
OLR Bill Analysis

sHB 5466

AN ACT CONCERNING SOCIAL ENTERPRISE BUSINESSES

SUMMARY:

This bill establishes a social enterprise business (SEB) as a type of for profit corporation. SEBs are formed primarily to create a social benefit, one that has a material positive impact on society or the environment. Under the bill, they must do so by engaging in one or more specified activities ranging from providing benefits to low-income people to furthering charitable, cultural, scientific, literary, or educational purposes (i.e., “specific public benefits”). SEBs must also distribute at least 20% of their distributed profits to charitable organizations serving the same specific public purpose.

The bill specifies how businesses formed and operating under the business corporation laws can become SEBs. A business can become a SEB by (1) amending its articles of incorporation to specify a specific public benefit as its primary purpose or (2) merging with another business that will become a SEB. Both actions must be approved by the shareholders as the bill specifies and comply with the statutes governing articles of incorporation and business mergers.

The bill specifies the duties and obligations of SEB directors and officers and protects them from liability for decisions made in specified contexts. It limits their fiduciary duty to shareholders, the SEB’s directors, and certain owners.

These parties are the only ones who may bring a “benefit enforcement proceeding” against the directors and officers to fulfill their respective duties and against the SEB to fulfill its social benefit and specified public benefit. They can use the proceedings to bring a claim or action against a director or officer for failing to pursue a social benefit specified in the SEB’s articles of incorporation or violating the

bill's standards of conduct.

The SEB must report annually to its shareholders on the extent to which it achieved its social benefit goals and have an independent third party review its performance every five years.

Lastly, the bill specifies how the SEB must distribute its assets if it dissolves.

EFFECTIVE DATE: January 1, 2013

§§ 1 & 4 — CRITERIA

The bill allows corporations formed under the statutes to establish themselves as SEBs and specifies the criteria for doing so. To become a SEB, the corporation must adopt as its primary purpose to create a material positive impact on society or the environment through one or more of the following specific public benefits:

1. provide beneficial products and services to low-income people and underserved individuals;
2. promote economic opportunities for people and communities beyond creating jobs in everyday business;
3. preserve or improve the environment;
4. improve human health;
5. promote the arts and sciences or advances in knowledge;
6. increase capital flows to entities serving a social purpose;
7. benefit society or the environment in other identifiable ways; or
8. significantly further one or more charitable, cultural, scientific, literary, or educational purposes, as defined in the federal Internal Revenue Code (IRC).

To meet the last criterion, the corporation must operate exclusively for religious, charitable, scientific, literary, or educational purposes;

foster national or international amateur sports competition; or prevent cruelty to children and animals (IRC, § 170 (c)(2)(B)).

Besides creating a specific public benefit, the corporation must distribute at least 20% of any distributed profits to a charitable organization serving the same specific public benefit.

§§ 2 & 3 — PROCEDURE FOR BECOMING A SEB

Method

Under the bill, a corporation can establish itself as a SEB or become part of another corporation that will.

A corporation can establish itself as a SEB by specifying in its articles of incorporation at least one specific public benefit it intends to create. The number of benefits does not limit its obligation to create one. But it cannot adopt a specific public benefit that requires influencing legislation or participating or intervening in campaigns for public office, as specified in IRC, § 170 (c)(2)(D).

Alternatively, the corporation can become a SEB by merging or exchanging shares with another corporation that will become a SEB.

Procedure

Regardless of the method the corporation chooses, it must comply with the statutes for amending articles of incorporation or effecting a merger. Those statutes require shareholders to be notified about the meeting where they must vote on the amendment or merger plan. Under the bill, the corporation's board of directors must state in the notice why it is proposing the action and how it will affect the shareholders.

The action is approved based on the higher of two outcomes: (1) the number of votes required by the corporation's bylaws to approve the action or (2) two-thirds of the votes cast by the outstanding shares. If the bylaws allow a class of shares to vote as a group, then a two-thirds vote of each class is required. If the shareholders approve the action, a shareholder who voted against it may require the corporation to purchase his or her shares for cash at their fair market value.

The corporation can subsequently add, amend, or delete specific public benefits from its articles of incorporation, but the articles must specify at least one such benefit if the corporation intends to remain a SEB. These changes must also be made according to the statutory procedure for changing articles of incorporation.

Maintaining and Enforcing a Code of Conduct and Conflict of Interest Policy

Besides requiring adopting a specific public benefit in its articles of incorporation, the corporation must maintain and enforce an ethical code of conduct and a conflict of interest policy consistent with the highest and best practices for its industry.

§ 5 — SEB DIRECTORS

Fiduciary Duty

Under the bill, SEB directors have a fiduciary duty only to the people entitled to bring a benefit enforcement action against the SEB (see below). They have no such duty with respect to the people who directly benefit from the SEB's specific public benefits.

Decision Making

The bill specifies the factors SEB directors must consider when determining if an action serves the SEB's best interest. A director must consider how an action or inaction affects:

1. the SEB's shareholders, employees, workforce, subsidiaries, and suppliers;
2. the interests of customers who benefit from the SEB's specific social benefits;
3. community and social considerations, including those of any community where the SEB's offices or facilities or those of its subsidiaries or suppliers are located;
4. local and global environment; and
5. the SEB's short- and long-term interests, including whether the

SEB's continued independence would best serve them.

Protections

Under the bill, directors who consider these interests and factors do not violate the standards of good conduct the statutes impose on corporate directors.

The bill also protects directors from liability for specified actions. Directors are not liable if the SEB fails to create a social benefit. Nor are they liable to anyone entitled to bring a benefit enforcement action for acting or failing to act while performing their duties if they did so in compliance with the bill and statutory standards for good conduct.

Lastly, the bill prohibits the SEB from imposing specific conditions or requirements on its directors. The SEB cannot require them to place the interests of any person or group above those of any other person or group unless doing so serves any of the SEB's specific public benefits. Nor can the SEB subject the directors to a different or higher standard of care regarding actions or inactions affecting control of the SEB.

§§ 6 & 7 — SEB OFFICERS

Fiduciary Duty

Like the directors, the SEB's officers have a fiduciary duty only to the people entitled to bring a benefit enforcement proceeding against the SEB. That duty does not extend to people who benefit from any of the SEB's specific public benefits.

Decision Making

SEB officers must consider the same interests and factors that directors must consider when determining if an action or inaction serves the SEB's best interest. An officer must do so with respect to issues over which he or she has discretion. The officer must also consider the interests and factors when it reasonably appears to him or her that a matter could materially affect them or the creation of a social benefit. In these instances, the officer does not violate his or her fiduciary duty to the SEB.

Protections from Liability

The bill protects the officers from liability for specified actions. They are not liable for any action taken in good faith business judgment if they believe it is consistent with:

1. any of the SEB's specific public benefits, as specified in the bylaws or articles of incorporation, and
2. any recognized standard for defining, reporting, or assessing a SEB's corporate and environmental performance (i.e., third party standard).

The standards must have been developed by an organization independent of the SEB. Further, the standards must be easily understood because the public can obtain the factors needed to measure the SEBs performance, their relative weights, and the identity of the people who develop and control changes to the standards and the process for changing them.

The bill also protects officers from liability from a benefit enforcement proceeding for acting or failing to act while performing their duties in compliance with the SEB's bylaws, as the law requires.

Social Enterprise Officer

The bill allows SEBs to designate social enterprise officers to perform those duties related to the SEB's public benefit, as specified in the bylaws or prescribed by the board of directors or a supervising officer. But any prescribed duties must be consistent with the bylaws.

§ 8 — BENEFIT ENFORCEMENT PROCEEDING

The bill allows specified groups to bring a benefit enforcement proceeding against the (1) directors and officers to fulfill their respective duties and (2) SEB to fulfill its social benefit and specified public benefit. The proceeding can be brought only by:

1. shareholders otherwise entitled to start or maintain a proceeding on any basis with regard to the right of the SEB;

2. SEB directors;
3. people who own beneficially or of record at least 10% equity interest in an entity of which the SEB is a subsidiary; or
4. other people or entities the SEB's articles of incorporation specify.

§ 9 — ANNUAL BENEFIT REPORT

Content

SEBs must submit annual benefit reports to shareholders in a format approved by their boards of directors. A report must describe the SEB's goals or outcomes for creating social benefits or any specific public benefit. It must:

1. specify the goals or outcomes;
2. describe the actions the SEB took to achieve them and the extent to which it succeeded;
3. describe any obstacles that prevented the SEB from attaining the goals or outcomes or creating the social benefit or any specific public benefit; and
4. specify the shareholder-approved goals or outcomes for the next report period.

The report must (1) assess the SEB's social and environmental performance based on third-party standards and (2) specify how it will improve its performance and attain the goals and outcomes for creating social benefits. The third-party standards must be the same ones that were used to assess social and environmental performance in other reports. If the current report does not use these standards to assess this performance, it must explain why.

The report must provide information on the SEB's finances, including a copy of the SEB's compensation plan, budget, and balance sheet. It must also identify the accounting method used to prepare these documents and list:

1. the 1% of the SEB's most highly compensated employees,
2. the SEB's financial investors, and
3. each person who owns beneficially or of record at least 5% of the SEB's shares.

Lastly, the report must provide a copy of the SEB's code of conduct and conflict of interest policies and list each director and officer, his or her mailing address, and, with respect to the directors, how much each was compensated during the year.

Distribution

The SEB must annually deliver the benefit report to each shareholder within one 120 days after the SEB's fiscal year ends or at the same time it delivers any other annual report to its shareholders. It must also publish the report on its website. When it delivers and publishes the report, the SEB must also deliver a copy to the secretary of the state.

Five-Year Independent Third Party Reviews

Every five years, the SEB must obtain an independent third party to review its annual benefit report and assess its social benefit and specific public benefit for consistency with the SEB's articles of incorporation.

§ 10 — DISSOLUTION

The bill specifies how a SEB must apply and distribute its assets if it dissolves. The SEB must pay, satisfy, and discharge all of its liabilities and other obligations or adequately provide for this to happen. It must also transfer or convey the assets it received or held to one or more SEBs or charitable organizations with a similar social benefit.

BACKGROUND

Related Bill

sSB 403, which the Commerce Committee reported favorably on March 27, allows individuals and institutions to form "low-profit limited liability companies," for profit businesses formed to attract

private investment and philanthropic capital to provide social benefits. The bill specifies the criteria a limited liability company (LLC) must meet to qualify as a low-profit LLC and makes conforming changes in the LLC statutes.

COMMITTEE ACTION

Commerce Committee

Joint Favorable Substitute

Yea 13 Nay 4 (03/27/2012)