

## TO “B” OR NOT TO “B” A BENEFIT CORPORATION \*

PUBLICATION, *IMPACTPHL VOLUME 78*: - MATTHEW L. DEVINE, ALEX SELDIN, JULY 22, 2024

As counsel for many socially-conscious businesses, perhaps the most frequent early-stage question we field from entrepreneurs is whether they should organize their business as a traditional business entity (such as a corporation or limited liability company) or as one of the newer, alternative entities (such as a benefit corporation or benefit limited liability company) that many socially responsible businesses are increasingly using in recent years. While there is no one right answer to this question, we thought we would weigh in with some key considerations that should help entrepreneurs decide on how they want to proceed.

First, it is important to note that this article will focus on benefit corporations as a distinct type of business under Delaware law rather than focusing on the confusingly named B Corporation certification program offered by the Wayne, PA-based nonprofit certifier B-Labs. A certified B Corporation is not actually a separate and distinct type of business entity, but is instead a signifier that a company has completed the rigorous B-Labs certification program, which is sort of a LEEDS-certification-style program for socially minded businesses. While it is possible to be both formed as a benefit corporation and be certified as a B Corporation, one is not a prerequisite for the other, and a discussion of the benefits and limitations of the certification program will be addressed in a future article.

**“... a benefit corporation actually has to do the things it claims it will do to further its public purpose or else be held accountable for failing to live up to its promises.”**

Before we get into the specifics of why a company may (or may not) want to form as a benefit corporation, here is some background on benefit corporations:

- A benefit corporation is a for-profit corporation, like Warby Parker or Ben and Jerry's, that seeks to produce a positive effect upon persons, entities, communities, or interests through one or more specific benefit purposes. The specific benefits largely align with the charitable purposes available to most nonprofits (e.g. the public benefit typically includes some sort of artistic, charitable, cultural, economic, educational, environmental, literary, medical, religious, scientific, or technological purpose) and are set forth in the company's certificate of incorporation. By embedding it side-by-side with the company's for-profit purpose in the company's charter, the Delaware statute requires benefit corporations to balance its for-profit interests with the best interests of those that its public benefit is intended to help. This is in contrast to traditional corporations, which do not require (and typically do not have) a specific benefit purpose in its organizing documents, meaning that traditional corporate boards are not required (and in many instances are not permitted to) weigh any other interests other than the pure financial interests of shareholders when making decisions for the corporation. In many cases, this means a choice between maximizing profits for the benefit of stockholders or facing a potential lawsuit for not doing so.

- To enforce this multi-bottom line mandate, the Delaware benefit corporation statute provides for two primary enforcement mechanisms: (i) the ability of stockholders who hold at least 2% of the company to bring suit against a board of directors (called a benefit proceeding) in order to compel the board to more fully weigh its beneficial purpose and (ii) the requirement that the company publish and post a report to its website showing its progress in accomplishing its beneficial purposes. While it is unclear what the exact consequences are for violating those provisions (to date, we are not aware of any case actually going to court involving a benefit proceeding, nor is there any statutory penalty for failing to publish this benefit report on at least a biennial basis), these mechanisms seem to serve primarily as an organizing feature and behavioral anchoring mechanism rather than as a separate and distinct threat not already faced by traditional corporations. Obviously, that could change as more benefit corporations are formed and mature, but for now, that is the current status quo.
- In addition to being able to use the same sort of naming conventions as traditional corporations (e.g. “Inc.,” “Corp.” and the like), benefit corporations are also permitted to use “Public Benefit Corporation” or “PBC” in their name to advertise the company’s benefit corporation status.

**“Many private foundations are able to make debt or equity investments in benefit corporations if the benefit corporation’s public purpose is aligned with the foundation’s charitable purpose.”**

With that as context, here are the typical reasons why many entrepreneurs choose to form benefit corporations:

- It builds brand loyalty. Although probably not as well-recognized in the market as the B Corporation certification program, a company that is formed as a benefit corporation can advertise its status in both its name and in its marketing materials. Numerous studies have shown that consumers are more likely to buy products and services from companies that market themselves as being socially responsible, and advertising itself as a benefit corporation is one way a company can show its commitment to the public. Moreover, the confusingly similar name of the benefit corporation to the B Corporation certification program likely also provides some spill-over value to benefit corporations due to its association with the better-recognized certification program in the marketplace.
- It actually does provide accountability. The history of corporate law in this country is replete with traditional corporations “greenwashing” or engaging in other forms of superficial “social responsibility” efforts. By actually providing mechanisms through which shareholders and the public can hold directors and the company responsible for its stated public purpose, benefit corporations have the ability to influence and change behavior for the better (even if these enforcement mechanisms are largely untested in a legal context). This means that a benefit corporation actually has to do the things it claims it will do to further its public purpose or else be held accountable for failing to live up to its promises. In our experience,

this type of accountability is why many companies decide to incorporate as a benefit corporation—so they can not only talk the talk, but that they can also walk.

**It may open up new sources of funding.** In addition to obtaining capital from traditional sources such as venture capital funds, angel investors, and banks, benefit corporations also have the ability to tap into new sources of capital. Many private foundations (including such large foundations like the Ford Foundation and the Kresge Foundation) are able to make debt or equity investments (called “Program-Related Investments” or “PRIs”) in benefit corporations if the benefit corporation’s public purpose is aligned with the foundation’s charitable purpose. In addition to being another source of capital not generally available to traditional corporations, PRIs are often made on better-than-market terms in order to satisfy some of the IRS rules governing PRIs for private foundations.

However, becoming a benefit corporation is not appropriate for every business or in every situation. As a general proposition, in deciding whether to incorporate as a benefit corporation, entrepreneurs should also weigh the following against some of the benefits listed above:

- **Mission alignment is critical.** Far too often, how a company makes money and how it fulfills its charitable purpose are two very different things. Although this is not typically an issue in good times, it can absolutely be a major issue in bad times if a company has to choose between doing good or meeting its financial obligations. For example, if a company decides to donate a certain amount of its goods to charity based on the number of goods it sells to the public, one can easily see how this could create an issue if profit margins narrow or supply chains are disrupted, causing internal conflict in a company’s operations. Better to have direct alignment between how the company makes money and its charitable purpose (e.g. a solar company meets its environmental purposes by selling more solar panels) than to have to plan for what happens on a rainy day and the tradeoffs that come with it.
- **It can be challenging to obtain PRIs or other new forms of capital.** While there are plenty of notable examples of companies that have been able to successfully expand the capital pool with PRIs or other forms of alternative capital, the risk with such an expanded pool is the chance that a company’s fundraising efforts are spread too thin. With so many different sources of capital available to a company, it can sometimes be challenging to prioritize attracting one source of capital versus another. Moreover, which types of capital a company focuses on will also be a market signal to others in the market as to what path a company intends to follow, which can have the effect of turning off some more traditional investors.
- **In a politically charged atmosphere, leading with values can turn off certain consumers or investors.** In the same way that many studies have shown that most consumers prefer to buy goods and services from socially responsible businesses, in a divided culture such as ours, marketing those same values can also have the opposite effect on certain consumers or investors. Said another way, if a company is aligned with a particular worldview or its orientation creates a narrow focus, some consumers or investors may not be interested. While no marketing campaign is perfect and no company will ever be able to capture all of

an entire market, an early-stage company many not want to deal with this additional source of headwind in the marketplace.

These are just a few of the considerations entrepreneurs may want to consider forming (or not forming) as a benefit corporation. At RCCB, we are committed to helping businesses of all types and sizes, and we prioritize working with and supporting companies that can do good while doing well. Whether you are considering forming a benefit corporation or some other type of business entity, our seasoned group of business attorneys, in tandem with our partners at ImpactPHL, can support you with virtually whatever your business needs.

*\* Author's Note: This article specifically focuses on entities formed under Delaware law. While many states (including Pennsylvania) have enacted benefit corporation statutes that are similar to Delaware's in many respects, Delaware corporate law is the closest thing to a national business law code in this country and Delaware is where most of our clients incorporate. Additionally, we will also focus primarily on "benefit corporations" rather than "benefit limited liability companies," although this is mostly out of convenience for purposes of this article rather than anything substantive. Many of the same factors that drive a company to be formed as a benefit corporation versus a traditional corporation will be the same for the company choosing between forming as a benefit limited liability company and a traditional limited liability company.*

## **PROFESSIONALS**

Matthew L. Devine

Alex Seldin

## **CAPABILITIES**

Corporate & Business