

The Rise of the For-Profit, Socially-Responsible Corporation in Canada

Date: May 29, 2015

Lawyers You Should Know: Dennis Tobin

Corporations want to be viewed as socially responsible enterprises for many reasons: it is good for business; it attracts and helps retain motivated employees; it has the chance of attracting additional investment from impact investors and it links entrepreneurial skills and drive for financial gain with environmental, social and governance impacts.

However, this notion is possibly at odds with two realities. The first is that current corporate law regimes governing for-profit corporations in North America have directors focused almost exclusively on the corporation's short term, financial bottom line. The second is a belief by some that social enterprise is limited to non-profit entities focused primarily on public benefit objects in an environment that is regulated and entitled to tax incentives.

The benefit corporation model may be a solution that enables the for-profit, socially responsible enterprise. It also represents a way to connect social impact investors with qualified, socially responsible corporations. The benefit corporation is a strictly voluntary status and serves as a for-profit model that enables a corporation to pursue profit-generating activities while contemporaneously promoting positive effects on society and the environment. This benefit corporation is also complementary to non-profit and charitable activities, but on a much larger scale.

Delaware's new legislative regime creating a "public benefit corporation" or "PBC" status defines a public benefit corporation as a for-profit entity "intended to produce a public benefit or public benefits and to operate in a responsible and sustainable manner." Directors of a Delaware PBC are required to manage it in a manner that balances the shareholders' financial interests, the best interests of stakeholders materially affected by the corporation's conduct, and a public benefit.^[1]

In an article by Kyle Westaway and Dirk Sampselle, published in the Emory Law Journal, the authors summarize what the benefit corporation model can achieve: "The rise of the benefit corporation simply presents a much needed option for those who wish to incorporate values-based decision making into their business practices and procedures. It also marks a return to

corporate form in which the limitation on investor liability is given in exchange for enterprises that are dedicated to benefitting the society and environment in which the enterprise operates.”^[2] The notion of a private enterprise for public gain is no longer an oxymoron,^[3] as benefit corporations allow for a broader definition of what “shareholder value” includes.^[4]

While the model legislation adopted by many states in the United States points directors to pursue a “general public benefit,” directors of PBCs are also free to pursue a “specific public benefit purpose.”^[5] Flexibility offered to PBC directors as a specific purpose is balanced with pecuniary interests of shareholders and best interests of those materially affected by the corporation’s conduct.

The public benefit corporation model began in 2012 and has been adopted in varying forms in 27 states in the United States and is being considered in many more. So far there are 1,550 known registered public benefit corporations in the USA.^[6] Support has been bipartisan for a number of reasons. In its simplest form the PBC requires amendments to existing corporate legislation on a strictly voluntary basis. It does not seek any tax exemptions or incentives and it avoids the need for new regulatory regimes. It does this by a commitment to its public purpose, transparency, and accountability.

What is Happening in Canada

In 2014, the Government of Canada called for submissions on its review of the *Canada Business Corporations Act* (CBCA), including the role of the socially responsible enterprise and in the Canadian context, the extent to which current CBCA incorporation provisions and structures facilitate the creation of socially responsible enterprises. There were many submissions, including one from the Canadian Bar Association, which included recommendations supporting the benefit corporation model. To that end, the proposed amendments included language to clarify the business judgment rule which governs the standards for corporate directors in making decisions about the best interest of the corporation.^[7]

The key recommendation would incorporate the common law principles set out in the *BCE Inc v 1976 Debenture Holders*^[8] decision of the Supreme Court of Canada that directors, in considering what is in the best interest of the corporation, should be permitted to consider not only the interests of shareholders, but also other stakeholders, including employees, creditors, consumers, governments and the environment in their decision-making. Directors should also be allowed to consider both short and long-term interests of the corporation, including benefits that may accrue to the benefit corporation from its long-term plans, and need not give priority to any particular interest. Changes to the business judgment rule, if any, are unlikely to be considered before the next mandatory review of the CBCA in 2016.

In 2013, the Ministry of Consumer Services in Ontario announced a social enterprise strategy entitled “*Impact - A Social Enterprise Strategy for Ontario*.”^[9] The Government stated in that report that, among other things, it wants to “support and attract both entrepreneurs and investors to do business in Ontario while contributing to the social good.” It is focused on social entrepreneurs, impact investors and accomplishing gains in the social sphere.

The “*Dual Purpose Corporate Structure Legislation: Stakeholder Engagement Report*” was released in 2014 as part of the impact mandate from the ministry to “explore introducing legislation to enable the creation of new ‘hybrid’ corporations.”^[10] While the panel was unable to reach consensus on whether dual purpose corporate structure legislation should be introduced, it did develop recommendations on what it should look like if it were introduced. The report documents areas where the panel achieved consensus and where it has not been possible to reach agreement. The report makes a total of 15 recommendations.

One of the recommendations of the Stakeholder Report was that public input be obtained. Submissions on the Stakeholder Engagement Report were due in May 2015. The authors of this article submitted a recommendation supporting the enactment of amendments to the *Ontario Business Corporations Act* to permit the benefit corporation model in Ontario.^[11]

British Columbia passed legislation effective July 2013 to permit the creation of Community Contribution Corporations (CCCs)^[12] and Nova Scotia has proposed legislation (which has not yet been enacted) to permit Community Interest Corporations (CICs).^[13] Both forms of legislation permit entities that are akin to non-profit enterprises with limited ability to engage in business activities and restrictions on providing returns to investors. However, it is unlikely that the federal government or the provincial governments will extend tax exemptions and incentives to a new class of corporation and as a result, non-profits and charities structured as “hybrid” corporations are unlikely to be attractive as a vehicle for attracting private investment and carrying on socially responsible enterprises using for profit means. Fewer than 30 CCCs have been created under the British Columbia legislation.

The benefit corporation model is a model for socially responsible, for-profit corporations. Legislative solutions that require new legislation, complimentary amendments to tax laws and new regulatory regimes that limit returns to investors are unlikely to be achieved in the foreseeable future and represent a solution at a different point in the spectrum of corporate enterprises. Instead, amendments to incorporate principles of taking into account broader stakeholder interests are possible in the short term and would enable for-profit corporations to embrace the benefits and responsibilities of being corporations committed to a public benefit as well as making a profit.

The Need to Clarify Basic Terms

All of the foregoing can be very complicated. One of the main complications is the understanding of and use of terms. Recommendations made under one understanding of a term will not result in the same recommendations applied to a different definition.

“Public Benefit Corporations”

For instance, public benefit corporations are defined in the legislative amendments enabling for-profit corporations to become public benefit corporations, such as the Delaware language referred to above. Delaware PBCs are for-profit entities, not subject to the types of restraints that non-profits and charities face, whose directors and officers are provided with enhanced freedom to pursue goals outside of profit-maximization, while sparing the fear of potential

liability for doing so. Benefit corporations have the same freedom as other for-profit corporations with the addition of having a societal mission. Such flexibility provides the corporation the ability to succeed in both its financial and non-financial goals. This means there are no constraints such as asset locks or dividend restrictions.

On the other hand, Ontario's *Not-for-Profit Corporations Act, 2010*, (ONCA) introduces the term "public benefit corporation" (PBC), and outlines special requirements for PBCs as not-for-profit entities compared to non-public benefit corporations. ONCA is yet to be implemented but it will replace the *Ontario Corporations Act* which currently governs non-profit organizations.

"Social Enterprise"

There seems to be an assumption that the definition of "social enterprise" and "socially responsible enterprise" is limited to the non-profit/charity end of the spectrum with the unfortunate connotation that for-profit corporations cannot "by definition" be "socially responsible".

The Impact Strategy defined "social enterprise" as "an organization that uses business strategies to maximize its social or environmental impact." The Stakeholder Report clarifies the definition to mean: "A corporate entity that exists primarily to promote public benefit using business strategies, building social and financial capital and offering innovative ways of operating for social and/or environmental purposes."

The terms "socially responsible" and "socially responsible enterprises" denote enterprises that strive to have positive impacts on society, the environment and communities. Consider removing the requirement that they are "primarily" focused on the stated goals. In this way, the definition would enable a larger number of enterprises across the corporate spectrum and provide access to a vastly larger pool of private capital

"Social Entrepreneurs"

Our experience with the relatively new concept of a for-profit public benefit corporation in Canada is a very paternalistic reaction with a quick focus on regulation. However, we question how to set loose the free market methods and entrepreneurial energies in such an environment.

Social entrepreneurs are referred to in the Ontario Impact Strategy. It quotes Jeff Skoll, a Canadian and the first president of eBay, who said "Social Entrepreneurs are disruptive innovators." Mr. Skoll went on to say "[f]irst of all, social entrepreneurs are entrepreneurs. Like business pioneers, social entrepreneurs are utterly determined to drive change with their innovative ideas. Both aim, in effect, to disrupt a status quo they see as sub-optimal If the goal is to drive change and be disruptive in an industry, confining the definition of 'social enterprise' strictly to the non-profit and charity sphere is a misnomer. Many for-profit companies have acted in a way to change the face of the industries in which they operate."^[14]

"Hybrid Corporations"

Benefit corporations were originally referred to as “hybrid” corporations. The word “hybrid” is used to suggest something that is a combination of two distinct breeds. Benefit corporations are not “hybrid” corporations but a single breed of corporate entity where new capabilities are enabled – a for-profit corporation with a social benefit purpose.

“Impact Investor”

The Ontario Impact Strategy defines an impact investor as “an investor who is interested in achieving a social return on investment, as well as a financial one.” The Stakeholder Report recommends “any proposed legislation should enable dual purpose corporations to attract share capital from investors seeking both a financial and a social return. It should also enable founders, employees and other stakeholders to have equity in the organization.”

Impact investors currently include private investors, foundations, ESG (environmental, social and governance) funds and ethical funds. With the advent of benefit corporations, corporations become impact investors through their everyday activities.

B Corporations

“B Corporation” is a certification, much like LEED for buildings, or Fair Trade for coffee, but it is not actually a type of social enterprise form. B Lab, a United States based non-profit, began using the assessment system to accredit socially conscious businesses as “B Corps”. The designation gained significant traction and has become a highly recognizable symbol that a company has met rigorous standards of social and environmental performance, transparency and accountability. Traditional corporations can receive the designation, and alternatively, a benefit corporation may not have undergone the certification process to be labelled a “B Corp”.^[15]

Why the For-Profit Benefit Corporation Model Will Work in Canada

While social enterprise legislation can be implemented at any point along the spectrum of corporate entities, it may be most useful for achieving goals of social good if implemented at the end of the spectrum where for-profit corporations live. The goal should be to enable for-profit enterprises to take action having regard to profit, people and the planet as a complement to the activities of governments and charities. A solution at one point in the spectrum does not necessarily exclude a solution at any other point in the spectrum or diminish the contribution of an enterprise at any other point. CCC and CIC type legislation could be effective in the non-profit/charity context; however, legislation enabling benefit corporations at the for-profit end is a solution that is likely to be adopted quickly and have a lasting impact.

As of December 2012, there were 1,107,540 employer businesses in Canada. Small businesses made up 98.2 percent of employer businesses, medium-sized businesses made up 1.6 percent of employer businesses and large businesses made up 0.1 percent of employer businesses. Roughly 35 per cent (389,116) of these employer businesses were in Ontario.^[16] Benefit corporation status is best suited to private, closely held enterprises, just like the majority of employers in Canada.

On a regional basis, the jurisdiction that adopts the most attractive and effective legislation will attract the greatest number of corporations who are looking to solve a corporate governance problem, who want to pursue a profit, people and planet bottom line and who want to create an organization based upon meaningful purpose.

The Government of Ontario should consider adopting the benefit corporation model. Benefit corporations marry the idea of capitalism in the free market with the idea that our society should operate in such a way as to provide the greatest good for the most people.

Benefit corporation legislation could be successful in attracting investors to do business in Ontario while contributing to the social good. A major hurdle of attracting investor money is the requirement to provide investors with a return on their investment. Benefit corporations would be owned by shareholders who would invest with a view to receiving a financial benefit through the declaration of dividends, the appreciation of their initial investment, or both. The introduction of benefit corporation legislation in Ontario could build on the strength of Ontario's dynamic and innovative business climate.^[17] The public demand for corporate social responsibility has provided significant impetus for the introduction of social enterprise legislation in the United States.

Corporate legislation is fairly consistent across the country. Amendments to the OBCA and the CBCA could form the model for legislative amendments across the country.

Conclusion

Traditionally, for-profit corporations have one mandate -- to maximize shareholder value. Several jurisdictions in the United States have recognized the market for a new type of for-profit corporation, the benefit corporation, which has a triple bottom line: profit, people, and the planet. The adoption of a modified form of corporation is driven by a broadly-based demand from businesses as well as other constituencies within society.

Shareholders, consumers, companies, governments and investors have become increasingly concerned about facilitating positive impacts on society and protecting the environment. However, as a result of the shareholder wealth mandate ingrained in our corporate tradition (if not our legislation), traditional organizational business forms have evolved to reward short-term thinking and a profits-first attitude.^[18] The benefit corporation provides a solution to these competing interests, is strictly voluntary, and serves as a for-profit model that enables a corporation to pursue profit-generating activities while contemporaneously promoting positive effects on society and the environment.

The authors acknowledge the assistance of Dhanbir Jaswal who is currently articling with Blaney McMurtry and will return this fall to practice in the commercial litigation group.

^[1] Alicia E. Plerhoples, "Delaware Public Benefit Corporations 90 Days Out: Who's Opting In?" Georgetown University Law Center, 14 UC Davis Bus. L. J. 247-280 (2014).

- [2] Kyle Westaway & Dirk Sampsel, “The Benefit Corporation: An Economic Analysis with Recommendations to Courts, Boards, and Legislatures” (2013) 62 Emory LJ 999 at 1006.
- [3] William D. Eggers & Paul Macmillan, *The Solution Revolution: How Business, Government and Social Enterprises are Teaming Up to Solve Society’s Toughest Problems* (USA: Harvard Business Review Press, 2013).
- [4] Nic Frances & Maryrose Cuskelly, *The End of Charity: Time for Social Enterprise* (Crows Nest, NSW: Allen & Unwin, 2008).
- [5] B Lab and Pennsylvania attorney William Clark have been instrumental in promoting a model form of legislation to enable the creation of benefit corporations, which states can adopt and adjust to suit their legislation goals. See William Clark, *Model Benefit Corporation Legislation* (4 October 2013), online: Benefit Corp Information Centre <http://benefitcorp.net/storage/documents/Model_Benefit_Corporation_Legislation.pdf>.
- [6] <http://benefitcorp.net/find-a-benefit-corp/search> (accessed May 22, 2015).
- [7] Submission on *Canadian Business Corporation Act* (May 2014), online: The Canadian Bar Association <<http://www.cba.org/cba/submissions/pdf/14-30-eng.pdf>>.
- [8] [2008] 3 SCR 560.
- [9] *Impact: A Social Enterprise Strategy for Ontario* (2013), online: Government of Ontario <<http://www.ontario.ca/document/impact-social-enterprise-strategy-ontario>>.
- [10] *Dual Purpose Corporate Structure Legislation: Stakeholder Engagement Report* (May 2014), online: Government of Ontario <<http://www.ontariocanada.com/registry/showAttachment.do?postingId=17642&attachmentId=26891>>.
- [11] Dennis Tobin & Lauren Dalton (1 May 2014), online: Blaney McMurtry <<http://www.blaney.com/sites/default/files/Tobin%20Dalton%20Final%20Submission%20May%204%202015%20Stakeholders%20report.pdf>>.
- [12] *Business Corporations Act*, SBC 2002, c 57.
- [13] *An Act Respecting Community Interest Companies*, SNS 2012, c 38.
- [14] Jeff Skoll & Sally Osberg, “Social Entrepreneurs Dare to Change the World”, (7 October 2013) online: CNN <<http://www.cnn.com/2013/09/07/opinion/skoll-osberg-social-entrepreneurs>>.
- [15] Online: Certified B Corporations <<https://www.bcorporation.net/en-us/certification>>.
- [16] Email from Patricia Côté, Information Officer, Industry Canada/Corporations Canada (9 April 2015).
- [17] “Building Ontario Up Today for a Brighter, Stronger Tomorrow” (14 July 2014), online: Ontario Liberal Party <<http://www.ontarioliberal.ca/NewsBlog/NewsDetails.aspx?id=Building+Ontario+Up+Today+For+A+Brighter%2c+Stronger+Tomorrow>>.
- [18] Carl Frankel & Allen Bromberger, *The Art of Social Enterprise: Business as if People Mattered*, (Gabriola Island: New Society Publishers, 2013).