Impact investing in the boardroom

Doug Raymond is a partner in the law firm Drinker Biddle & Reath LLP (www.drinkerbiddle.com).

For boards considering a broader focus on social responsibility, the benefit corporation model may be attractive.

BY DOUG RAYMOND

The United States is experiencing the beginnings of what is expected to be a $30 trillion transfer of wealth from the Baby Boomers to their Generation X and Millennial children. As the younger generations assume control of their inheritances, companies will learn how their investment styles and objectives differ from those of their parents. While investment advisors and others try to predict the implications of this for their business models, one trend is becoming more clear: these younger investors will be much more focused on the broader societal impacts of the companies in which they invest. Indeed, many will make it a priority to more closely align their investments with their personal concerns about issues such as the environment, fair trade, social justice, sustainability and other broader societal issues.

This has significant implications for enterprises seeking to attract such investors, as they must focus not only on economic returns but also on specific social, humanitarian or environmental outcomes. According to one recent study, investments characterized as socially responsible almost doubled between 2012 and 2014, to about $6.5 trillion. This market for socially and environmentally responsible investments is expected to continue to grow rapidly.

For boards considering a broader focus on social responsibility, the benefit corporation model is a fairly recent development that may be attractive. The benefit corporation structure provides a legal framework to establish a for-profit (but still) socially responsible business that can attract impact investors as well as other sources of capital.

Benefit corporations generally are the same as traditional business corporations, but unlike a typical corporation: (1) they must have a corporate purpose that includes creating a material, positive impact on society and the environment; (2) the fiduciary duties of directors are expanded to require consideration of nonfinancial and stakeholder interests beyond the economic interests of shareholders; and (3) they must periodically report on their overall social and environmental performance as assessed against a credible, independent, and transparent third-party standard.

The laws authorizing a benefit corporation provide its board with tools, including an expanded business judgment rule and special liability protections that allow the boards of these corporations to make commitments to stakeholders that are equivalent to their commitments to shareholders.

These laws also provide boards of benefit corporations with significantly more flexibility when evaluating potential sale and liquidity options, and provide the ability for businesses to operate with a mission-driven focus even following a sale or initial public offering.

Although some are concerned that this increased flexibility equates to the elimination of objective standards that may make judicial review of questionable board decisions practically impossible, benefit corporations are able to demonstrate to customers and investors a long-term commitment to a broader social agenda (such as ensuring worker safety in factories or minimizing environmental impacts of operations) notwithstanding the absence of profitability.

The transparency of the required reporting means that investors and other stakeholders can evaluate a company's social and environmental performance in a manner similar to how investors use financial statements to understand and evaluate the financial performance of a company.

Though still developing, benefit corporations are becoming a recognized vehicle for businesses that are looking to encompass a broader approach, and for the customers and investors who are looking for companies that are committed to a broader societal focus than profit maximization. Benefit corporation legislation has now been adopted by 31 jurisdictions in the United States, including Delaware. More than 3,600 companies have opted into the new status under benefit corporation laws, including more than 500 corporations in Delaware.

For example, Campbell's Soup Co., in addition to its own corporate responsibility initiatives, became one of the first public companies to own a benefit corporation when it acquired the healthy baby food company Plum Organics in 2013. Plum is a self-described mission-driven company that focuses not only on selling healthy food for infants and children but also on sustainability.

As investment capital flows to investors with more demanding investment criteria around social responsibility, the markets are expected to try and meet that demand. Directors should consider the implications on their businesses of the enormous wealth transfer that is occurring and how they will respond to demands not only for profitable investments, but socially responsible ones. ■

The author can be contacted at douglas.raymond@dbr.com. Elizabeth Babson, an associate with Drinker Biddle & Reath, assisted in the preparation of this column.