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### **B Corps & Benefit Corporations—Getting to Know Them By Julia Cheng, Esq.**

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#### ***The Emergence of B-corps and Benefit Corporations***

Global climate change, deteriorating environmental conditions, decreasing energy resources, the cyclical financial crisis, and high unemployment rates have prompted many entrepreneurs to become mindful of the social and environmental impact they exert on their surroundings through their business activities. Traditionally, under the law, directors and officers could be sued for decisions that do not result in maximizing shareholder value. Such a structure led to the unfortunate event where the founders of the environmentally and socially conscious Ben and Jerry's Ice Cream were forced to sell their company to the highest bidder, Unilever, under shareholder pressure. Changing environmental and social conditions along with the fear among entrepreneurs of forced sales of their companies to less civic-minded companies have propelled the call for operating companies where social and environmental values are taken into serious account in making major company decisions, also known as the "triple bottom line."

As of this spring, seven states have passed laws allowing the formation of benefit corporations, including New York and California. Unlike traditional corporations, benefit corporations are *required* to create a general public benefit, and directors and officers are protected should they take into account non-financial values in major company decisions.<sup>1</sup> B Lab, a non-profit organization, has offered certification programs where companies can be certified as a B Corp upon meeting certain comprehensive and transparent social and environmental performance standards. As a business lawyer, I have been approached several times by clients with questions as to the differences between incorporating as a benefit corporation under state laws, being certified as a B Corp by B Lab, and how both differ from a nonprofit organization. Through this article I wish to answer these questions, as well as provide

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<sup>1</sup> In California, there is also a category of corporations called the flexible purpose corporations. Unlike benefit corporations, flexible purpose corporations are not obligated to pursue a generalized public benefit, but rather, one or more special purposes as provided in the statute.

information that I hope will be helpful to readers should they be interested in becoming a benefit corporation. This article will focus on benefit corporations in New York and California.<sup>2</sup>

### ***B Lab—Certified B Corps***

To begin, any for-profit company, whether it be a sole proprietorship, an LLC, or a corporation, can be certified as a B Corp by B Lab. B Lab is a nonprofit organization based in Pennsylvania that developed the concept of benefit corporations. Companies interested in applying for certification must complete several tasks. First, applicants must take and pass the B Impact Assessment, which is an online exam assessing the applicant company's labor and environmental practices. Questions on the assessment vary depending on the company's size and sector, and usually take 60-90 minutes to complete. **As this assessment evaluates whether or not your company is eligible to apply for certification, prior to taking the assessment, it does not hurt to print out a copy of the assessment, look through their questions to gauge how ready your company is for certification and if not, what needs to be improved.**

Once your company passes the B Impact Assessment, B Lab will then conduct a phone interview with you to discuss your responses to the B Impact Assessment. The interview usually takes 60-90 minutes, and can be scheduled on line. Based on the interview, B Lab may ask you to submit additional documents to support your responses to the B Impact Assessment.

The next step will be adopting the B Corporation Legal Framework, which entails amending the company's governing documents to make the company's commitment to social and environmental causes legally binding. **By adopting the B Corporation Legal Framework, the company is bound by law to take social and environmental factors into consideration when making major company decisions.** Shareholders and any parties specified in the company's governing documents will have the right to bring lawsuits. Officers and directors will be protected in the event they consider social and environmental factors other than maximizing shareholder profits in making decisions. If the company is already incorporated as a benefit corporation under state laws (see discussion below), the company is deemed to have adopted the B Corporation Legal Framework.

The final step involves signing a Term Sheet that makes the certification official, provided that the company pays annual certification fees ranging from \$500 up to \$20,000 depending on

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<sup>2</sup> Please note that laws regarding benefit corporations vary from state to state. Therefore, it is important that you consult with an attorney familiar with benefit corporations in your state when considering the entity as an option.

company sales figures. The certification is good for two years and needs to be recertified as standards evolve. Also, to maintain the accuracy of the certification, B Lab will conduct on-site reviews on 10% of B corps. Once certified, the company will be searchable as a certified B Corp on B Lab's website.

### ***Benefit Corporations Under State Laws***

**To begin, a company does not need to be certified by B Lab in order to register as a benefit corporation under state laws.** The company can become a benefit corporation by fulfilling the state legal requirements as set forth below. One thing worthy of note is, whereas companies certified by B Lab can be searched via B Lab's website, one cannot tell whether if a company is indeed a benefit corporation under applicable state laws (at least in California and New York) as the state databases so far do not provide information as to whether a corporation is a traditional corporation or a benefit corporation. One will need to examine the actual incorporation documents to ascertain whether or not the company is, indeed a benefit corporation under state laws. **Until the states update their database systems, this may cause a company to lean in favor of seeking certification by B Lab as an additional step to increase visibility.**

A new company can incorporate as a benefit corporation by including the following statements in its incorporation document: (1) a statement that it is a benefit corporation, and (2) if desired, adding one or more specific purposes as listed in the relevant state statutes, such as assisting low-income individuals, promoting economic opportunity, preserving the environment, improving human health, promoting arts and sciences, increasing the flow of capital to entities with a public benefit purpose, and accomplishing any other particular environmental/social benefit.

An existing company can become a benefit corporation under state laws: (1) by amending its incorporation document and filing the amended document with the State if the company is a corporation, or (2) by merger or conversion to a benefit corporation if the company is not a corporation. **Prior to filing an amendment, merging, or converting, the company will need 3/4 (soon to be 2/3) shareholder approval for a New York company,<sup>3</sup> and 2/3 shareholder approval for a California company.** The company can terminate its status as a benefit corporation by again, seeking 3/4 (soon to be 2/3) shareholder approval for a New York company and 2/3 shareholder approval for a California company. **Note that current New York and California laws only allow companies to operate as a benefit corporation in the legal**

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<sup>3</sup> The required vote under the original statute is in the process of being reduced from 3/4 to 2/3 by a proposed amendment to the statute. S. 6088, 112<sup>th</sup> Cong (2012).

**form of a corporation as opposed to any other entities. If the existing company is not a corporation (such as an LLC), and wishes to maintain its non-corporation form, the company cannot take advantage of the state benefit corporation laws.**

**Of particular attention that needs to be paid to companies treated as benefit corporations under state laws is the annual reporting requirement, which is not required under certification by B Lab. Directors and officers can be held accountable for failure to deliver annual reports.** Each year, the benefit corporation is required to file an annual report with the state that compares the company's social and environmental performance against an independent third party standard and distribute the report through its website and to shareholders. In California, if the company does not have a website, it will need to provide a report to any person that requests a copy. The report will need to discuss the company's pursuit of the general or specific public benefit, the extent to which they were actually achieved and any obstacles. **Last but not least, the reports to be delivered to shareholders are required to list names of persons owning 5% or more of the company's outstanding stock, and the compensation paid to each director.** Whereas the laws do not specifically state which third party standards are acceptable, examples of third party standards are B Impact Assessment, Global Reporting Initiative, Green Seal, Green America, International Organization for Standardization, People4Earth Business Framework, Food Alliance ISO 26000, and the UL Environment-ULE 880. **It may be worth taking the time to look into these third party standards to see how your company measures up in terms of social and environmental performance against their criteria.**

### ***B Corps, Benefit Corporations and... Non-Profit Corporations?***

To add to the confusion, as mentioned by several of my clients, are the differences between B Corps/benefit corporations and non-profit corporations. **The key difference is, as of the date of this article, B corps and benefit corporations in New York and California are treated no differently from traditional companies in terms of taxation.**<sup>4</sup> In addition, as B corps and benefit corporations are for-profit structures, these entities can attract outside investors whereas a nonprofit cannot. Note though, in event you seek to raise money not through investors, but rather, through donations and grants, most of the time foundations will require you to be a so-called 501(c)3 nonprofit. Last but not least, B corps and benefit corporations can pay people whatever compensation they wish to attract top talent, whereas nonprofits may raise eyebrows from the IRS or state agencies in event the salaries are excessive.

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<sup>4</sup> This may change in the future as the City of Philadelphia does accord benefit corporations certain tax benefits.

## **Conclusion**

Like all other major decisions in business, choosing the right form of entity for your company is not always an easy task. It requires careful consideration of various factors, among them the mission of your company, the interest of stakeholders such as shareholders, donors, personnel and the audience or market whom you serve, and, of course, tax consequences. Company can operate as a benefit corporation either through certification by B Lab or fulfilling state legal requirements, or both. The concept of benefit corporations is relatively new and is yet to be tried in courts and hence, it is difficult to gauge the enforceability or viability of the model. However, the intention behind the movement is positive, and one can always welcome additional flexibility in doing business.

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