

# California Benefit Corporations: An Introduction

08.31.16 | Linda J. Rosenthal, JD



In recent years, the social enterprise model of business “with conscience” has been springing up all around the world.

In “[Social Enterprises: A Revolution Under the Radar](#),” we explained that California has been a leader of this emerging movement within the United States.

What brought about the development of an innovative, hybrid concept of corporate structure? Simply put, neither the traditional, *for-profit* nor the rigid *nonprofit* format fit the bill.

### **California’s “Benefit Corporation”**

Each jurisdiction that has jumped on the bandwagon of this novel theory of corporate structure has fashioned its own statute.

California is unique in that it has adopted not just one but *two* hybrid formats: the “benefit corporation” and the “social purpose” corporation (originally called the “flexible purpose” corporation)

Here, we’ll focus on the primary variation, the “benefit corporation.” which is organized as a *for-profit* business, but with a twist: In addition to the general business purpose of making a profit, the benefit corporation *must* create “... general public benefit,” and “*may* identify one or more specific public benefits that shall be the purpose or purposes....” (*emph. added*)

In carrying out these purposes, the directors and officers must take into account *multiple* interests, not just the bottom line of increasing profits for the shareholders.

This is new, uncharted, territory in corporate law.

”

---

*The board of a benefit corporation, which must pursue the general public benefit in its corporate activities, must consider the impact of its business decisions on the entity’s employees, its suppliers, the environment, and the community at large. But how such considerations balance against consideration of the shareholders’ interests is still to be determined.*

Which interests predominate, or take precedence?

***How is this Accomplished?***

There are two key questions for directors and officers. First: What are the rules about carrying out these multiple purposes? Second: How can directors and officers fulfill their duties *and* stay safe from liability for their actions in making choices and operating the benefit corporation.

For now, we’ll focus on the rules themselves. We’ll discuss “safe harbors” and other protections from liability in subsequent posts, as well as additional disclosure and reporting responsibilities.

***Compare: Traditional For-Profit***

In a regular California corporation, the purpose is to carry on any lawful business activity (or a narrower, more specific purpose), but the bottom line is the goal of maximizing value for the shareholders.

The directors have fiduciary obligations to the corporation and its shareholders to act in good faith and with due care (under a reasonably prudent person standard) and to promote the corporation’s best interests.

The only permissible focus is generating profits. Directors are not guarantors, though, of the actual success of the business, so long as they exercise these duties of good faith and due care.

***Benefit Corporations***

In a benefit corporation, the obligations of the directors are described the same but – and this is the key distinction – in the benefit corporation, there are *multiple purposes* including (at least) a general public purposes (and possibly, one or more specific public purposes). There are also multiple impacts and interests that must be considered when making decisions for the corporation. No single purpose takes priority or precedence over any other. So benefit corporation directors have a more complex task.

Because the benefit format is so new, we have little to go on right now beyond the words of the enacting statute: California Corporations Code sections 14610 *et seq.*, and in particular, sections 14620-14623.

***General Rule***

Here’s how the statute begins:

”

---

14620(a). A director shall perform the duties of a director including duties as a member of any committee of the board upon which the director may serve, in good faith, in a manner the director believes to be in the best interests of the benefit corporation and with that care, including reasonable inquiry, as an ordinarily prudent person in a like position would use under similar circumstances.

So far, so good. It's identical to the language in the section describing the duties of a regular, for-profit corporation director.

**Directors: Considering “Impacts”**

Then, the distinction arising from *multiple* purposes appears, as the Corporations Code discusses the mandatory “impacts” – that is, people and issues – that must be considered:

”

---

14620(b). In discharging their respective duties, and in considering the best interests of the benefit corporation, the board of directors, committees of the board, and individual directors of a benefit corporation **shall** consider the impacts of **any** action or proposed action upon **all** of the following:

- The shareholders of the benefit corporation.
- The employees and workforce of the benefit corporation and its subsidiaries and suppliers.
- The interests of customers of the benefit corporation as beneficiaries of the general or specific public purposes of the benefit corporation.
- Community and societal considerations, including those of any community in which offices or facilities of the benefit corporation or its subsidiaries or suppliers are located.
- The local or global environment
- The short-term and long-term interests of the benefit corporation, including benefits that may accrue to the benefit corporation from its long-term plans and the possibility that these interests may be best served by retaining control of the benefit corporation rather than selling or transferring control to another entity.
- The ability of the benefit corporation to accomplish its general, and any specific, public benefit purpose.

That's certainly a rather staggering list of “impacts” that directors *must* consider in taking “any action or proposed action”! (The use of “shall” in a statute indicates that what follows is mandatory. It's not discretionary, and it's not “pick and choose” one or more if you feel like it.)

Sometimes in section 14620(b), the reference is *only* to people or interests connected directly with the benefit corporation itself. But in other instances, there are references to people or interests connected *as well* with any subsidiaries or suppliers.

These nuances and complexities of the required analysis is why we've included the full language of the statute rather than merely summarizing or paraphrasing it.

The key point is that shareholders' interests are no longer treated as primary to, or exclusive of, other interests – as is the case with regular, for-profit corporations.

***Directors: What Else May Be Considered***

In the next subsection, directors are given some additional leeway (“may” means optional) in possibly considering . . . well, . . . almost anything else:

Section 14620(c). In discharging their respective duties, the persons described in subdivision (b) may consider any of the following:

*The resources, intent, and conduct, including past, stated, and potential conduct, of any person seeking to acquire control of the corporation.*

*Any other pertinent factors or the interests of any other person or group.*

The only apparent limitation is that any such other factors be “pertinent.”

***Officers: When and What They Must Consider***

The Corporations Code includes additional section describing the duties of “officers” in certain situations. Here, the term “officers” means the “chairman of the board or a president, or both, a secretary, a chief financial officer and such other officers with such titles and duties as shall be stated in the bylaws or determined by the board ....”

In many organizations, the top paid staff member may or may not be such an officer. In terms of these statutory mandates, it's important to keep straight who is wearing which “hat.”

*Section 14622(a). Each officer of a benefit corporation shall consider the interests and factors described in Section 14620 in the manner provided in that section when either of the following applies:*

*The officer has discretion to act with respect to a matter.*

*It reasonably appears to the officer that the matter may have a material effect on any of the following:*

*The creation of a general or specific public benefit by the benefit corporation.*

*Any of the interests or factors referred to in subdivision (b) of Section 14620.*

**Conclusion**

This is an extraordinarily broad – and vague – list of items that must considered when directors and officers of a California benefit corporation make decisions.

If this exciting, new “social enterprise” format did not carry so much promise for dealing with important issues in today's world, it might be entirely reasonable to dismiss it as just too complicated

and unsettled.

But (as we'll cover in later posts), there's also broad protection for directors and officers and, over time, more guidance will emerge. So – for now – buckle your seat belts, and settle in for an interesting ride.