the balancing of the various stakeholder interests, a shareholder must meet a minimum ownership requirement--in Delaware, 2% of the company, or in the case of public companies, $2 million worth of stock. Moreover, stakeholder balancing decisions are specifically protected by the business judgment rule in fiduciary lawsuits. Finally, the statutes protect directors from monetary liability in such lawsuits.

Q: Will the accountability provisions put the directors in a situation where they are required to take actions they might not otherwise take?

The statutes are carefully drafted to require that the board consider or balance the interests of stakeholders. The statute does not mandate any particular outcome. It simply gives the board tools with which to preserve their mission.

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Q: What about the expense of converting?

In most situations, the expense should be very limited. For a company where all the shareholders support a change, the conversion is simply a matter of obtaining director and shareholder consents to an amendment to the certificate of incorporation, and filing that amendment with the Secretary of State in the jurisdiction where the company is incorporated. In most jurisdictions, no further change is required, not even a change to the corporate name.

Where some of a company's current shareholders object to the change, there may be additional issues, such as satisfying a supermajority vote or providing appraisal rights to shareholders who do not consent to the change. Generally, however, these issues can usually be managed with minimal expense.

Q: Are there legal obstacles to taking a benefit corporation public or for a public corporation to convert to benefit status?

No. In fact, a number of public corporations are incorporated in states that have "other constituencies" statutes already. These statutes specifically provide that directors can consider other stakeholders' interests. Those statutes have been in place for almost 25 years and have not created concerns with respect to IPOs.

Q: What about reporting? How does a company know it is properly attending to all stakeholders?

Benefit corporations are required to assess and report on key impact measurements. In most states, this is an annual report showing the company's performance related to third party standards. In all states, this report is given to shareholders and in most it is posted publicly as well.

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Frequently Asked Questions **for *Attorneys***

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Attorney FAQ

Q: Why does B Lab certification have a legal requirement?

Under traditional corporate law, the fundamental purpose of a corporation is to earn profits for shareholders. This means that directors generally favor the interests of shareholders over environmental and social concerns. B Lab's legal requirement alters this convention of favoring shareholder financial interests over all else, and allows a business to incorporate its values into its corporate DNA.

Q: Doesn't traditional corporate law allow a board to act on environmental and social values?

Only when those values do not conflict with shareholder value. This conflict can be is particularly vivid when a company is sold. In a sale process, traditional corporate law requires the board to accept the highest bid, no matter how that bid affects other stakeholder interests. Moreover, even outside of the sale context, shareholder value is the ultimate measure of director success under traditional fiduciary duties. This was made clear in a 2010 case decided by the Delaware Chancery Court, eBay v. Craigslist. Indeed, the Chief Justice of the Delaware Supreme Court, the leading jurisdiction for corporation law in the United States, devoted a recent journal article to this very point.

Q: Outside of the ability to obtain B Corp certification, what legal advantages does benefit corporation status provide?

Benefit corporations have an expanded purpose that includes pursuing value for all stakeholders. This provides directors and officers with much more flexibility. The provisions of benefit corporation statutes also expand business judgment rule protection to director decisions that take the interests of all stakeholders into account. Importantly, these statutes explicit protect directors from liability for weighing or considering the interests of various stakeholders.

Q: Could opting into benefit corporation status give the directors too many choices?

It is clear that the board of a benefit corporation will have a greater array of choices when faced with a choice that may provide short term value to shareholders at the expense of other important constituencies. However, providing this flexibility is the goal of the benefit corporation model.

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Q: Will adopting benefit corporation status create more lawsuits that criticize the board for failing to honor its obligation to the various stakeholders?

The statutes are carefully designed to avoid frivolous lawsuits. First, constituencies other than shareholders are not entitled to bring lawsuits; only shareholders may bring lawsuits challenging board decisions. In addition, in order to bring a lawsuit challenging the balancing of the various stakeholder interests, a shareholder must meet a minimum ownership requirement--in Delaware, 2% of the company, or in the case of public companies, $2 million worth of stock. Moreover, fiduciary claims challenging stakeholder balancing decisions are specifically protected by the business judgment rule, under which it is very difficult to pursue a lawsuit. Finally, the statutes protect directors from monetary liability in such lawsuits. For companies with authentic stakeholder values, the adoption of the benefit corporation model should decrease the chance of lawsuits, since the statutes provide protection from lawsuits where a director's decision takes stakeholder interests into consideration.

Q: This sounds risky for investors. What protects them?

Shareholders retain all the protections that they have in a traditional corporate model. First, they have all their corporate governance rights. They elect the directors and vote on major corporate transactions such as charter amendments or mergers. In privately-held companies, they may also negotiate additional protective provisions. Conflict transactions will still be subject to a fairness test, so that directors cannot pursue their own interests ahead of the interest of shareholders and other stakeholders. Shareholders will retain the ability to bring the same types of lawsuits they can bring against a traditional corporation, including demands to review the company's books and records, election review proceedings to make sure elections are being conducted fairly, and derivative suits to pursue corporate claims against directors for breach of fiduciary duty. The only change under the benefit corporation model is the value proposition: the idea that true long-term value is built through purpose that aligns all stakeholder interests, including the interests of shareholders.

Q: Is investing in a benefit corporation a viable alternative for an institution that has a duty to its investors, such as its LPs, to maximize value?

Absolutely. First, the benefit corporation's commitment to stakeholder interests can create value for shareholders that does not exist outside of that status. By making such a commitment, a business may engage its employees, its customers and its business partners in a manner that creates more long-term value for its shareholders. Even if that were not the case, it may well be that any costs associated with a company's mission can simply be viewed as a cost in that entity's business model, and that model may still provide an opportunity to obtain an acceptable return.

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Q: This all sounds good, but is there any legal precedent to back it up? Isn't it risky for a business to adopt this new form?

All business plans have some risk, but the benefit corporation legislation is structured to reduce risk. The precedent that applies to traditional corporations, such as the eBay case, validates lawsuits against companies that consider mission. While there is no guarantee that a benefit corporation will not be sued for pursuing its mission, the adoption of the benefit corporation model should decrease that risk.

Q: But will there be lawsuits from the other direction, challenging directors for not pursuing mission?

The statutes are designed to minimize the risk of such lawsuits by restricting the ability to bring such suits to shareholders with significant economic interests, and expanding legal protections for such decisions.

Q: What about the expense of converting?

In most situations, the expense should be very limited. For a company where all the shareholders support a change, the conversion is simply a matter of obtaining director and shareholder consents to an amendment to the certificate of incorporation, and filing that amendment with the Secretary of State in the jurisdiction where the company is incorporated. In most jurisdictions, no further change is required, not even a change to the corporate name.

Where some of a company's current shareholders object to the change, there may be additional issues, such as satisfying a supermajority vote or providing appraisal rights to shareholders who do not consent to the change. In most cases, however, these issues can usually be managed with minimal expense.

Attorney FAQ

Q: Are there legal obstacles to taking a benefit corporation public or for a public corporation to convert to benefit status?

No. In fact, a number of public corporations are incorporated in states that have “other constituencies” statutes already. These statutes specifically provide that directors can consider other stakeholders’ interests. Those statutes have been in place for almost 25 years and have not created concerns with respect to IPOs.

Q: If that’s the case, why wouldn’t the other constituency model satisfy the needs that the public benefit model is designed for?

The other constituency model does not include the accountability or transparency provisions included in the benefit corporation model. Directors may but are not required to consider stakeholder interests. Furthermore, there is no reporting requirement that ensures that the corporation is in fact looking after the interests of other stakeholders.

Q: Will the accountability provisions put the directors in a situation where they are required to take actions they might not otherwise take?

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The statutes are carefully drafted to require that the board consider or balance the interests of stakeholders. The statute does not mandate any particular outcome. It simply gives the board tools with which to pursue broad purpose and build value for all shareholders.

Q: What about reporting provisions--are they burdensome?

For a company that is already a certified B Corporation, the reporting requirements really add nothing new. The B Impact Assessment should provide a template for satisfying most state statutory requirements. For those corporations that are not certified, there will be a new requirement, but converted corporations to date have not found the requirements to be burdensome.

Q: Is a benefit corporation required to disclose sensitive information?

No. The statutes do not require the disclosure of competitively or otherwise sensitive information.

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Frequently Asked Questions **for *Business Operations***

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Benefit Corporation

Business Operations

Q: From the perspective of the directors and officers charged with managing a corporation, how does a benefit corporation differ from a traditional corporation?

In order to answer that question, it is important to emphasize that the trend in modern corporate law and finance has been to treat the corporation solely as an asset of its shareholders, so that directors and officers must manage that asset with the primary purpose of maximizing its value for the benefit of those shareholders. Thus, directors and officers must justify decisions primarily on the maximization of shareholder value, with at most a secondary concern for other stakeholders.

In contrast, a benefit corporation has a broad purpose of creating value for all stakeholders. This means that directors and officers can and must consider the interests of other stakeholders, in addition to pursuing a financial return for shareholders.

Q: But don't directors and officers in traditional corporations already consider other stakeholders?

It is true that managers already can take other stakeholders into account because doing so may ultimately be in the best interests of shareholders. However, in a traditional corporation, if the interests of shareholders conflict with the interests of other stakeholders, the managers are required to take the path that is best for the shareholders, because only shareholder value is mandatory.

Q: Will shareholders get decreased returns in benefit corporations?

Not necessarily. By committing to consider the interests of other stakeholders, a benefit corporation may create value through employee engagement, customer loyalty and similar attributes, thereby improving outcomes for all stakeholders -- including the owners. Furthermore, certain profit making opportunities may not be available without a true commitment to other stakeholders.

Q: How does this work into day-to-day decision making?

In many cases, benefit corporation status is not likely to have a significant effect on the day-to-day operations of a corporation. The fact is that corporations operate in an ecosystem where they constantly interact with a variety of stakeholders—customers, employees, suppliers, etc.—and that interaction requires that the interests of those stakeholders be considered, whether or not that consideration implicates the ultimate purpose of the corporation.

Business Operations

Q: What does that mean as a practical matter at the board level?

Best practices will continue to evolve, but corporations that adopt the benefit corporation model will continue the movement that has already begun with environmental, social and governance reporting. There will be more discussions at the board level of the effects a particular policy or decision will have on various stakeholders, and the board will be empowered to take those effects into account when making decisions.

Q: How does this affect long term planning?

At a very practical level, benefit corporation status may allow directors to make decisions that, by benefiting stakeholders, actually create long term net present value for shareholders, without a concern for how those decisions affect short term market value.

Q: What about recordkeeping?

Benefit corporations that are following best practices will be reporting against a third party standard, and the board should have full access to, and spend time discussing that report in depth. Where appropriate, the minutes should reflect the board's consideration of stakeholder interests in its decision making.

Q: Will benefit corporation status add significant procedural requirements?

While each situation may be different, in many cases there will not be significant additional procedural requirements because environmental, social and governance reporting is already a significant part of board function. Where it is not, that reporting may be the biggest additional procedural requirement. From the perspective of regular decision making and policy setting functions, there should not be significant additional procedural requirements, given the already integral role of stakeholders in corporate decision making.

Q: Can you provide an example to make this more concrete? What if the corporation on whose board I sit is deciding whether or not to acquire a new product line?

In deciding whether to acquire a line of business, a benefit corporation would consider all the usual business issues, such as whether the product fits properly into the current business, what type of synergies would be created, etc. The company would also consider a variety of other stakeholder issues, such as the environmental footprint of the new product line, its role in the market, and its supply chain. These are elements that a long-term focused company is likely to consider in any event, but because the company is a benefit corporation, its purpose will specifically encompass making a positive impact on those affected by the new line of business.