

**PROPOSED LEGISLATION TO AMEND CHAPTER 607, FLORIDA STATUTES,
TO PROVIDE FOR THE CREATION OF A
FLORIDA SOCIAL PURPOSE CORPORATION AND A
FLORIDA BENEFIT CORPORATION**

MEMORANDUM OF THE BUSINESS LAW SECTION OF THE FLORIDA BAR

January 15, 2014

SUMMARY

The proposed legislation, currently filed as SB 654, calls for amending Chapter 607, Florida Statutes (the “Florida Business Corporation Act”), to add two supplements (Parts II and III; Part I being the existing statute) that would allow for the creation of two new forms of corporate enterprise, one form called a “Social Purpose Corporation” (ss. 607.501-513), the other called a “Benefit Corporation” (ss. 607.601-613). Each of these enterprises will allow entrepreneurs and investors to cause their corporation to engage in significant societal benefit programs that may not involve or satisfy the traditional corporate norm of profit maximization.

The proposal provides for alternative forms of enterprise. The principal difference between a Social Purpose Corporation and a Benefit Corporation is the statutory public benefit purpose imposed upon each of the corporations. A Social Purpose Corporation has the statutory purpose of pursuing or creating one or more public benefits which may be quite specific (s. 607.506). In contrast, a Benefit Corporation has the statutory purpose of pursuing or creating a “general public benefit,” which is a broad purpose intended to encompass many societal and environmental factors that are impacted by the business and operations of the corporation (s. 607.606). If the founders of the corporation desire to pursue a focused public benefit, the Social Purpose Corporation would be their likely choice. If the founders desire to pursue broad public benefit goals, including environmental, employee, community and other societal factors, the

Benefit Corporation would be the likely choice of enterprise.

DIRECTOR AND OFFICER MANDATE

A key provision applicable to both types of corporations is that the directors and officers are mandated to consider the effects of any corporate action or inaction upon the benefit goals of the corporation (ss. 607.507 and 607.607). This is a major difference from standard corporate law, which does not impose such a mandate.

DIRECTOR AND OFFICER IMMUNITY AND ACCOUNTABILITY

Although directors and officers are mandated to consider the benefit goals of the Social Purpose or Benefit corporation, a failure to pursue or achieve one or more of the benefit goals will not result in the imposition of any personal liability against the directors or officers, unless the corporation's articles of incorporation expressly provide otherwise (ss. 607.507(2) and 607.607(2)). This immunity from personal liability is appropriate, as directors and officers of all corporations, including these new types of corporations, are still required under their duty of care obligation to consider the overall economic welfare of the corporation. Although a Social Purpose or Benefit Corporation may have been formed with public benefit purposes, circumstances might cause the directors and officers to choose not to pursue such benefit goals because of economic or other factors relative to the corporation's short or long-term viability.

The immunity from personal liability, however, does not shield directors and officers from accountability. The legislative provisions for each of these new types of corporations (a) require a so-called Annual Benefit Report to be sent to each shareholder each year describing the efforts made during the year to achieve the corporation's benefit goals (ss. 607.512 and 607.612) and (b) provide for a so-called "benefit enforcement" judicial proceeding that may be brought by a shareholder or certain others alleging that the directors and/or officers have failed to satisfy

their obligations in making corporate decisions (ss. 607.511 and 607.611). Such judicial actions may result in injunctive relief, but no monetary penalties can be assessed against the directors or officers. Moreover, shareholders who are dissatisfied with decisions made (or not made) by the directors have the power under Chapter 607 to remove current directors from office and to elect new directors who presumably would more effectively pursue the applicable public benefit purpose(s).

INTERFACE WITH FLORIDA BUSINESS CORPORATION ACT

Both the Social Purpose Corporation and the Benefit Corporation are formed pursuant to Chapter 607, the Florida Business Corporation Act. All provisions of the Florida Business Corporation Act apply to each of these new forms of enterprise to the extent not otherwise covered by the specific provisions set forth in ss. 607.501 ff. and ss. 607.601 ff.

REVENUE POSITIVE IMPACT

Adoption of the legislative proposal will be revenue positive for the State of Florida, both directly and indirectly. Corporate attorneys and organizations familiar with such new forms of enterprise advise that there is a growing desire among entrepreneurs and investors to create corporations that have specific or general public benefit purposes. Numerous corporations have been formed to date in the 20 states that have thus far adopted analogous legislation. Each newly formed or converted Social Purpose or Benefit Corporation will pay the filing fees and additional periodic fees applicable to all corporations organized in the State of Florida. Because the formation and periodic reporting processes are consistent with those applicable to ordinary business corporations, there will be no need for additional administrative infrastructure to handle formations and filings of the proposed corporate entities. From a public perspective, these newly formed or converted corporations will attract additional investment from those investors and

entrepreneurs who seek to pursue and support public benefit goals, thus injecting additional investment funds into the economy of the state, with all the flow through revenue enhancements that tend to follow such private investment funding.

BACKGROUND OF LEGISLATIVE PROPOSAL

The primary purpose of both a Social Purpose Corporation and a Benefit Corporation is to allow directors and officers to cause the corporation to pursue, in a significant manner, public benefit goals in addition to, or even as a priority over, the generally accepted corporate goal of profit maximization. The principal targets for these new entity forms are so-called “green corporations” that wish to pursue socially beneficial goals while at the same time still having profit-making capacities and pursuing profit-making goals. The profit-making goals distinguish such corporations from charities and from not-for-profit corporations.

Creating the opportunity for such a new form of entity is appropriate and necessary despite (i) the existence of the so-called “stakeholder provisions” in s. 607.0830 of the Florida Business Corporation Act, (ii) the power of corporations to make donations for the public welfare and for charitable, scientific, or educational purposes (s. 607.0302(12)), and (iii) the protections accorded to directors by the business judgment rule. Although these factors exist under current corporate law, there is a strong and reasonably perceived concern among entrepreneurs and other corporate professionals that traditional corporate law poses substantial liability risks for directors and officers who cause the corporation to pursue societal goals at an alleged undue expense to the corporation’s bottom line.

The rationale for this alternative form of corporate enterprise has been described by two

leading experts as follows:¹

“The sustainable business movement, impact investing and social enterprise sectors are developing rapidly but are constrained by an outdated legal framework that is not equipped to accommodate for-profit entities whose social benefit purpose is central to their existence. The Benefit Corporation is the most comprehensive yet flexible legal entity devised to address the needs of entrepreneurs and investors and, ultimately, the general public. Benefit Corporations offer clear market differentiation, broad legal protection to directors and officers, expanded shareholder rights, and greater access to capital than current alternative approaches.”

As stated by another commentator:²

“Social enterprises are entities dedicated to a blended mission of earning profits for owners and promoting social good. They are neither typical businesses, concentrated on the bottom line of profit, nor traditional charities....Their founders instead see value in blending both goals....Yet, these social entrepreneurs worry traditional organizational forms designed for either businesses or charities will constrain their ability to achieve the gains they see in blended mission enterprises.”

Advocates of the benefit corporation recognize that there is a risk of “green-washing,” i.e.

¹ William H. Clark, Jr. & Larry Vranka, *White Paper: The Need and Rationale for the Benefit Corporation* (January 26, 2012).

² Dana Brakman Reiser, *The Next Big Thing: Flexible-Purpose Corporations*, Brooklyn Law School Legal Studies Research Papers (Oct. 2012), available at <http://ssrn.com/abstract=2166474>.

that corporations will use the Social Purpose or Benefit Corporation mantle to wrap themselves in a cloak of social goodness while failing to pursue meaningfully any beneficial societal goals. “Green-washing” is a potential risk because directors of such corporations are only mandated to consider benefit goals, not implement them, nor is there any personal monetary liability imposed upon directors or officers who fail to pursue or achieve such goals. Ultimately it would be up to the corporation’s shareholders to determine whether a change in management or direction is necessary. Thus, it is recognized that there are technical risks of “green-washing” as well as misleading investors whose expectations are not met. However, mitigating the possibility of green-washing are such factors as (i) the disclosure requirements and remedies under state and federal securities and false advertising regulations, (ii) the capacity of shareholders to remove directors and elect new directors, (iii) the negative publicity that would ensue to corporations that mislead the public and (iv) the annual reporting and enforcement proceedings provided for in the Social Purpose and Benefit Corporation statutory provisions. On the whole, we believe that the risk of green-washing, while apparent, is far outweighed by providing to legitimate, good faith entrepreneurs and investors a more effective and less risky opportunity to pursue in a substantial manner public benefit goals within the framework of profit-making corporations.

PRINCIPAL ELEMENTS OF THE SOCIAL PURPOSE AND BENEFIT CORPORATIONS

The principal statutory elements of a Social Purpose Corporation and a Benefit Corporation are substantially identical. The primary differences are principally related to the distinction regarding the breadth of the corporation’s statutory benefit purpose. Those principal elements are:

1. The corporation is formed (or converts to such by amending its existing Articles

of Incorporation or merges into one of those new types of enterprises) under the Florida Business Corporation Act (ss. 607.503-504 and 607.603-604).

2. Except for statutory provisions specifically applicable to Social Purpose or Benefit Corporations, all otherwise non-conflicting provisions of the Florida Business Corporation Act apply (ss. 607.501(3) and 607.601(3)).
3. The corporation's Articles of Incorporation must state that it is a Social Purpose Corporation or a Benefit Corporation, as the case may be (ss. 607.503 and 607.603).
4. The Social Purpose Corporation has the statutory purpose of creating "public benefit," defined as "a positive effect, or the minimization of negative effects, taken as a whole, on the environment or on one or more categories of persons or entities...of an artistic, charitable, economic, educational, cultural, literary, religious, social, ecological or scientific nature, from the business and operations of a social purpose corporation...." (s. 607.502(6))

The Benefit Corporation has the statutory purpose of creating a "general public benefit," defined as "a material, positive effect on society and the environment, taken as a whole, as assessed using a third- party standard, which is attributable to the business and operations of a benefit corporation." (s. 607.602(5)).

We have underlined the words above regarding the Social Purpose Corporation to highlight the principal difference between the Social Purpose and the Benefit Corporation, as the marked language reflects the fact that a Social Purpose Corporation can choose to have only one or perhaps several limited

benefit purposes, contrary to the broad statutory purpose mandated for the Benefit Corporation.

5. The corporation's Articles of Incorporation may include one or more specific public benefit purposes in addition to the applicable statutory public benefit purpose (ss. 607.506(2) and 607.606(2)). For a Benefit Corporation, however, adoption in the Articles of a specific public benefit will not relieve the directors and officers of the mandate to consider broad societal and environmental factors in making any corporate decision (607.606(2))
6. Directors and officers of a Social Purpose Corporation are mandated to consider the effects of any corporate action or inaction upon the shareholders and upon the corporation's ability to accomplish a public benefit purpose, generally focused on its specific public benefit purpose (s. 607.507(1)). Directors and officers of a Benefit Corporation are similarly mandated but, in addition, must consider the effects of any corporate action or inaction upon, *inter alia*, employees, customers, suppliers, the local and global environment, and other community and societal factors (s. 607.607(1)).
7. Directors are not personally liable for monetary damages to the corporation, shareholders or any potential beneficiaries of general or specific benefit goals for failure to pursue or create a public benefit (unless otherwise expressly provided in the articles of incorporation) (ss. 607.507(2) and 607.607(2)).
8. Directors and officers are subject to duty of care and fiduciary principles applicable in all corporations under the Florida Business Corporation Act (ss. 607.507(2), 607.607(2) and 607.0830).

9. An “Annual Benefit Report” must be prepared and distributed to shareholders each year assessing the extent to which the corporation pursued and achieved benefit goals. (ss. 607.512 and 607.612). The report by a Benefit Corporation must contain an assessment of the overall societal and environmental performance of the corporation using an identified “third-party standard.” (s. 607.612). A “third-party standard” is defined as “a recognized standard for defining, reporting and assessing the societal and environmental performance of a business.” (s. 607.602(10)). There are currently several independent companies and agencies that have developed evaluative standards and we expect that others may be developed as the number of benefit corporations grow. A Social Purpose Corporation must also prepare and distribute an Annual Benefit Report but the report need not be assessed using a third- party standard unless the Articles of Incorporation or the board of directors of the Social Purpose Corporation so requires or determines.
10. A “benefit enforcement proceeding” may be brought against a director or officer directly by the corporation or derivatively by a shareholder or other authorized person for failure to pursue or create a public benefit, although no personal monetary liability can be assessed (ss. 607.511 and 607.611).

In brief, the fundamental elements of both the Social Purpose Corporation and Benefit Corporation are:

- (1) statutorily defined benefit purposes;
- (2) potential adoption of additional “specific public benefit” purpose(s) in the Articles of Incorporation;

- (3) mandate to directors and officers to consider the effect of any corporate action or inaction upon the corporation's ability to accomplish its statutory and any specific public benefit purposes;
- (4) liability protections accorded to directors and officers; and
- (5) accountability standards and transparency through annual reports, benefit enforcement proceedings and, for Benefit Corporations, assessment of societal and environmental performance against a third party standard.

These fundamental elements are consistent with the benefit corporation legislation adopted in other states.

SOCIAL PURPOSE CORPORATION AND BENEFIT CORPORATION AS ALTERNATIVE FORMS OF ENTERPRISE

The proposed legislation provides entrepreneurs and investors with a choice to form (or convert or merge into) either a Social Purpose Corporation or a Benefit Corporation.

Entrepreneurs and investors who want a “fully green” corporation will likely choose the Benefit Corporation model. Those that prefer a corporation that has a narrower, specific public benefit focus will likely select the Social Purpose Corporation model. There appears to be interest for both types of enterprises and therefore it is appropriate to allow entrepreneurs and investors to determine which form best suits their goals.

An example may explain the difference between the Social Purpose Corporation and the Benefit Corporation. Suppose that a Florida for-profit pharmaceutical corporation plans to manufacture an anti-malarial drug and distribute that drug at low or no cost in African countries. If that is the corporation's sole benefit purpose, the corporation could appropriately be formed as, or convert or merge into, a Social Purpose Corporation. However, if the corporation is also

dedicated to creating favorable employee programs, running its operations pursuant to strict environmental and ecological policies, and undertaking activities to benefit the local community, in other words to pursue policies that have broad public and social welfare consequences, the corporation may prefer to qualify and be formed as, or convert or merge into, a Benefit Corporation.

The difference between the goals of the two corporations is basically one of degree. The Social Purpose Corporation has the statutory purpose to pursue or create one or more fairly specific public benefits (although there is no limitation on the number or breadth of the goals that a Social Purpose Corporation may choose to pursue). The Benefit Corporation has a much broader defined statutory purpose encompassing societal and environmental factors. A Benefit Corporation could also adopt in its Articles of Incorporation one or more “specific public benefits” which has one or more focused purposes, but pursuit of those specifically-identified focused purposes would not relieve directors from the mandate to consider the “general public benefit” with regard to any corporate action or inaction.

STATE ADOPTIONS

To date, Benefit Corporation legislation has been adopted in the following 20 states or jurisdictions: Arizona, Arkansas, California, Colorado, Delaware, District of Columbia, Hawaii, Illinois, Louisiana, Maryland, Massachusetts, Nevada, New Jersey, New York, Oregon, Pennsylvania, Rhode Island, South Carolina, Vermont and Virginia. Social Purpose Corporation legislation (or comparably designated legislation) has been adopted in California and Washington.

California is the only state that has adopted both the Benefit Corporation and the Social Purpose Corporation models (in California the alternative to the Benefit Corporation is called a

Flexible Purpose Corporation). Washington only adopted the Social Purpose Corporation (using the same nomenclature). All other states have adopted solely the Benefit Corporation model. In our judgment, adoption of the proposed legislation that allows entrepreneurs and investors to decide which type of enterprise best fits their goals is preferable and creates greater opportunity and incentive to form an enterprise under Florida law.

Additional states are considering potential legislation. Information regarding benefit corporations and potential state adoptions can be found on the web site

<http://www.bcorporations.net>.

The number of such corporations formed to date in the various states is difficult to ascertain because in many states such corporations are simply listed under standard corporate statistics. It is clear, however, that there is both entrepreneur and investor interest in these alternative forms of corporate entities. One report found that from January-August, 2012, 60 Benefit Corporations and 15 Flexible Purpose Corporations were formed in California.

AMENDMENT TO CHAPTER 607

The proposed legislation includes amendments to s. 607.1302, the appraisal rights provision. The election and termination provisions for the Social Purpose Corporation and the Benefit Corporation each provide for appraisal rights for shareholders objecting to such change in corporate status (ss. 607.504-505 and 607.604-605). This necessitates amendment to Ch. 607.1302 to include such transactions among the transactions for which appraisal rights are accorded.

CONCLUSION

In our judgment there is no downside and only an upside to allowing the creation in Florida of a Social Purpose or a Benefit Corporation. Standard business corporations are in no

way affected by these new forms of enterprise. The proposed legislation will allow entrepreneurs and investors to pursue societal goals within the context of a for-profit corporation. Given the adoption of similar legislation in a growing number of states, this alternative form of enterprise is an “idea whose time has come.” The proposed legislation, we believe, will be a positive addition to the corporate law of Florida and, given the alternatives offered, may put Florida corporate law in the forefront in this expanding movement.

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