

Converting to a Delaware Public Benefit Corporation: Lessons from Experience



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January 27, 2022

The past two years have seen a dramatic shift in practice relating to the Delaware public benefit corporation (the PBC)—a corporate form that requires the board of directors to balance stockholders' monetary interests, the best interests of those materially affected by the corporation's conduct, and a particular public benefit purpose selected by the corporation. The balancing requirement replaces the focus of traditional Delaware corporations, which is ultimately promoting stockholder value.

In 2020, the Delaware legislature made it much simpler for an existing corporation to become a PBC, by, among other things, lowering the required statutory stockholder approval to a simple majority vote. In 2020 into 2021, our firm advised the first two major public companies—Veeva Systems and United Therapeutics—that decided to convert to the PBC form. We have also worked with many private companies as they have converted to the PBC form, navigated life as a PBC, and approached M&A in the PBC context. At the time of this publication, there are 15 public PBCs and thousands of private PBCs in existence. Several PBCs, including Lemonade, Inc., have successfully gone public as a PBC. These developments all dovetail with an increasing focus on Environmental, Social, and Corporate Governance (ESG) issues and the proper role of the corporation in society.

The increased prevalence of PBCs in the marketplace has caused more and more boards of directors of Delaware corporations, both public and private, and some that may have previously questioned the likely success of a conversion, to consider a conversion to the PBC form. The process to convert to a PBC, like any major corporate decision, should be taken seriously and evaluated with the assistance of corporate advisors, including experienced legal counsel. This article provides a broad overview of the development of the PBC form, the mechanics of what it means to be a PBC, the steps to convert from a traditional Delaware corporation to a PBC, and some of the practicalities of operating as a PBC.

I. Brief History of the PBC Form

Under Delaware law and the well-established business judgment rule, the board of a traditional Delaware corporation has broad latitude in how to run the day-to-day affairs of the corporation. At the same time, Delaware law also provides that a board's decisions must ultimately relate to the purpose of advancing stockholder value. In practice, this means that Delaware boards can consider various interests and constituencies, but their decisions must ultimately tie to promoting and protecting stockholder value. This rule narrows in the context of a sale of control, where a board may only consider the best short-term value available to stockholders.

The PBC form alters these rules. The ultimate end of a PBC is not the promotion of stockholder value, but rather advancing and balancing 1) stockholder value, 2) the best interests of those materially affected by the corporation's conduct, which captures a potentially wide universe of stakeholders, such as employees, customers, suppliers, and local communities, and 3) a public benefit purpose selected by the corporation.

Until 2013, Delaware did not have a statute that permitted corporate fiduciaries to directly consider non-stockholder interests as ends in themselves, such as the "constituency" statutes enacted by other states. However, in 2013, the Delaware legislature amended the General Corporation Law (DGCL) to implement an alternative approach to this issue: the PBC. The PBC provisions of the DGCL were enacted to give corporations the flexibility to opt in to a new corporate form that would not only permit but *mandate* that directors balance different stakeholder interests and corporate objectives when acting as a board—while still maintaining many of the governance features of a traditional Delaware corporation.

Part of the recent increase in the popularity of the PBC form owes to the reduction of statutory barriers to becoming a PBC. Under the original version of Delaware's PBC statute, the ability to convert from a traditional corporation to a PBC (and vice versa) was extremely limited as a practical matter. In 2013, a corporation had to obtain approval by 90 percent of its stockholder voting power to become a PBC, and dissenting stockholders would have been entitled to pursue appraisal rights (a court-based determination of fair value) in connection with a conversion. The statute was subsequently amended in 2015 to reduce the stockholder vote requirement to two-thirds and eliminate the associated appraisal rights for some public companies. Finally, in 2020, the statute was amended to eliminate appraisal rights triggered simply by a conversion and to require only a simple majority for stockholder approval (absent greater requirements in a company's governing documents). Today, PBCs largely follow the same technical rules and statutory provisions applicable to traditional corporations—but with important additional obligations imposed by the PBC statute.

II. The Mechanics of a Public Benefit Corporation

A Delaware PBC is governed by a fairly spare set of statutory provisions that can be found in Subchapter XV of the DGCL. In all other respects, the PBC is governed by the remainder of the corporate statute applicable to traditional corporations. The special statutory rules that apply to a PBC distill down to a few essential categories, described below.

A. The Balancing Requirement and the Certificate of Incorporation

The core requirement for establishing a PBC under Delaware law is that the corporation provide in its certificate of incorporation that it is a PBC and set forth the specified public benefit purpose of the corporation. The statute offers a great deal of flexibility regarding what qualifies as a "public benefit":

a positive effect (or reduction of negative effects) on 1 or more categories of persons, entities, communities or interests (other than stockholders in their capacities as stockholders) including, but not limited to, effects of an artistic, charitable, cultural, economic, educational, environmental, literary, medical, religious, scientific or technological nature.

The statute provides that the public benefit purpose, balanced with stockholder pecuniary interests and the interests of those materially affected by the company's conduct, will guide various corporate decisions. The statute also provides more generally that a Delaware PBC should be operated so as to produce public benefits and operate in a "responsible and sustainable manner."

From a ministerial standpoint, the statute requires that the heading of the certificate of incorporation clearly state that the corporation is a PBC. The statute no longer requires that a corporation change its name to reflect its PBC status—and in our experience most PBCs choose not to change their name.

B. PBC Reporting Requirements

The Delaware statute requires that, at least every other year, a PBC provide its stockholders with a statement as to the PBC's promotion of its public benefit purpose and the best interests of those materially affected by the PBC's conduct. The report must include certain required information, such as an assessment of the PBC's success in fulfilling its purposes, objectives, and standards established by the board, and factual information relating to the attainment of those standards and objectives. PBCs have a great deal of flexibility, however, in fashioning their reports, and practice is still evolving. The statute also provides that a PBC can choose to provide the report more frequently, make it available to the public, or use a third party to certify or assess the attainment of its goals. Many companies that publish sustainability reports may choose to leverage such reports in designing a PBC report, albeit with an eye to what the DGCL specifically requires.

Aside from the formal report, the statute requires that every notice of a PBC's stockholder meetings contain a statement that the corporation is a PBC. The corporation's stock certificates (or if a corporation's shares are uncertificated and kept in book entry-form, notices provided in lieu of

certificates) must state that the corporation is a PBC. If a PBC is *not* publicly traded and the name of the corporation does *not* contain a reference to its PBC status, then, whenever the PBC newly issues stock, it must provide notice to the resulting stockholder that the company is a PBC; if the PBC is publicly listed, no such additional action is needed.

C. Stockholder Lawsuits

A noteworthy feature of the Delaware PBC is that *only* stockholders can enforce the Delaware law-based obligations of a PBC's board, including the core balancing requirement of a PBC. The statute expressly provides that other stakeholders cannot bring such actions. In addition, the statute specifies that in a lawsuit to enforce the balancing requirement, the stockholder plaintiffs must individually or collectively own at least two percent of the PBC's shares, or in the case of a publicly listed PBC, the lesser of that percentage or a market value of \$2,000,000. Aside from these rules, the statute also contains various protections for directors, providing, among other things, that a director generally will not be deemed to have a conflict of interest merely because he or she owns stock and, in effect, that the business judgment rule applies in the PBC context.

III. How to Convert to a PBC

To convert to the PBC form, a company will want to keep in mind several steps and considerations. Of course, a newly formed corporation can become a PBC from the start, and various aspects of the discussion in this article will be pertinent for such a corporation as well.

A. Legal Paths for Becoming a PBC

To become a Delaware PBC, a company must be identified as such in its certificate of incorporation and set forth a public benefit purpose in its certificate. For an existing Delaware corporation, the simplest (and in our experience, the most common) technical path to becoming a PBC is likely to amend its certificate of incorporation, depending on the company's vote requirements in its governing documents and other related structural considerations. A corporation could also become a PBC by merging with an existing PBC, and an entity formed outside of Delaware could additionally consider domesticating as or converting to a Delaware PBC. This article generally envisions amending the certificate of incorporation to become a PBC.

B. Board Approval and Decision-Making

The decision to become a PBC generally begins with the board of directors. The board should approach the decision seriously, taking into account the pros and cons of converting to the PBC form, soliciting views from management, and using advisors as appropriate. The board's decision is governed by its *current* fiduciary duties. Accordingly, for a traditional corporation formed under Delaware law, the board will need to discharge its duties of care and loyalty in making the conversion decision. Fundamentally, the board must determine that the conversion is in the best interests of its stockholders—that is, that the conversion promotes stockholder value.

To this end, the board of directors should evaluate how the PBC structure will relate to and advance the company's business and maximize stockholder value in the long run. In our experience, companies that have converted to the PBC form view the conversion as aligning the company's legal form with how the business is already run and what makes the business successful. In most cases, we would expect the decision to become a PBC to be protected by the business judgment rule, as long as the board carefully considers the conversion.

C. Crafting the Public Benefit Purpose

Once the decision has been made to pursue a PBC conversion, the board of directors, with the assistance of management and outside advisors, should craft an appropriate public benefit purpose to include in the company's certificate of incorporation. The language of the statute provides a great deal of flexibility in designing a suitable public benefit purpose, although that designing is a balancing act. The corporation's public benefit purpose will guide future decision-making at the company. Accordingly, the public benefit purpose should be specific enough to guide such decision-making, but not so narrow as to unnecessarily constrain the corporation's future conduct or quickly become unable to accommodate an evolving business. Because the public benefit purpose is contained in the corporation's certificate of incorporation, making changes after it has already been implemented will require a charter amendment and new board and stockholder approvals. Experienced legal counsel can assist in the preparation of an appropriate statement of public benefit purpose.

D. Stockholder Approval

Once the board approves the conversion to the PBC form and before the conversion can become effective, the corporation's stockholders will need to approve the conversion (i.e., in many cases, the charter amendment). Private corporations can often choose to obtain this stockholder approval by providing appropriate disclosures to stockholders and soliciting stockholder approval by written consent in lieu of a meeting. Public companies will, in most cases, need to obtain stockholder approval at a stockholder meeting, which requires filing a preliminary proxy statement with the U.S. Securities and Exchange Commission (SEC), which is subject to review and comment, and filing and mailing a definitive proxy statement to stockholders.

For both private and public companies, boards and management considering a conversion to the PBC form will of course want to think ahead to investor support and whether sufficient support will exist, now and in the future.

For private companies, in our experience, many investors are willing to consider supporting the PBC form and will want to hear why a conversion is advantageous to stockholders and the business. Assessing such support is critical both for the company's ongoing financing needs and for purposes of obtaining approval of the conversion. Private companies will also need to navigate their web of governing documents to determine which approvals will be needed. Where stockholders act by written consent, appropriate notices will need to be provided after the fact to stockholders who do not provide consent.

For public companies, our experience is, again, that many investors are willing to consider supporting the PBC form. Both Veeva and United Therapeutics received overwhelming support from their stockholders. Investors will want to understand why a conversion is in the best interests of investors and fits in with the "story" of the business. Investors will likely also consider other aspects of the company's governance structure and the existing rights and protections of the public stockholders. In this regard, public companies should consider whether to engage a public relations firm to build investor support.

Public companies will also want to think ahead to several related factors. One is the reaction of proxy advisory firms. Such firms have shown willingness to support conversions, but will consider them on a case-by-case basis, in light of the company's business and existing governance practices and structures.

Another consideration relates to anticipating potential reactions from the SEC on disclosures to stockholders. Here again, Veeva and United Therapeutics are helpful examples, as the proxy statements filed by both withstood SEC review and comment.

The required stockholder vote to add the public benefit purpose to the certificate of incorporation is the same as would apply to any other charter amendment under a company's governing documents. Once the amendment has been approved, the corporation need only file the amendment with the Office of the Secretary of State of the State of Delaware, and the conversion to a PBC is complete.

E. Other Preparations

Beyond the very important approval process, a company considering a conversion to a PBC will want to plan ahead on other fronts.

A company converting to the PBC form will want to think about outreach to employees, customers, suppliers, and local communities to inform them of the conversion—including where, for example, those constituencies are important stakeholders whose interests helped animate a decision to convert.

A company considering a conversion should also work with legal counsel to consider whether other appropriate changes should be made to the company's governing documents—for example, to other provisions of its charter, its bylaws, its form indemnification agreement for directors and officers, and any corporate governance guidelines or committee charters that are in place.

A company will, of course, also want to think ahead to what life would look like for the company as a PBC. One important consideration for any PBC is how to approach the required biennial report to stockholders on the company's attainment of its PBC goals—for example, the presentation of the report, the stakeholder interests that will be reported on, who at the company will be responsible for producing the report, and what data will be used in the report. Another is how the board will organize and document its deliberations to ensure that it is thinking about the appropriate balancing requirements and how that can best be demonstrated in (among other things) meeting minutes, resolutions, and actions by written consent.

A related consideration is whether the board will use a third party, such as B Lab, to assess or certify the company's compliance with its PBC goals. Becoming a PBC and becoming B Lab-certified (or seeking certification from another third party) are two different, independent decisions.

Finally, the company will want to keep in mind housekeeping requirements with regard to stock certificates and notices to stockholders, as discussed above.

IV. Practicalities of Operating a PBC

A. Legal Guidance Concerning PBCs

Although several examples of successful conversions now exist and the statutory provisions on PBCs are fairly clear, the Delaware courts have not yet had the opportunity to analyze the unique nature of PBCs. In contrast to the traditional corporate context—where thousands of cases exist and help guide corporate behavior—there is no case law addressing PBCs specifically. This is an important item to consider when contemplating a conversion.

That said, despite the lack of direct guidance from the judiciary, we believe certain existing governance principles should apply in the PBC context. Initially, the business judgment rule—the Delaware principle that judges will not scrutinize or disturb most of the informed business decisions of disinterested directors—should apply to many decisions of a PBC board, as it would in the context of a traditional Delaware corporation. The PBC statute codifies this principle by providing that an informed decision by PBC directors will be deemed to have satisfied the statutory tripartite balancing obligation as long as the directors are disinterested and act in an informed manner and their decision is "not such that no person of ordinary, sound judgement would approve." The fiduciary duties of care and loyalty applicable to directors of a traditional Delaware corporation should likewise apply to the directors of a PBC. However, the application of these principles in specific cases differ for PBCs given the different considerations and requirements confronting corporate fiduciaries of a PBC.

B. PBCs in the M&A Context

As practitioners and investors have noted, despite many of the anticipated similarities in litigation involving PBCs and traditional corporations in many contexts, the expectations for board members in M&A situations will likely differ for PBCs. When the board of a traditional corporation decides to sell control of the company, the focus of the board's fiduciary duties shifts to obtaining the best monetary value for stockholders in the short term; other constituencies cannot be considered (the imposition of this narrow obligation is often referred to as the "*Revlon*" doctrine). Courts will evaluate a traditional Delaware corporation's board under an enhanced standard of review in this context.

In the PBC context, however, the applicable standard of review will be different in many respects. Instead of focusing solely on short-term stockholder gain, the board of a PBC would still engage in the tripartite balancing required by the statute—such that aspects of the "*Revlon*" doctrine would not apply to PBCs.

V. Conclusion

For a company that is interested in becoming a PBC, enough examples now exist to provide insight into when a conversion may make sense and the process that likely lies ahead. From those examples, we know that a successful conversion can be achievable, even for an already public company, depending on a company's business, its governance profile, and its investor base. Board members and management will want to consider, however, what is most sensible for the business: remaining a traditional corporation, with the latitude the business judgment rule typically affords in the course of promoting stockholder value, or embedding within the corporate form a public benefit purpose and the consideration of stakeholders as ends in themselves.

For more information on public benefit corporations or any related matter, please contact any member of Wilson Sonsini's Delaware office or [corporate governance](#) practice.