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Benefit Corporations and Certified B Corps—What's the Difference?

As social enterprises and impact investing gain popularity, alternative for-profit legal forms, such as benefit corporations and certifications, for example B Corporations (B Corps), have emerged to meet the needs of businesses and investors committed to social and environmental impact. Although the terms are often used interchangeably, "benefit corporations" and "B Corps" are different in important ways. Understanding the key features and strategic uses of these alternative legal structures and certifications is important, especially for social entrepreneurs, NGO sponsors, and impact investors. While these can be helpful tools for social enterprises, it is important to note that firms can maintain a mission and achieve social and environmental impact without adopting an alternative legal structure or pursuing a certification when the mission or impact is baked into their business model. This ultimately may be more important than the "virtue signaling" label of the benefit corporation or Certified B Corp.

Alternative Legal Structures for Social Enterprises

While traditional for-profit corporate entities are legally required to focus on maximizing shareholder value, many US states have adopted social enterprise legislation that allows firms to consider other stakeholders without breaching fiduciary duties to shareholders. Under these statutes, social enterprises pursue a dual mission of profit and public benefit by adopting an alternative entity structure such as a benefit corporation, benefit LLC, or low-profit limited liability company (L3C).

The decision to adopt an alternative legal structure requires a firm to carefully consider its goals, including the type of funding it seeks to attract. These structures can raise questions with traditional investors as to whether return is being compromised for public impact. It may be difficult for investors to understand the different features of these legal structures, leading to a potential hesitancy to provide capital. On the other hand, there are mission or impact investors who are attracted to these legal structures because such investors believe these structures reflect a commitment to stakeholder and not just shareholder interests.

There is little precedent to determine how effective these structures are for shielding directors from claims of breach of fiduciary duty by considering broader stakeholder interests. Currently, most benefit corporations are private, and the risk of shareholder claims is limited because benefit corporations and Certified B Corps tend to attract mission or impact investors.

This article will focus on the Delaware public benefit corporation (there is also a corresponding Delaware public benefit limited liability company), but it is important to understand that the social enterprise statutes are not standardized across states. Currently, there is significant variation as to the structures of these entities and the implications for investors.

Delaware Public Benefit Corporations (PBCs)

A public benefit corporation (PBC) is a legal status in Delaware (layered on top of the traditional corporate status) for businesses that want to balance profit-making with social and environmental missions. Unlike traditional corporations that prioritize shareholder value, PBCs must operate responsibly and sustainably—in addition to profits, PBCs must consider how their decisions materially affect a broader group of stakeholders including employees, customers, the community, and the environment. This dual-purpose approach is embedded in the company's charter and legal obligations, contributing to long-term mission alignment.

The Delaware PBC statute and benefit corporation legislation in other states generally emphasize three key features: purpose, accountability, and transparency. The transparency component of the Delaware statute gives PBCs more flexibility than benefit corporations in other states.

<u>Key Features</u>

1. <u>Purpose</u>: The Certificate of Incorporation of a PBC must identify one or more specific public benefits to be promoted by the corporation. Often called "mission lock-in," the PBC's legal structure helps formalize the company's mission, protecting it from being overridden by profit-maximizing pressures. There is, however, an "escape valve" if investors decide to reverse this mission lock—the public benefits established in the Certificate of Incorporation may be amended or eliminated by a vote of at least two-thirds of the outstanding stock. Similarly, any merger or reorganization materially altering or eliminating a PBC's public benefit may be approved by a two-thirds vote. This escape valve has been used in the case of the sale of certain well-known benefit corporations.

2. <u>Accountability</u>: Alongside shareholder interests, directors are required to consider the interests of other stakeholders materially affected by the corporation's conduct. This formal recognition of public benefit objectives can enhance a company's credibility with consumers, partners, and investors.

3. <u>Transparency</u>: To increase transparency, PBCs must provide regular reports to shareholders no less than every two years on their social and environmental performance. While many states require benefit corporations to publish an annual benefit report, Delaware PBCs are only required to publish a report every two years and are not required to use a third-party standard. Additionally, Delaware PBCs are only required to make this report to their own shareholders, rather than to the public.

Certified B Corporations (B Corps)

B Corp certification is a voluntary designation awarded by the nonprofit, B Lab, to for-profit companies that meet rigorous standards of social and environmental performance, accountability, and transparency. B Corp certification serves as a third-party validation of a company's impact practices but does not necessarily alter the company's legal entity status. Certified B Corps must be for-profit businesses, but the certification can be achieved by various entity types, including corporations, cooperatives, LLCs, professional corporations, and LLPs. B Corp certification signals a company's commitment to social and environmental impact, building credibility and trust with consumers and impact-focused investors. Certification may also help companies stand out in a crowded market by demonstrating their commitment to higher standards of purpose and performance.

<u>Key Features</u>

1. <u>Rigorous Standards</u>: Companies must score at least 80 out of 200 points on the B Impact Assessment, which evaluates their impact on workers, customers, community, and the environment. Achieving B Corp certification signals to investors that the company is purpose-driven and is committed to creating "benefit for all" stakeholders.

2. Accountability: All Certified B Corps are required make a legal commitment to stakeholder governance and must amend their governing documents to include the consideration of all stakeholders in their decision-making, not just shareholders or investors. S Corps and C Corps seeking B Corp certification must register as a benefit corporation in their state to legally opt out of the default shareholder primacy. Small companies must meet this legal requirement prior to finalizing their B Corp certification. Subsidiaries (regardless of size) and larger companies must satisfy the legal requirement within two years of certifying. Certain Certified B Corps have abandoned their status and opted not to make the conversion after going public, but others have not.

3. Transparency: Certified B Corps must make a public B Corp profile and publish their B Impact Report on B Lab's website. To maintain the certification, Certified B Corps must recertify every three years.

Strategic Uses of PBCs and Certified B Corps in the Fund Context

1. Locking in Mission: Using an alternative legal structure or obtaining B Corp certification can effectively "lock in" a social enterprise's mission, even though it is not permanently "locked" because of the "escape valve" discussed above.

2. Attracting Impact-First Investors: Depending on the investors a firm wants to attract, it must be thoughtful about opting into these alternative forms and certifications. Impact-first investors who prioritize achieving social or environmental outcomes over financial returns are often drawn to alternative legal structures and Certified B Corps. These investors seek assurance that their capital will be used to drive meaningful impact and benefit multiple stakeholders. For traditional investors, however, alternative structures and Certified B Corps may raise concerns about trading returns for impact.

3. Enhancing Fund Appeal: Funds that are NGO or tax-exempt sponsored often consider an alternative structure or Certified B Corp as a manager to help bridge the gap between a tax-exempt sponsor and a for-profit management entity. This approach can be perceived as locking mission into the management of the fund and can be combined with management compensation tied to achieving impact or fulfilling a mission.

Conclusion

Alternative legal structures and B Corp certifications are powerful tools for social enterprises committed to creating social and environmental value. For social entrepreneurs, NGO sponsors, and impact investors, these structures offer a means of embedding mission, enhancing credibility, and attracting impact-first capital. By understanding and leveraging the benefits of alternative structures and Certified B Corps, businesses and funds can align their operations with their values and drive sustainable, impactful growth. Firms must be strategic about the implications of these forms and certifications for their specific goals and the types of investors they are trying to attract. It is important to note that firms can maintain a mission and achieve social and environmental impact without adopting an alternative legal structure or pursuing a certification when the mission or impact is baked into their business model. This ultimately may be more important than the "virtue signaling" label of the benefit corporation or Certified B Corp.

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For more information on the issues discussed here, please contact your Morgan Lewis Impact Investing attorney.

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Morgan Lewis has one of the nation's leading Impact Investing practices and in June 2024 was ranked as one of two firms in Band 1 by *Chambers* in its inaugural rankings for Impact Investing in the United States.

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