Board Procedures for Public Benefit Corporations

Summary:

In 2013, Delaware adopted legislation authorizing a corporation created in Delaware to become a Public Benefit Corporation (a "PBC"). The new law (like its counterparts, now adopted in more than 30 U.S. jurisdictions) allows for-profit companies to operate in a manner that sustainably creates long-term value for its shareholders and others. Specifically, the Delaware law defines a PBC as a for-profit corporation that

> is intended to produce a public benefit or benefits and to operate in a responsible and sustainable manner[1]

The statute does not define "responsible and sustainable," but instead mandates that the directors must balance the interests of its shareholders with the public benefits it has identified in its charter,[2] and with the interests of those materially affected by the corporation's conduct.[3] The Delaware law gives directors broad discretion with respect to such balancing,[4] and allows corporations to eliminate monetary liability for disinterested directors making such balancing decisions.[5] The statute also requires that the corporation provide its stockholders with a report (a "Benefit Report") at least once every two years. The report must include:

- the sustainability objectives established by the board;
- standards adopted to measure progress in promoting those objectives;
- factual information based on those standards regarding the corporation's success in meeting the standards; and
- an assessment of the corporation's success in meeting the standards.

Thus, in order to operate in a responsible and sustainable manner and meet its reporting requirements, the board of a PBC should engage in a continuing process of:

1. determining who is materially affected by the corporation's business,
2. developing and maintaining criteria for balancing both the interests of those so effected, as well as any specific benefit identified in the corporation's charter, and
3. measuring progress against those criteria.

The board may determine that some or all of the balancing obligations may be met by adopting one or more third party standards, and engaging in a continuing process of measuring against those standards. This will allow for a process that both meets compliance obligations <u>and</u> provides directors with continuing education and best practices on the company's social and environmental impact objectives.

The list below is an example of procedures a board may adopt in order to ensure that it is properly attending to the balancing question. There is no requirement that these particular procedures be followed.

Committee

- Establish a stand-alone committee or delegate sustainability issues to audit, governance or other committee.
- Include in committee charter oversight of and/or recommendation with respect to:
    - Third party standards, if any
    - Internally generated standards
    - Choice of certifying body or bodies, if any
    - Benefit Report
    - Sustainability objectives and standards
    - Sustainability strategies and policies

Management Role

- Recommendations on third party standards and internally generated standards
- Recommendations on certification issues
- Recommendation of sustainability objectives and standards
- Recommendation of sustainability strategies and policies
- Report on progress toward impact objectives
- Draft Benefit Report

Periodic Activity

- Cycle should be synchronized with benefit reporting period
- Sustainability objectives to be established and assessed on an annual basis
- Quarterly committee meetings
- Quarterly report to Board, with longer session once or twice a year, giving Board significant opportunity to balance those materially affected, identified public benefits, and stockholders' pecuniary interests
- Board to approve Benefit Report and impact objectives

Non-Periodic Activity

- Management charged with bringing significant sustainability issues to the board that come up out of cycle and that are not covered by policies (e.g., effect of a strategic change or product change on workers or customers; significant building projects)
- Committee should consider sustainability issues implicated by new developments (e.g., whether to purchase renewable energy or obtain LEED certification for new buildings, effect of a transaction on workers' compensation or customer access).
- Committee may make balance decision, or decide to take balance question to Board based on significance; should report any decision to board

Process Issues

- Management recommendations to committee and committee recommendations to board should be distributed well in advance of committee and board meetings in order to give directors adequate time to review
- Where possible, directors should print out material to read, rather than reading on line

- Where materials update prior materials, directors should be provided with redline copies, so that they can focus on changes
- Minutes should reflect sustainability issues discussed, resolution of those issues, and any direction given to the committee or management
- Internal checklists should be reviewed to determine whether sustainability issues should be added
- Where third party or internal standard is adopted, materials and minutes should reflect consideration of how standard maps to interests of those effected by the corporation's conduct

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[1] 8 Del. C. § 362.

[2] The statute requires a PBC to identify a public benefit or benefits in the statement of business or purpose (which is included in the certificate of incorporation filed with the Delaware Secretary of State). "Public benefit" is defined as "positive effect (or reduction of negative effects) on 1 or more categories of persons, entities, communities or interests (other than stockholders in their capacities as stockholders) including, but not limited to, effects of an artistic, charitable, cultural, economic, educational, environmental, literary, medical, religious, scientific or technological nature." 8 Del. C. § 362.

[3] The statute requires that the "board of directors manage or direct the business and affairs of the public benefit corporation in a manner that balances the pecuniary interests of the stockholders, the best interests of those materially affected by the corporation's conduct, and the specific public benefit or benefits identified in its certificate of incorporation." 8 Del. C. § 365.

[4] The statute essentially mandates the business judgment rule for balancing decisions, providing that with respect to balancing decisions, a director will be deemed to satisfy the director's fiduciary duties "if such director's decision is both informed and disinterested, and not such that no person or ordinary, sound judgment would approve." Id.

[5] Id. The statute also provides that the directors balancing obligations do not create duties to any person, and can be enforced only by stockholders owning at least 2% of the corporation's stock (or in the case of a public company, at least $2,000,000 worth of stock).