QIC INSIGHT

Public Benefit Corporations – A Move Towards "Stakeholder Capitalism" and Enhanced ESG Performance

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Executive Summary

In Q4 2021, QIC Global Infrastructure endorsed the conversion of Generate, its largest U.S. infrastructure investment company, to a Delaware Public Benefit Corporation ("PBC") – a new class of for-profit corporations that are legally required to balance stakeholder needs and outcomes alongside financial considerations.

Generate's conversion to a PBC is significant for QIC clients and infrastructure investors because it:

- Represents a nascent but accelerating global trend away from "Shareholder Primacy" towards "Stakeholder Capitalism" whereby commercial corporations elevate environmental and social objectives in their corporate purpose.
- Exemplifies a major trend towards legitimized and evidence-based sustainability performance to counter rising risks of green-washing in an increasingly environmentally conscious world.
- Highlights QIC's industry leading efforts toward enhanced Environmental, Social, and Governance ("**ESG**") performance across its portfolio and a pathway to Net Zero Emissions.

In this insight piece, we introduce the relatively new American corporate form of the PBC as a legally binding means to support Stakeholder Capitalism and to achieve corporate missions to further the public good. We also highlight the benefits of the PBC form for other infrastructure companies and infrastructure investors exploring a similar conversion, including by reference to precedent case studies including that of Generate.

Importantly, the PBC form aligns with QIC's approach to ESG management for its infrastructure investments, which entails supporting our investment companies to embrace sustainability efforts that positively impact their employees, customers, and the broader community. We believe this approach will ensure companies are well positioned to deliver superior investment outcomes over the long term.

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Overview of Delaware Public Benefit Corporations

Adopted in Delaware in 2013, a PBC is a relatively new class of for-profit corporations that is "intended to produce a public benefit or public benefits and to operate in a responsible and sustainable manner."[1]

The Delaware corporate code defines a "public benefit" broadly as "a positive effect or reduction of negative effects on one or more categories of persons, entities, communities or interests (other than stockholders in their capacities as stockholders), including effects of an artistic, charitable, cultural, economic, educational, environmental, literary, medical, religious, scientific, or technological nature." [2]

A PBC is a for-profit entity that is *legally required* to balance stakeholder needs and outcomes alongside financial considerations. A PBC is required to identify in its certificate of incorporation (or corporate charter) the public benefit(s) it will promote. Its board of directors are then obligated to manage or direct the business and affairs of the PBC in a manner that balances the pecuniary interests of the stockholders, the best interests of those materially affected by the corporation's conduct, and the specific public benefit(s) identified in the PBC's certificate of incorporation or corporate charter. More specifically, the board of directors of a PBC has an additional fiduciary duty to uphold the public benefit(s) identified in its certificate of incorporation or corporate charter in addition to the traditional fiduciary duty to maximize stockholders' economic interests as under a traditional Delaware corporation.

This dual fiduciary duty is the defining feature of the PBC that formalizes non-financial corporate objectives and elevates them to the level of shareholder value maximization. In this context, while the dual fiduciary duty represents an evolutionary step in corporate governance that is particularly relevant to ESG commitments, caution needs to be exercised in the selection of one or more public benefits that appropriately align with a company's core business model.

From a reporting standpoint, a PBC is obligated to provide its stockholders a report, at least biennially, that includes the objectives the board has established to promote the public benefit(s), the standards the board has adopted to measure the corporation's progress in promoting the public benefit(s), and an assessment of the corporation's success in meeting the objectives and promoting the identified public benefit(s). As with the selection of one or more appropriate public benefits, the set of measures adopted by a company to measure and monitor its performance in relation to the public benefit(s) are of utmost importance.

PBCs are separate and distinct from "Certified B-Corporations" ("B-Corps"). B-Corps are businesses certified by the independent non-profit organization B-Lab that evaluates, for an annual fee, how a company's operations and business model impact its workers, community, environment, and customers. Unlike a PBC conversion, attaining B-Corp status does not change a company's legal status.

1 The Delaware Code Online. (n.d.). Retrieved from https://delcode.delaware.gov/title8/c001/sc15/
2 Delaware Code, Title 8, §362(b).

The following table illustrates the differences between a PBC, a traditional Delaware corporation, a Certified B-Corp, and a non-profit entity in the U.S.

	Delaware PBC	Traditional Delaware Corporation	Certified B-Corp	Non-Profit Entity
Description	• An alternative corporate form and legal entity of a for-profit corporation that is intended to produce a public benefit and to operate in a responsible and sustainable manner	• A company that is legally registered in the state of Delaware but may conduct business in any state	• A company that has a third-party certification conferred by the non-profit B Lab after meeting a specified standard of social and environmental performance	• An entity that must have a charitable purpose, does not earn profits, and is eligible for state and federal tax exemption
Fiduciary Duties/Obligations	• PBC directors and officers must make informed decisions to balance stockholders' economic interests, the interest of those materially affected by the PBC's conduct, and the public benefit identified in the corporate charter • Traditional fiduciary duties of loyalty and care • Customary investor reporting obligations in addition to biennial report to stockholders on the PBC's pursuit of its public benefit	• Board generally must consider maximizing shareholder value as its primary directive • Traditional fiduciary duties of loyalty and care • Customary investor reporting obligations	• Required to consider stakeholders as part of B Lab license agreement	• Required to pursue charitable activities and make grants to further tax-exempt purpose • Generally may not compete against taxable entities in the marketplace
Legal Requirements	• Directors must consider stockholder value, the public benefit, and impact of company's actions on stakeholders	• Directors **must** consider stockholder value and **may** consider public benefits and impact of company's actions on stakeholders	• B-Corp certification does not affect company's legal status • Requires payment of license fee to B Lab; subject to changes in B Lab rules • Companies must undergo a B Impact Assessment and a B "audit" every three years to maintain certification	• No owners/stockholders • Restrictions on impermissible private/non-charitable benefit • No electioneering and insubstantial lobbying
Tax Treatment	• Taxed as a corporation	• Taxed as a corporation	• Taxed as a corporation	• State and federal tax-exempt for mission-related income

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Key Benefits and Considerations for a PBC

The PBC structure brings many benefits to a company, including delivering a clear message to the external community that the company is truly committed to achieving its corporate mission, to do good in a sustainable manner.

Operating as a PBC demonstrates a company's authentic commitment to sustainability and to making a positive social and/or environmental impact. The PBC is an ideal option for companies whose impact is tied to financial returns since the alignment of the stated public benefit with the core business purpose means PBC conversion has little risk of introducing conflict between balancing profit and purpose.

In addition, the PBC structure provides stockholders increased transparency into measurable operational and ESG data not typically shared in financial statements. Finally, in an increasingly ESG-conscious macroeconomic environment, the PBC structure attracts ESG-conscious stakeholders, including investors, customers, business partners, and employees who have embraced stakeholder capitalism versus the single-minded pursuit of profit that underlies the traditional shareholder primacy model.

The key consideration in converting to a PBC relates to it being a relatively new corporate form. In potential cases where conflicts may arise for directors' balancing dual fiduciary duties, there is currently no depth of legal precedents with regards to decision-making in Delaware courts. This risk can be largely mitigated through clear convergence of a company's operations and its adopted public benefit. Additionally, owing to a general lack of investor education on PBCs, there is often confusion of PBCs with B-Corps and non-profit forms.

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Case Study: **Generate**

In November 2021, with the support of its board and shareholders, including QIC, Generate elected to convert to a PBC. Generate builds, owns, operates, and finances sustainable infrastructure that delivers affordable and reliable resource solutions to companies, governments, and communities.

Since its founding in 2014, Generate's vision has been to rebuild the world with sustainable infrastructure, aligning the incentives of its stakeholders for the long term. Converting to a PBC reinforces the company's commitment to this mission and makes the company's charter consistent with its core values.

The PBC structure and Generate's mission embody Generate's vision and beliefs that there need not be a tradeoff between financial results and sustainability. QIC considers that the PBC conversion will be beneficial for Generate's public profile with respect to its customers, development partners, employees, and capital providers. As ESG and sustainability themes are further prioritized both locally and globally, we expect being a PBC will enhance long-term value for Generate.

Generate

- A sustainable distributed **infrastructure platform** based in the U.S.
- **>US$2bn** portfolio of 2,000+ operating projects
- **40+** asset creation partners

Images courtesy of Generate.

DISTRIBUTED & COMMUNITY SOLAR

DISTRIBUTED WASTE TO VALUE

HYDROGEN MOBILITY

CAMPUS ELECTRIC MOBILITY

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PBC Precedents

In recent years, there has been a notable increase in the number of PBCs in the U.S., including at least 10 publicly listed PBCs as of mid-2021[2], many of which attained PBC status within the last two years.

The listed PBCs span a broad range of industries, and the growing popularity of the PBC form reflects the desire of companies to formalize their commitment to social and environmental factors and to differentiate themselves in an ever more ESG-focused world.

Following are brief profiles of select publicly listed PBCs. Importantly, in all of these examples, PBC missions and company business models are fairly aligned, rendering the benefits of PBC status clear to investors and other stakeholders.

In the unlisted universe, there are approximately 3,000 companies registered as PBCs in the U.S., including Method (eco-home care), Plum Organics (organic baby food), Cotopaxi (outdoor gear & apparel), and AltSchool (education start-up).

Select Profiles of Listed PBCs

Veeva Systems

Formed in 2007, Veeva Systems is an American cloud-computing company specializing in pharmaceutical and life sciences industry applications. It was the first public company to convert to a PBC. Veeva's PBC purpose "to help make the industries it serves more productive and create high-quality employment opportunities" aligns with its business model to deliver technology, data, and services to support life sciences companies in their mission to improve and extend life.

Lemonade

Founded in 2015, Lemonade is a U.S.-based insurance company offering renters', homeowners', pet, and term life insurance products to consumers using artificial intelligence technology. Lemonade's PBC public benefit to "harness novel business models, technologies and private-nonprofit partnerships to deliver insurance products where charitable giving is a core feature, for the benefit of communities and their common causes" is consistent with its sustainable business model that includes annually giving a portion of its underwriting profits to a non-profit organization chosen by each customer upon sign up. Notably, Lemonade was 2020's most successful IPO debut. After establishing PBC status in 2016 pre-IPO, it raised $481.5m from major investors such as SoftBank (2017 and 2019; $420m total) and Allianz (2017; Undisc.).

Allbirds

Formed in 2016, Allbirds is a New Zealand-U.S. company that sells footwear and apparel. Its PBC purpose of "environmental conservation" is in line with its business model to produce sustainable, eco-friendly products made of renewable materials such as wool and trees to minimize its carbon footprint throughout its supply chain in an effort to achieve net zero emissions and to address climate change at the heart of its business. In its inaugural 2020 Sustainability Report to shareholders, Allbirds cited that it has been carbon neutral since 2019, inclusive of offsets of Scope 1, 2, and 3 emissions. The company reported on specific metrics related to carbon reduction targets, including a commitment to cut in half by 2025 its carbon footprint as measured by its products' per unit carbon emissions, and then reduce it further to less than 1kg CO_2e/product by 2030.

[2] Marquis, C. (2021, June 14). Public Benefit Corporations Flourish In The Public Markets.
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Linking PBC and ESG Trends

The increase in popularity of PBCs is believed to be inextricably linked to the global rise in ESG consciousness. As governments, corporations and investors become more committed to the sustainability of economic activities, mechanisms are being sought to formalize such commitments and to effectively measure and monitor ESG performance.

These trends have to date manifested as non-binding environmental targets, voluntary sustainability reporting, and long-term environmental objectives. But as public and private sector support for sustainability gathers pace, more formal commitments and reporting mechanisms emerge, including those under the PBC form.

Public Sector Regulatory Support

From a U.S. regulatory perspective, the Biden administration has ushered in a new era of American climate leadership, placing climate change at the center of its focus. The administration has demonstrated strong support for sustainability and ESG, having the U.S. re-join the Paris Climate Agreement. In addition, it has released a sweeping infrastructure package of US$2 trillion to facilitate energy transition and climate change resilience and established a target for the U.S. to achieve a 50% reduction in 2005 levels of domestic GHG emissions by 2030. This backdrop of increasing public sector commitment to environmental sustainability provides fertile ground for the continuing emergence and adoption of the PBC.

In Europe, the European Union ("EU") has vowed to deliver on the "European Green Deal." This proposes transformational change to turn the EU into a climate neutral continent by 2050 by reducing net emissions at least 55% by 2030 compared to 1990 levels.

Echoing similar developments to those in the U.S., the European Commission now plans to release a proposal on Sustainable Corporate Governance legislation, the objective being to better align long-term interests of company management, shareholders, stakeholders, and society rather than allowing businesses to focus exclusively on short-term financial performance.

Corporate Sector and Investor Support

Beyond policy, there has been a more widespread embrace of sustainability among both investors and corporations. Since the COVID-19 pandemic, there has been pronounced growth in sustainable and ESG-related investments, with monthly global flows into ESG funds more than doubling between early 2020 and early 2021.[3]

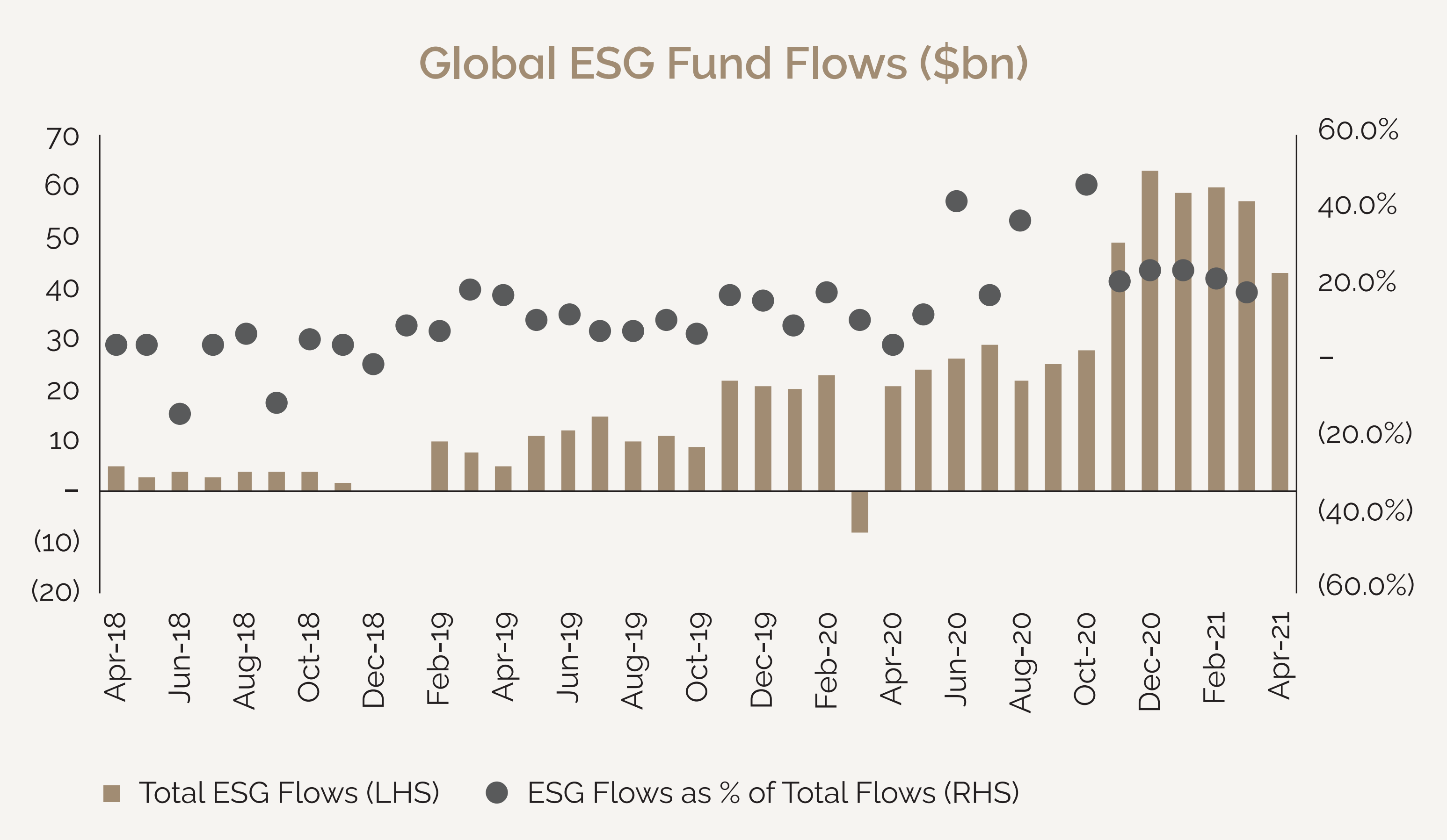

Figure: Illustrating global ESG inflows pre- and post-pandemic.
Source: Morgan Stanley Research

[3] Morgan Stanley Research. (2021, May 18). Reopening to a Regime Change. Retrieved from Morgan Stanley Research

Meanwhile, the theme of "Stakeholder Capitalism" has been more widely supported by investors and corporations. While investors have been increasingly incorporating ESG metrics that go beyond financial performance into portfolio allocation decisions, corporations have more broadly committed to emissions reductions targets such as Net Zero Emissions in alignment with the goals of the Paris Agreement and have adopted ESG-linked management compensation schemes. Currently, approximately 50% of companies in the S&P 500 have management incentives tied in some way to ESG metrics. Both investors and corporations have heightened scrutiny of corporate-level emissions, highlighting a shift in perspectives that elevates the role and importance of ESG in the market[4]. For QIC Global Infrastructure, our focus on sustainability is embedded across the origination and execution of new investments and our active portfolio and asset management approach. This is aligned with our long-held role as active stewards of the assets we manage on behalf of our investors. For example, we recently formalized our net zero emissions commitment for the two pooled funds we manage (the QIC Global Infrastructure Fund and the QIC Infrastructure Portfolio[5]) and continue to drive ESG-linked KPIs and associated management incentives across our portfolios.

Against this backdrop, the PBC form has emerged as a legal framework for sustainability missions to be incorporated into corporate governance.

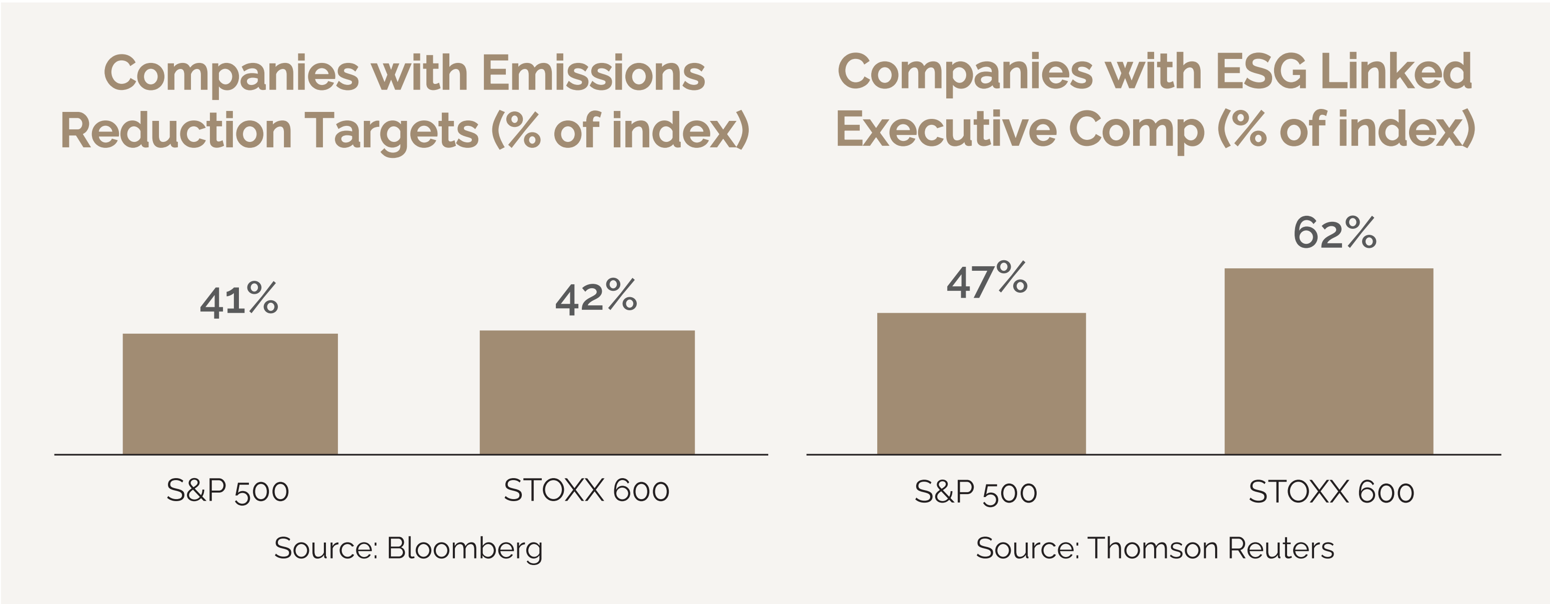

Figure: Support of ESG initiatives by U.S. and European companies.

PBC and the Global Context

Parallel to the Delaware PBC, there has been a rise in recent years in alternative corporate forms outside of the U.S. that similarly require companies to factor social and environmental considerations into their decision making. Several countries — Italy, France, Colombia, Ecuador, Peru, and Rwanda — now have this type of legislation in place, as does Canada's British Columbia province[6].

France has a similar construct to the U.S. Delaware PBC – the *entreprise à mission*. Passed in France in 2019 under the new PACTE Law[7], *entreprise à mission* obligates firms to consider the socio-environmental consequences of business activity[8]. PACTE contains regulatory safeguards to ensure that corporations meet the sustainability goals they lay out: for instance, companies breaching their missions could face liability issues for a breach of fiduciary duties. The European entity of Danone Corporation became a pioneer of the *entreprise à mission* and played a key role in lobbying for the passage of PACTE[9].

Since sustainability will remain potentially one of the most powerful secular themes in the market, PBCs are likely to be increasingly popular with respect to both public and private companies in the years ahead. Given its long duration nature, infrastructure is a logical asset class for PBCs to form and prosper as the world drives to decarbonization and becomes, as a result, more sustainable.

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