Washington State
House of Representatives
Office of Program Research

BILL ANALYSIS

Judiciary Committee

HB 1111

Title: An act relating to the duties of corporate directors.

Brief Description: Determining the best interests of a corporation.

Sponsors: Representatives Morris, Linville and B. Sullivan.

Brief Summary of Bill

- Explicitly allows a director of a corporation to consider more than the interests of shareholders when the director is discharging his or her duty to act in the best interest of the corporation.
- Allows a director to consider the interests of employees, customers, suppliers and creditors as well as the general economy, community and societal interests.

Hearing Date: 1/19/07

Staff: Bill Perry (786-7123).

Background:

The Washington Business Corporation Act (WBCA) requires directors of corporations to discharge their duties "in the best interests of the corporation." The WBCA does not, however, explicitly define the best interests of a corporation. Traditionally, the most commonly accepted view has been that the purpose of a corporation, and therefore the duty of its directors, is to maximize the wealth of the corporation's shareholders. This view is sometimes referred to as "shareholder primacy." Supporters of this view argue that it makes the most overall economic sense and that investors will be reluctant to buy shares in a company that is not primarily concerned with their investments.

Some commentators and interest groups have been critical of this traditional view as being too narrow. In some cases, the criticism has been that maximizing shareholder wealth is too often construed as requiring decisions to maximize short term gain at the expense of the long term health of the corporation. In other cases, the criticism has been that shareholder primacy ignores

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other important issues and provides little incentive for corporations to act in socially responsible ways. For reasons ranging from a desire to protect against hostile takeovers to concerns about employee welfare or environmental preservation, suggestions have been made to broaden explicitly the scope of what is in the best interests of a corporation.   Supporters of the traditional view argue that these non-traditional concerns are and should be addressed by other means such as labor and environmental laws.

The question of how broadly or narrowly the best interests or a corporation should be viewed is sometimes referred to as the "corporate constituency" issue.

Starting with Pennsylvania in 1931, a majority of states have now enacted some form of a corporate constituency statute. These statutes expressly allow, but do not require, a board of directors to consider other factors in addition to shareholders' interests in determining what is in the best interests of the corporation.

Summary of Bill:

The WBCA is amended to allow a director of a corporation to consider several factors beyond shareholders' interests in determining what actions are in the best interests of the corporation. Factors that a director may consider include:

- Interests of employees, customers, suppliers and creditors;
- The state and national economy;
- Community and societal considerations; and
- Long-term and short-term interests, including the continued independence of the corporation.

Appropriation: None.

Fiscal Note: Not requested.

Effective Date: The bill takes effect 90 days after adjournment of session in which bill is passed.