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BENEFIT CORPORATIONS

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You asked for information on benefit corporations including how they differ from traditional corporations, how other states changed their laws to allow them, and whether Connecticut considered any bills on benefit corporations.

SUMMARY

Benefit corporations are one of several new business entities being proposed around the country as an alternative to traditional for-profit and non-profit entities. Benefit corporations are like traditional corporations but they must state in their articles of incorporation that they have a purpose of creating a "general public benefit." A "general public benefit" is a material, positive impact on society and the environment, as measured by a third party standard, through activities that promote a combination of specific public benefits. Benefit corporations may also identify the specific public benefits that they seek to create.

Seven states currently have benefit corporation laws: California, Hawaii (which calls them sustainable business corporations), Maryland, New Jersey, New York, Vermont, and Virginia. In all of these states, benefit corporations must declare their intention to create general and specific public benefits in their articles of incorporation. These state laws have a number of provisions in common.

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1. Shareholders must vote to become a benefit corporation, terminate that status, modify the specific public benefits that it will pursue, or merge with another entity. New York requires a ¾ vote while the remaining states require a $^{2}/_{3}$ vote.

2. Creating the general or specific public benefits is considered in the benefit corporation's best interests.

3. Directors must consider certain factors when making decisions about what is in the corporation's best interests, including the effect on shareholders, employees, suppliers, customers, the community, and the environment.

4. Directors are generally protected from liability if (a) they comply with the benefit corporation laws or (b) the corporation does not create a benefit. Some states limit claims against the corporation or directors for failing to create a benefit or meet the standard of conduct to "benefit enforcement proceedings."

5. The corporation must publish an annual benefit report (a) describing how it performed on the general and specific public benefits that it sought to create and (b) assessing its societal and environmental performance according to third-party standards.

6. Generally, other corporation laws apply unless they conflict with the specific benefit corporation law.

Some states have additional provisions, such as requiring the corporation to designate a benefit director or benefit officer.

A number of states are also considering benefit corporation bills this year. Connecticut has not yet considered any bills on benefit corporations.

More information on benefit corporations can found on various websites, including benefitcorp.net which includes a list of benefit corporations around the country. The low-profit limited liability company (L3C) is another new form of business organization that is being considered around the country. For more information on these entities, see OLR Report 2011-R-0344.

STATE LAWS

Seven states currently have benefit corporation laws.

1. California (Corporations Code § 14600 et seq.),
2. Hawaii (Hawaii Rev. Stat. § 420D-1 et seq.),
3. Maryland (Corporations and Associations Code § 5-6C-01 et seq.),
4. New Jersey (N.J.S. § 14A:18-1 et seq.),
5. New York (Business Corporation Law § 1701 et seq.) (New York law also authorizes public benefit corporations but these entities are quasi-public authorities such as the port authority.),
6. Vermont (11A V.S.A. § 21.01 et seq.), and
7. Virginia (Virginia Code § 13.1-782 et seq).

These laws have a number of provisions in common. The sections below highlight the most important features of these laws and some of the variations among the seven states.

Specific Public Benefits

All of the state laws allow a benefit corporation to designate one or more "specific public benefits" that it will attempt to create. They all include the following as "specific public benefits":

1. providing low-income or underserved individuals or communities with beneficial products or services (Maryland applies this to all individuals and communities);
2. promoting economic opportunities for people and communities, beyond creating jobs in the normal course of business;
3. preserving the environment;
4. improving human health;
5. promoting the arts, sciences, or advancing knowledge;

6. increasing the flow of capital to entities with a public benefit purpose; and

7. accomplishing any other particular benefit for society or the environment.

Hawaii also includes as a “specific public benefit,” using patent rights to:

1. create and retain Hawaiian and U.S. jobs;

2. uphold fair labor standards in the U.S. and internationally by prohibiting child or forced labor, employment discrimination, restrictions on freedom of association, and denial of the right to collectively bargain; or

3. enhance environmental protection in the U.S. and internationally.

Directors

All of the state laws require directors to consider certain factors when determining what is in the corporation’s best interests. Typically, this requires them to consider the effects on the:

1. shareholders;

2. corporation’s, subsidiaries’, and suppliers’ employees and workforce;

3. interests of customers as beneficiaries of the general or specific public benefit purpose;

4. community and society including the community where the corporation, a subsidiary, or supplier has offices or facilities; and

5. local an global environment.

Some states specify additional considerations. Four states (California, New Jersey, Vermont and Virginia) require directors to consider the corporation's short- and long-term interests including benefits that may accrue from long-term plans and the possibility that these interests and the corporation's public benefit purposes may be best served by the corporation's continued independence. California and Virginia also explicitly require directors to consider the corporation's ability to achieve its general and specific public benefit purposes.

Most states also allow directors to consider other factors or interests of other groups that the directors consider appropriate. A few states specify other effects that directors may consider. For example, California, Hawaii, New York, and Virginia specify that a director may consider the resources; intent; past, stated, and potential conduct of anyone seeking to acquire control of the corporation.

Most of the states (California, New Jersey, New York, Vermont, and Virginia) state that a director need not give priority to a particular person's interests under these factors over the interests of another unless the corporation has stated its intention to do so.

Most of the states (1) protect directors from liability if they comply with the benefit corporation laws and if the corporation fails to create a public benefit and (2) specify that a director has no duty to a person that is a beneficiary of the corporation's public benefit purpose.

Benefit Director. Hawaii, New Jersey, and Vermont require the corporation to designate someone as benefit director. The benefit director must be independent of the corporation and Hawaii additionally requires that he or she have no material relationship with the corporation.

While the corporation can designate additional responsibilities for the benefit director, all three states require him or her to prepare the annual benefit report and state an opinion whether (1) the corporation acted according to its public purposes in all material respects and (2) directors and officers complied with their duties under this law. The benefit director must describe any failures by the corporation or directors to meet those standards.

Officers

Four states require an officer to consider the same interests and factors as a director when making certain decisions. Hawaii and New Jersey require this when the officer (1) has discretion in a matter and (2) it reasonably appears that the matter may have a material effect on any of the interests or factors or creating the public benefit. California and Vermont require it when the officer either has discretion or there may be a material effect.

These states also provide protections from liability for officers. These protections vary by state but include protection from liability if the (1) officer performs his or her duties complying with the law or (2) corporation fails to create a benefit. California and Vermont provide that an officer has no fiduciary duty to a person who is beneficiary of the public benefit.

Benefit Officer. Hawaii, New Jersey, and Vermont require or allow the corporation to designate a benefit officer to perform management duties related to the corporation's general or specific public benefits. If a corporation has a benefit officer, Hawaii and New Jersey require the officer to prepare the annual benefit report.

Benefit Enforcement Proceeding

Four states (California, New Jersey, Vermont, and Virginia) only allow a claim against the corporation or a director under the benefit corporation laws in a "benefit enforcement proceeding." These states specify that such a claim can be brought by the corporation or a shareholder, director, and certain others. The claims are against a director or officer for (1) failing to pursue the general or specific public benefit purpose or (2) violating the duty or standard of conduct under these laws. California, New York, and Virginia also allow such an action to enforce the annual benefit reporting requirement.

California includes additional provisions that (1) the corporation is not liable for money damages for failing to create a benefit and (2) a court that finds a failure to comply with the benefit corporation law without justification can award the plaintiff reasonable expenses including attorney's fees.

Annual Benefit Report

All of the state laws require the benefit corporation to give shareholders an annual benefit report and post it on its public website (if it does not have a website it must provide a free copy to anyone on request). The report must:

1. describe how the corporation pursued a general public benefit and any designated specific public benefit, the extent the benefits were created, and circumstances that hindered creating the public benefit and

2. assess the corporation's societal and environmental performance according to third-party standards.

Vermont requires more specific details. The report must state specific goals or outcomes for creating the benefits, actions taken to achieve those goals or outcomes, what hindered attaining them, specific actions the corporation can take to improve its social and environmental performance and attain its goals or outcomes, and specific goals or outcomes for the next reporting period.

Some states require additional information including:

1. the compensation paid to corporate directors and the names of people owning 5% or more of its shares (Hawaii, New Jersey, New York, and Vermont) and

2. the names and addresses of (a) directors and officers (Hawaii and New Jersey) or (b) the benefit director and officer (Vermont).

Third-Party Standard. All of the states require using a third-party standard for defining, reporting, and assessing the corporation's social and environmental performance. An independent person or entity must develop the standard and the factors used to measure performance, their relative weightings, and who develops and can change them must be publicly available.

In addition, California and Hawaii require identifying the:

1. directors, officers, material owners, and governing body of the third-party organization;

2. process for revising the standard;

3. process for changing membership of the third-party organization; and

4. sources of the organization's financial support and any relationships that could reasonably be considered to present a potential conflict of interest.

California also requires the entity to (1) have no material financial relationship with the benefit corporation or its subsidiaries and certain others, (2) use necessary and appropriate expertise to assess overall corporate social and environmental performance, and (3) use a balanced multi-stakeholder approach with a minimum 30 day public comment period to develop the standard.

California and New York require the annual benefit report to describe the benefit corporation's process and rationale for selecting the 3rd party standard. California and Hawaii also require the report to describe any connections the corporation has with the entity establishing the 3rd party standard.

Opinion. California requires the benefit corporation's board to include a statement in the report on whether they failed to pursue benefits in all material respects. If the board's opinion is that they did not, they must describe how they failed. In Hawaii, New Jersey, and Vermont, the benefit director must state an opinion in the report whether (1) the corporation acted according to its public purposes in all material respects and (2) directors and officers complied with their duties under this law. The benefit director must describe any failures that occurred.

Finalizing the Report. Hawaii and Vermont require additional procedures before finalizing the report.

1. In Hawaii, the corporation must post its draft report on its public website or make it otherwise publicly available for a 60 day public comment period. The final report must include formal responses to all questions, concerns, comments, and suggestions raised during the comment period.

2. In Vermont, shareholders must approve or reject the report by a majority vote after a reasonable opportunity for review.

Government Filing. New Jersey and New York require filing the report with a state agency. In New Jersey, failure to file for two years forfeits the corporation's status as a benefit corporation, but it is automatically reinstated when the report is filed.

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