

FOR GOOD AND FOR PROFIT: THE EMERGENCE OF THE MARYLAND BENEFIT CORPORATION

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When starting a new business (or reorganizing an existing one) those leading the decision-making process face a variety of choices, including the type of entity. In addition to the typical entity choices (e.g., stock corporation, nonstock corporation, limited liability company), those with mission-driven, public benefit goals in mind also evaluate whether the business is best organized as a tax-exempt entity. A concern for mission-driven businesses has long been the ability to balance profit maximization with mission-related goals. Although there are advantages to being tax-exempt, the primary requirement of a tax-exempt organization is that it not provide a private benefit. Therefore, entrepreneurs who want to provide societal benefits typically feel caught between their mission-related goals and their desire to profit from the business. The same concerns affect the ability of mission-driven businesses to raise capital.

In an apparent effort to address those concerns and become a leader in the area, Maryland recently created a new type of corporation, the “benefit corporation,” that requires for-profit corporations opting into its framework to include societal and environmental considerations in their decision-making processes. As a result, a Maryland benefit corporation (“MBC”) is meant to combine public benefit goals with profit-making goals.

What Is a Maryland Benefit Corporation?

Although Vermont is close on its heels, Maryland is the first state to adopt legislation establishing benefit corporations.¹ Some are referring to the MBC as a for-profit/not-for-profit hybrid – a potentially distorting moniker because the benefit corporation is still a for-profit corporation. For the most part, an MBC will be organized and operated in the same manner as a “traditional” corporation.² The main distinction between a traditional Maryland corporation and an MBC is the factors that will be considered in certain decision-making processes. In a traditional corporation, directors must make decisions subject to their fiduciary duties to the corporation’s stockholders, which are often interpreted to require short-term profit maximization, without giving weight to any broader societal or mission-driven considerations. In contrast, MBC’s are required to weigh broader considerations in making decisions and not to give priority to any one factor, including profit. Taking considerations other than profit into account when measuring performance is commonly referred to as triple-bottom line analysis.

The devil is ultimately in the details, and while the MBC legislation is specific about requirements on some fronts, an MBC’s founders (or reorganizers) will have flexibility on many others - just as they would with a traditional Maryland corporation.

¹ The legislation, which takes effect October 1, 2010, adds a new subtitle 6C to title 5 of the Maryland Corporations and Associations Article (“C.A.”). Specifically, the new benefit corporation provisions will be codified as C.A. sections 5-6C-01 through 5-6C-08. See http://mlis.state.md.us/2010rs/chapters_noln/Ch_98_hb1009T.pdf.

² See new C.A. § 5-6C-02(A).

What Are the Requirements for a Maryland Benefit Corporation?

There are two primary requirements for an MBC: (1) the purpose of the MBC must be to create a “general public benefit” and (2) the benefit must be measured by a third-party standard. In addition, a corporation must affirmatively elect to be an MBC and comply with certain annual reporting requirements.

General Public Benefit

Under the statute, an MBC must have the creation of a general public benefit as a purpose. A corporation will satisfy the general benefit requirement if its purpose is to create a material, positive impact on society and the environment through activities that promote a combination of “specific” public benefits. The following benefits are considered specific public benefits, and may be separately noted in the MBC’s charter:

- providing individuals or communities with beneficial products or services;
- promoting economic opportunity for individuals or communities beyond the creation of jobs in the normal course of business;
- preserving the environment;
- improving human health;
- promoting the arts, sciences, or advancement of knowledge;
- increasing the flow of capital to entities with a public benefit purpose; or
- the accomplishment of any other particular benefit for society or the environment.³

Third-Party Standard

As noted above, to be an MBC it is not enough to simply have the necessary purpose. In addition, the impact created by the purpose must be measured by a third-party standard. There is little guidance with respect to what will constitute an acceptable third-party standard. The statute states that the third-party standard must be a “transparent” standard that is developed by a person or entity independent of the MBC for “defining, reporting, and assessing best practices in corporate social and environmental performance.”⁴

One likely candidate for an acceptable third-party standard is included in the certification elements of the “B Corporation” framework established by B Lab, a Berwyn, Pennsylvania-based non-profit organization. B Lab has been a leading proponent of benefit corporation legislation and established a rating system for certifying triple-bottom line companies according to five categories. Once certified, the companies are subject to periodic audits.⁵ B Lab is also a member of a consortium of government, private sector and nonprofit groups that is

³ New C.A. §§ 5-6C-01(D) and 5-6C-06(B).

⁴ New C.A. § 5-6C-01(E).

⁵ See <http://www.bcorporation.net/become>.

developing a global rating system, called Global Impact Investing Rating System (“GIIRS”), which was recently endorsed by the Obama administration.

While B Lab’s rating system and GIIRS should be acceptable standards, it remains to be seen whether a standard that was not created for the purpose of rating triple-bottom line companies could be used. For example, the United States Green Building Council’s LEED certification system is an accepted method for measuring a building’s energy and environmental impact. Would compliance with LEED requirements and certification satisfy the third-party standard requirement if one of an entity’s specific benefits is preserving the environment?

Why Would an Organization Want to Be a Maryland Benefit Corporation?

Incorporating as an MBC provides two principal advantages. First, it removes any doubt that directors may consider factors other than profit in making decisions for the company. Second, it requires assessment of those other factors against a third-party standard.

At the core of the MBC is the legal creation of triple-bottom-line companies. An MBC is required by law to consider public benefit purposes when determining what is in the “best interests” of the corporation. Historically, even in states where it was permissible to include language in a charter allowing directors to consider the interests of non-stockholder stakeholders (e.g., employees, local communities), there has been a residual concern that shoehorning such language into a charter left directors exposed to litigation. The lack of express statutory authority to consider both public benefits *and* stockholder value creates a perception that stockholder value should have precedence. The MBC legislation attempts to lessen or eliminate the exposure (real or perceived). The statute also makes it clear that the directors do not owe any duty to non-stockholder stakeholders that are beneficiaries of the MBC’s public benefit purposes.⁶ Therefore, incorporating as an MBC removes any uncertainty that may exist regarding the ability of the business to give equal weight to economic, environmental and societal considerations.

In addition to the perceived profit requirement, mission-driven companies have been impeded by the inability of investors to measure the achievement of the mission-related purposes. The requirement that an MBC have measurable (and measured) goals, provides credibility and accountability to the MBC.

Further, in contrast with a tax-exempt organization, the MBC may provide private benefits to investors in the form of profits. Existing non-profit organizations may also find it attractive to use the MBC as the form of entity for any for-profit subsidiaries or ventures in which it wants to engage. Although there is no established tax advantage to the use of the MBC, a non-profit (and potential donors) may be more comfortable engaging in a for-profit enterprise if the enterprise is subject to certain public benefit requirements.

Conclusion

With the emergence of a state-recognized benefit corporation, the hope is that capital markets will view benefit corporations favorably, and, thereby, increase opportunities for mission-

⁶ New C.A. § 5-6C-07(B).

driven businesses.⁷ By removing both the fiduciary duty concerns and requiring third-party measurements, MBC's may be more attractive to institutional investors than traditional corporations.

While some of the desired results of being an MBC remain quite speculative, some banks, socially responsible private equity firms and angel investors, and private foundations are already lending to or investing in companies that have included public benefit considerations in their organizational documents outside of the MBC framework. The MBC should be an attractive alternative to such "mission investors." Traditionally, mission investors have concentrated on environmental protection, health, economic development, education and housing, so we anticipate "early adopters" of MBCs to come from those industries.

The MBC is not for every business that has a mission-related component. However, it provides another option for many businesses. In addition to the traditional choice-of-entity considerations, the organization should consider the following factors, among others, in evaluating whether an MBC is the right entity for it:

- Is the entity going to be soliciting capital from third parties? If so, who are the potential investors?
- Will the investors come from the traditional capital markets (i.e., venture funds, institutional investors)?
- Will the investors have a "mission" focus or a profit focus?
- If the investors are not "mission" investors, could they be turned off by the potentially competing interests of stockholders and stakeholders?
- How critical is the maintenance of the "mission" to the organizers?
- What third party standard would apply to the business?

If you are interested in working through whether a benefit corporation might make sense for your organization, or if you have other business needs, please contact Brian Cyr (bcyr@rosenbergmartin.com) or Jessica Lubar (jlubar@rosenbergmartin.com) at (410) 727-6600 or another attorney in our corporate or transactional tax groups:

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⁷ See

http://www.bcorporation.net/resources/bcorp/documents/2010_Term_Sheet_Constituency_States_LLCS_LLPS2.pdf.