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ADVOCATES

How to Become a Colorado Public Benefit Corporation

This outline summarizes the major steps involved in becoming a Colorado public benefit corporation – a new form of corporate entity that has a purpose to produce public benefit as well as financial return.

> *Note: This outline is general information only, not legal or tax advice. Before taking any steps to become a public benefit corporation, businesses should obtain legal and tax advice specific to their situation.*

What is different about a PBC?

A public benefit corporation differs from a traditional corporation in three principal ways:

Purpose. A public benefit corporation is intended to operate in a responsible and sustainable manner, and has a corporate purpose to promote one or more public benefits, which must be described in its articles of incorporation. The public benefit language affects your company's legal responsibilities, so craft it with care.

Accountability. A traditional corporation must prioritize the financial interest of its shareholders. In contrast, the directors of a PBC have a fiduciary duty to manage the PBC's business in a way that balances three factors:

- the financial interest of the shareholders,
- the best interests of those materially affected by the PBC's conduct, and
- the PBC's public benefit purpose(s).

This obligation is enforceable by shareholders holding at least 2% of the PBC's stock, but not by other stakeholders such as employees or customers. If they choose, PBCs may add language to their articles that protects their directors against monetary liability for failure to meet this balancing requirement.

Transparency. A public benefit corporation is required to prepare an annual public report that:

- describes how the company has promoted its public benefit purpose(s) and the interests of those materially affected, and
- assesses its overall social and environmental performance against a third party standard.

If you are organizing a new corporation…

A public benefit corporation is a corporation, not an LLC or partnership. So if you organize as a PBC, your company will be taxed as a corporation (either C corp or S corp). Article 55 and Article 56 cooperatives also are eligible. A cooperative can elect PBC status and still be taxed as a cooperative.

Considerations that apply when forming a traditional corporation also generally apply to PBCs. For example, if the company will have more than one owner, it's best to implement share transfer restrictions, as you would in any other corporation.

In addition, organizers of a public benefit corporation will include in their articles of incorporation:

- a company name that includes "public benefit corporation" or "P.B.C." or "PBC";
- a statement that the company is a public benefit corporation;
- one or more public benefits that the company will pursue; and
- optionally, language limiting the directors' liability.

If you are electing PBC status for an existing Colorado corporation…

Existing Colorado corporations may become PBCs by amending their articles of incorporation to include the four elements in the bulleted list above.

The amendment must be approved by shareholders holding at least two-thirds of each class of shares, including any non-voting shares. Dissenters' rights apply. (See below for more on dissenters' rights.)

If your company is not organized as a Colorado corporation…

If your company is not currently taxed as a corporation, consider the tax impact of converting to corporate form. (See below for more on change of tax status.)

If you are converting to a Colorado PBC from an LLC, from any other non-corporate form of entity, or from another state of incorporation, you are changing your form of entity. That will require new governing documents. It could also affect existing contractual requirements or licenses you may hold. (See the question on "due diligence" below.)

If your company is a professional corporation, or other form of entity to which special statutory rules apply, you'll need to check on the ability of that specific form of entity to convert into a PBC.

What are dissenters' rights?

Dissenters' rights are a special form of minority shareholder protection that applies in certain transactions – usually a sell-the-company deal such as a merger. A shareholder who opposes the transaction has the right to demand payment of the "fair value" of their shares in cash, instead of whatever they would receive for their shares in the transaction.

Where dissenters' rights apply, shareholders must be given notice of those rights before the transaction is approved, and that notice should be accompanied by a disclosure document describing the transaction. If the company and the dissenting shareholder disagree on valuation, fair value is determined by a court proceeding.

Electing to become a PBC is a dissenters' rights transaction, so shareholders potentially could require the company to buy them out before proceeding with the change. Therefore, if your company has any outside investors, it is important to plan your shareholder approval process carefully.

Would becoming a PBC change your company's tax status?

A PBC is taxed as a corporation. If your company is not currently taxed as a corporation, and converts to a PBC, it will be taxed as a corporation going forward (either C corp or S corp). For example, an LLC is usually taxed as a partnership, so converting to a PBC would involve a change of tax status.

If your company is currently taxed as a corporation (or cooperative), becoming a public benefit corporation will not change its tax status.

If your company is not taxed as a corporation, consult your tax advisor about the tax impact of converting to corporate form.

What is involved in changing your company's name?

Becoming a PBC changes the legal name of your company. Make appropriate changes to your bank accounts, and anywhere else the full legal name of your company is used, including stock certificates. Branding will not be affected, if it does not include the entity identifier at the end of your company name (such as "Inc.").

What other due diligence is needed?

If you are converting from another form of entity or state of incorporation, the conversion may trigger contractual requirements for third party consent or notice, and could affect any permits or licenses you hold. Before proceeding, carry out a "due diligence" review of such matters.

Even if your company is currently a corporation, certain kinds of contracts (such as bank loans) could include requirements for notice or consent before amending your articles of incorporation. Check with your lawyer about looking for provisions like that in your agreements.

How do you file the paperwork?

The documents to become a PBC are filed online with the Colorado Secretary of State, and resemble the filing process for traditional corporations.

Adopting benefit corporation status involves a significant change to legal rights and responsibilities. Before deciding that the public benefit corporation form is right for your business, we recommend consulting an attorney who is knowledgeable about the new entity.

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About the author…

Seth Henry, a lawyer at Blue Dot Advocates, helped draft the Colorado benefit corporation legislation, and worked extensively with the stakeholder group that negotiated its final form. Blue Dot Advocates is a law firm serving companies and investors who seek to use business as a tool for the common good. We have counseled numerous clients on using the benefit corporation and other forms of structural mission protection. If you are considering organizing a benefit corporation, or converting your existing business into a benefit corporation, we would be happy to assist.

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