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Corporation Purpose

Business Roundtable "Statement on the Purpose of a Corporation" Proposes New Paradigm.

On Monday, Business Roundtable released a "Statement on the Purpose of a Corporation." The Purpose Statement represents a bold vision of the 21st Century corporation and highlights the signatories' commitment to all their stakeholders, which they divide into five categories: customers, employees, suppliers, communities and long-term value creation for shareholders.

We believe it is essential, however, that the Purpose Statement not be misinterpreted as inconsistent with fundamental principles of corporate law, and, in particular, the fiduciary duties of directors. Instead, the Purpose Statement should be read as articulating the interconnection of these categories in fulfilling those duties.

Background

The majority of large U.S. corporations are organized under the general corporation law of the State of Delaware. Under Delaware law, directors of these corporations owe their fiduciary duties to the corporation and its stockholders. Unlike a number of other states, Delaware does not have a permissive constituency statute. Such statutes permit directors to consider the interests of other constituencies, such as employees, but even then typically only in a merger and acquisition context. Delaware and a number of other states have adopted "public benefit corporation" statutes, which allow businesses to be organized as public benefit corporations that, by the terms of their charters, allow for the public benefit to be a stated objective of the organization.

Analysis

The statutory, as well as judicial, focus on a board's fiduciary duty to the corporation and its stockholders does not preclude a board from considering the interests of other constituencies as part of the determination of what creates long-term value for the corporation and its stockholders. For example, a decision to raise the minimum wage for employees, or provide other benefits, may initially affect the corporation's short-term profitability, but in the long-term may provide substantial value creation by enhancing the company's reputation as an employer of first choice and thereby attracting and retaining employees. As corporations seek to strike the appropriate balance and implement a decision-making framework, they may wish to consult with institutional investors.

We believe that a Board's decision based on such an evaluation, if made on an informed basis, would be fully protected by the business judgment rule. We also believe, however, that a decision by a board that is not grounded in the best interests of the corporation and its stockholders likely would not be protected by the business judgment rule under the current state of the law. Further, it is unclear how a Court applying Delaware law would think about factors other than shareholder value in evaluating a board's fulfillment of its duties under Delaware cases, such as *Revlon*, involving a sale of control.

A prerequisite to any change in the current state of the law is a carefully considered determination of how a board should balance the interests of various constituencies. This will often involve not just balancing stockholder and non-stockholder constituencies but different non-stockholder constituencies. For example, a decision to decommission a coal-fired electric generating facility could benefit the environment, but increase costs to consumers and reduce employment for the miners supplying the coal.

In summary, Business Roundtable's Purpose Statement has made a valuable contribution to the debate, which has been developing over the last several years, as to the considerations directors can and should evaluate as they exercise due care in reaching corporate decisions. The Purpose Statement's clear message is that directors should consider information about the impact of their decisions on multiple constituencies, because that impact in turn will directly affect the corporation and its stockholders. This need not be read as being inconsistent with the current state of the law. Rather, properly implemented, it is constructive and additive to the corporate governance lexicon.

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