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Generations Summer 2021 - Impact Investing: Renewed Interest in 'Benefit Corporations'

This is the third in a series of articles about impact investing, which is generally understood to denote investments made with the intention of generating positive, measurable social and environmental impact, and a financial return. For a general overview of impact investing and a discussion of how to develop an impact investing strategy and measure the social impact of investments, please refer to the first article in this series, "Impact Investing: How to Define Your Goals and Measure Your Impact." The second article in our series, "Impact Investing: Finding Profit Through Purpose," analyzed the assumption that investors expect lower returns on impact investments, and it provided strategies to maximize the financial returns of impact investments. In this article, we provide insight into benefit corporations and explain why an impact investor should consider benefit corporations when implementing an impact investing strategy.

Distinction from Certified B Corporations or "B Corps"

Benefit corporations are often discussed with but are distinct from certified B corporations, which are referred to as "B corps."[1] A benefit corporation is a legally designated, for-profit corporate entity such as a limited liability company, partnership or corporation that voluntarily meets higher standards of corporate purpose, accountability and transparency than those that apply to traditional business corporations. Because benefit corporations are creatures of state corporate law, there is some variation from state to state in the requirements to qualify as a benefit corporation.[2] However, state statutes generally require that a benefit corporation (i) pursue a general public benefit with a material positive impact on society and the environment; (ii) consider the impact of corporate decisions on all stakeholders, including shareholders, employees, customers, the community and the environment; and (iii) annually report to shareholders on its overall social and environmental performance against a third-party standard.[3] At this time, benefit corporation statutes have been enacted in 37 states in the United States, the District of Columbia and Puerto Rico and are pending in four states.[4] In contrast, certified B corporations are organizations that have been certified by B Lab, an independent third-party nonprofit organization, as meeting B corporation standards. B corporation standards measure a business entity's accountability, community involvement, treatment of employees and consumers, and environmental impact. B Lab does not limit B corporation certification to any particular corporate form, which makes certification an attractive option for businesses formed in a state without a benefit corporation statute. An entity formed as a benefit corporation does not have to become certified by B Lab or any other private or governmental organization to qualify as a benefit corporation, but many benefit corporations (including Patagonia) subsequently become B corps because the certification carries additional value and the credibility of third-party oversight.

Appeal of Investing in a Benefit Corporation

Benefit corporations, such as Warby Parker, have been able to raise funding from top-tier mainstream investors including Founders Fund and First Round Capital. And they are not alone—according to reports, 295 venture-backed benefit corporations raised approximately $2.5 billion between 2013 and 2019,[5] and research from B Lab revealed that as of May

2017, almost every Silicon Valley venture capital firm had invested in at least one benefit corporation.[6] In addition, two benefit corporations—Lemonade Inc., a property and casualty insurance company, and Vital Farms, Inc., a provider of eggs and dairy products from humanely and pasture-raised animals—successfully completed initial public offerings in 2020. A third benefit corporation—education technology company Coursera, Inc.—went public on March 31, 2021. In February 2021, Veeva Systems Inc. became the first public company to convert to a benefit corporation, and other public companies have announced that they are exploring conversion. At the same time, retail and institutional investors, led by Larry Fink at BlackRock,[7] have found benefit corporations to be increasingly attractive because of their required consideration of all stakeholders and integrated reporting to shareholders.[8] Investors see value in benefit corporations for several reasons, but the following features of benefit corporations are particularly valuable to the impact investor: **Accountability and greater transparency.** Benefit corporations offer access to operational, sustainability and impact data that is not presented in traditional financial statements. Benefit corporations are required annually to define, assess and report on key impact metrics. This typically comes in the form of an annual report, which must be provided to shareholders and may also be published, containing an assessment of the corporation's social and environmental performance against a third-party standard.[9] The report also describes how the benefit corporation pursued its general public benefit; the ways in which such benefit was created, hindered or challenged; and the process and rationale for selecting the third-party standard used in the assessment.[10] This information can reduce due diligence costs and risks for impact investors, who seek reliable ways to measure the impact of their investments. Although there are several third-party standards from which to choose, many benefit corporations use the B Impact Assessment, a free tool offered by B Lab for assessing corporate social and environmental performance. This tool allows investors to compare performance across companies and industries.[11] The most recent annual benefit reports of Patagonia, King Arthur Flour and Kickstarter are publicly available. **Corporate purpose is impact-driven.** Benefit corporations commit to creating public benefit and sustainable value in addition to generating profit. State statutes and the tax code also treat benefit corporations as for-profit enterprises, even though the legal focus of such entities may contrast sharply with that of traditional business corporations, which require a board of directors to maximize shareholder value. The added value of benefit corporations over B corp certification and other corporate forms is the legal protection to pursue the stakeholder model. More specifically, the business judgment of the board of directors of a benefit corporation is protected under state law, which empowers and directs the board to affirmatively consider and balance the impact of its decisions on all stakeholders. This protection ensures that the directors consider the company's general public benefit in corporate decision-making and that decisions are impact-driven. At the same time, shareholders of benefit corporations retain all the protections that they have in the traditional corporate model, including corporate governance, voting rights and the ability to bring lawsuits.

How Soon Is Now?

Benefit corporations and B corps are fertile territory for both the impact-first and the financial-first impact investor, because the requirements of benefit corporation or certified B corp status address many important concerns of impact investors, particularly reliable impact measurement and accountability through annual reporting to shareholders. The key distinction of the benefit corporation is the underlying proposition that long-term value is not created by focusing solely on shareholder value but rather by considering and balancing the interests of all stakeholders. Although research comparing the financial returns of benefit corporations and B corps to traditional corporations that pursue the shareholder primacy model is lacking, the proposition that long-term value is created when all constituencies are considered in corporate decision-making is closely aligned with impact investors' goals. The benefit corporation model requires companies to simultaneously pursue profits and purpose, which is the fundamental objective of the impact investor.

[1] For a comprehensive discussion of the differences between benefit corporations and B corps and how the benefit corporation structure relates to B corporation certification, refer to "Benefit Corporations & Certified B Corps," Benefit Corporation.

[2] For example, the General Corporation Law of the State of Delaware uses the term "public benefit corporation," which is defined as "a for-profit corporation organized under and subject to the requirements of this chapter that is intended to produce a public benefit or public benefits and to operate in a responsible and sustainable manner." General Corporation Law of the State of Delaware, Section 362 (2015).

[3] Notably, Delaware law does not require benefit reports to use a third-party standard as an assessment tool.

[4] "State by State Status of Legislation," Benefit Corporation.

[5] Michael B. Dorff, James Hicks and Steven Davidoff Solomon, "The Future or Fancy? An Empirical Study of Public Benefit Corporations," 2020.

[6] Rick Alexander, "How Investors Really Feel About B Corps," B the Change, May 24, 2017.

[7] Larry Fink, "A Sense of Purpose," Annual Letter to CEOs, BlackRock. See also, Larry Fink, "A Fundamental Reshaping of Finance," Annual Letter to CEOs, BlackRock.

[8] See, generally, "Just Good Business: An Investor's Guide to B Corps."

[9] "A Legislative Guide to Benefit Corporations."

[10] *Ibid.* See also, B Lab, "Benefit Corporation Reporting Requirements."

<p">[11] B Lab, "How do I pick a third party standard?" See also, B Lab, "B Impact Assessment." </p">

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