

Flexible Purpose Corporations: Come January 2015, They will be Social Purpose Corporations

10.10.14 | Linda J. Rosenthal, JD



California has been in the forefront of the recent movement to facilitate establishment of social enterprises: for-profit corporations that are authorized to make money *and* benefit society. The Legislature authorized two new corporate models: “benefit corporations” and “flexible purpose corporations.” Socially conscious businesses were permitted to form – or convert into – these new hybrid formats beginning January 1, 2012.

But in just the second year of this new corporate format, the author of the original enabling legislation proposed – and the Legislature passed – important follow-up amendments to the Corporate Flexibility Act of 2011 to “strengthen and improve” it and to “achieve greater flexibility to combine shareholder profitability with one or more additional special purposes.” In September, Governor Jerry Brown signed the new law, which goes fully into effect on January 1, 2015.

New Name

A key change is a new name for the corporate format originally called a “flexible purpose corporation.” The name of the law is changed to the Social Purpose Corporation Act; all corporations formed under this law will be known as “social purpose corporations.” According to the bill’s author, this new name “more accurately reflect[s] the spirit of the law.” The law changes many corresponding references in the statute to reflect this name change.

Any corporation formed as a flexible purpose corporation before the first of next year continues its corporate existence but will be known as a social purpose corporation.

An interesting note: The only significant opposition to the 2013 bill was from the California Association of Nonprofits. This group’s objections were to the new name only, not the rest of the bill. Specifically, the organization asserted that the original name, flexible purpose corporation, was

adopted after careful consideration as an accurate and useful description of the new format. The group did not believe that any change was warranted:

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The proposed term “social purpose corporation” will mislead the public into confusing such corporations with nonprofit organizations, leading to them mistakenly to think that these corporations are tax-exempt nonprofits. As a result they may make donations of goods and/or investments of cash in the mistaken belief that they are donating to a nonprofit. The conflation of nonprofit and for-profit corporations has already proven to be a source of confusion for Californians.

Change in Director Duties

Another important element in the new law is that directors of a social purpose corporation are now required to take into consideration when making decisions the special mission and purpose of the corporation in carrying out their duties. Under the 2011 law, directors were encouraged to do this, but it was not mandatory.

Also, another feature under the old law that was voluntary for smaller flexible purpose corporations has been made mandatory for all social purpose corporations. The exemption to the requirement to report to shareholders has been eliminated.

Easier Status Changes

The Act makes it easier for out-of-state firms to form or to switch status to become a California social purpose corporation. But it also adds more protections for dissenters’ rights.

There are also changes to the California Corporations Code to become more in line with other states’ successes in encouraging businesses to pursue a socially conscious mission.