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'Public Benefit' Corporate Model Is Making Inroads

By **Tom Zanki**

Law360 (May 14, 2021, 2:31 PM EDT) -- More businesses are going public as "public benefit corporations," a legal designation that signals a company's commitment to goals beyond maximizing profits, though the jury is still out on whether carrying such a label actually generates positive social impacts.

In the last 10 months, at least five companies went public as PBCs. And more could follow suit, as some venture-backed startups considered initial public offering candidates have already converted to this structure.

A PBC is a for-profit company whose charter specifies its intent to pursue a public benefit — be it environmental, social or other goals — alongside its commitment to serve stockholders' best interests. The state of Delaware, where many public companies incorporate for business or tax reasons, potentially accelerated this trend by making it easier to become a PBC.

The First State last summer reduced stockholder-voting requirements to convert to a PBC from two-thirds to a simple majority, while strengthening legal protections for boards of directors, among other things. At least three dozen states have passed benefit corporation legislation.

The budding momentum follows a Business Roundtable statement in 2019 urging corporations to move beyond shareholder primacy and embrace a stakeholder-oriented mission that takes a business' relationships with broader constituencies into account. Given recent legal changes, as well as growing interest among companies and investors to publicly support environmental, social and governance, or ESG, goals, some attorneys expect more companies to convert to a PBC.

"We're seeing greater incidences of companies that are considering the move to PBC status," Mintz Levin Cohn Ferris Glovsky and Popeo PC partner Tom Burton said, calling it a "critical and fundamental change" away from the idea of shareholder primacy.

"It allows for a very clear and unambiguous recognition of focuses by the corporation beyond merely making money to shareholders," Burton said. "That's a pretty big deal."

Recent PBCs to go public include synthetic biology company Zymergen Inc. and online educator Coursera Inc., both of which raised at least $500 million in IPOs since March that priced at the high end of their ranges. Pasture-raised eggs producer Vital Farms Inc. and technology-focused insurance platform

Lemonade Inc. priced above-range IPOs last summer.

Sustainable farming company AppHarvest Inc. also went public through a merger with a special purpose acquisition company in February. These companies follow the 2017 IPO of Laureate Education Inc., which said it was the first PBC to go public on any stock exchange.

PBC directors are responsible for balancing the interests of stockholders with those of constituencies materially affected by the company's conduct — be it employees, consumers or the surrounding community — and the public benefit specified in the corporation's charter. The three-part balancing act is considered broader than the fiduciary standard applicable to directors of traditional companies, which only requires that they act in the best interests of stockholders.

Freshfields Bruckhaus Deringer LLP partner Pamela Marcogliese said Delaware's amended statute governing PBCs affords directors flexibility, requiring them to consider three sets of interests without mandating how they balance them. The law also enables directors to be more deliberative in how they factor multiple interests, Freshfields partner Sarah Solum added.

"It makes it possible for the company's board to be upfront about how they think about their various constituents, whether it's employees or customers, or the communities in which they operate, alongside their stockholders," said Solum, who advised Zymergen's IPO with Marcogliese.

Attorneys say likely candidates for PBC status are companies whose cultures and business models already reflect a mission-driven approach.

Vital Farms touts itself as an ethical food company committed to the humane treatment of farm animals and sustainable farming, while Zymergen said its "biofacturing" process creates products in a more environmentally friendly manner than traditional chemistry. Lemonade said it donates "excess premiums" to nonprofit institutions selected by its customers as part of its "giveback" program.

PBCs are required to report biennially on how they are meeting their benefit objectives. Such appeals could attract customers or workers who want to support a company committed to certain values and also attract investors, given the growth of ESG-focused mutual funds. But whether converting to a PBC is necessary to achieve mission-oriented goals is open to debate.

Ann Lipton, a professor at Tulane University Law School, said corporate managers have wide discretion to benefit non-shareholder constituencies under the "business judgment" doctrine, which is intended to shield directors from frivolous lawsuits on the presumption they are acting in good faith to serve corporations and their stakeholders absent clear evidence to the contrary.

Lipton said what impedes more boards from serving a stakeholder-oriented mission is that shareholders unhappy with management's priorities can vote out directors and make such companies ripe for takeovers. She said benefit corporation laws don't alter that dynamic, making the impact of such laws more aesthetic than actually binding companies to a social purpose.

"The way the laws are set up now, they're incredibly weak," Lipton said. "It is almost impossible to sue a benefit corporation for not actually pursuing the benefit."

The five companies that recently went public as PBCs say they are taking legal and business risks by assuming PBC status, according to Securities and Exchange Commission disclosures.

The companies told regulators they could be subject to derivative suits if they fail to balance shareholder and public benefit interests, a liability that doesn't exist for traditional corporations. PBC shareholders must own a minimum number of shares before they can file suit.

Several PBCs also warned they could become less attractive takeover candidates and that share prices could fall if they balance their interests in ways that shareholders don't like. Companies normally warn investors of scenarios in which their stock may drop as part of standard risk disclosures.

Marcogliese added that PBC status doesn't insulate a company from investor scrutiny, be it for their financial performance or whether they are achieving their stated public benefits.

"It doesn't prevent an activist or a shareholder from bringing shareholder proposals or trying to run a proxy contest or approaching management with grievances," Marcogliese said. "You're still under the scrutiny of shareholders for everything you do as a public company."

Ultimately, multiple companies said they believe their stock performance won't be affected by PBC status, betting that doing well financially and doing a public good can go together.

"We do not believe that an investment in the stock of a public benefit corporation differs materially from an investment in a corporation that is not designated as a public benefit corporation," Lemonade and Zymergen said in similar disclosures, adding they believe achieving PBC goals "will not materially affect the financial interests of our stockholders."

Companies are also betting that PBC status will benefit their culture and recruitment strategy.

"Being a PBC gives our employees, board and shareholders a clear understanding of what we value as a company, and sets expectations about how we are authorized to set the company strategy," Zymergen chief science officer and co-founder Zach Serber said in a statement. "It's our north star and helps us attract and retain like-minded people."

Several notable private companies also apparently see reputational benefits to being a PBC, including outdoor clothing company Patagonia and shoemaker Allbirds, which is considered a "unicorn" with a private valuation north of $1 billion and is a rumored IPO candidate.

More PBCs could also go public through mergers with blank-check companies. Sustainable Development Acquisition I raised $275 million in a February IPO, filing as a public benefit corporation. The company said it hopes to acquire a profitable business that advances the United Nations' Sustainable Development Goals.

"I would say that we're in the early days of a real and substantial trend," Burton said. "And that when you look back, five years from now, it is going to be very common to see companies structured as PBCs."

--Editing by Philip Shea and Alyssa Miller.