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Analysis of Enrolled Senate Bills 1445-6

Topic: Low-profit Limited Liability Companies
Sponsor: Senators Allen and Barcia
Co-Sponsors: None
Committee: Senate Commerce and Tourism
House Commerce (discharged)

Date Introduced: July 24, 2008

Date Enrolled: December 18, 2008

Date of Analysis: December 17, 2008

Position: The Department of Labor & Economic Growth supports the bill.

Problem/Background: The concept of a low-profit limited liability company, or L3C, was developed by the Mary Elizabeth and Gordon B. Mannweiler Foundation and has been adopted in Vermont. The concept is intended to provide a mechanism for increasing the flow of capital from the private sector to community and economic development and other social enterprises. In theory, adoption of the L3C mechanism will make it easier for socially motivated investors to qualify as a Program-Related Investment (PRI) under the federal tax code, because the relevant tax code provisions are incorporated in the authorizing statute. Although Vermont is the only state that has enacted such a proposal, bills have also been introduced in Georgia, Montana, and North Carolina. Michigan companies seeking to enjoy the advantage of an L3C could choose to incorporate under Vermont law.

Description of Bill: The bills amend the Michigan Limited Liability Company Act to provide for the creation of low-profit limited liability companies, or L3C's. Senate Bill 1445 defines a low-profit limited liability company as an entity that conducts its activities in accordance with the following requirements:

- It significantly furthers accomplishment of one or more charitable or education purposes, as defined in the Internal Revenue Code, and would not have been formed except to accomplish those purposes.

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- The production of income or appreciation of property is not a significant purpose. In the absence of other factors, the fact that significant income or capital is produced is not conclusive evidence of significant purpose.
- The purposes of the entity do not include one or more political or legislative purposes described in Section 170 (c) (2) (d) of the Internal Revenue Code.

Senate Bill 1446 provides that the name of a low-profit limited liability company must contain those words, or the abbreviation L3.C or l3.c., with or without periods or other punctuation. The Attorney General may take action to dissolve an L3C if the entity has ceased to meet any of the requirements prescribed in Senate Bill 1445 and for 60 days failed to file a certificate of amendment.

Summary of Arguments

Pro: The current tax code discourages social innovation. Heather Peeler, a Senior Consultant for Community Wealth Ventures, notes in a recent article that “tax-exempt entities have limited avenues to access capital, and a strong profit orientation may jeopardize their tax status.” She goes on to say that “corporate structures do not satisfactorily recognize the public benefits that are the core of social enterprise”. The L3C concept was designed to address this conundrum and bridge the gap between the profit and non-profit sectors. The bills will increase the amount of capital invested in economic and community development and other social enterprises.

The low-profit limited liability company is likely to be a very popular mechanism. If Michigan law does not allow it, companies will choose to use the laws of Vermont or other states to create their business entity.

Con: Although there may be a need for a different business model in the Limited Liability Company Act to reflect social enterprises, much more detail would be desirable. There is an entire statute devoted to nonprofit corporations. Recent improvements in the nonprofit law that would require, among other things, a minimum of three directors would not apply to LC3s. Why should low-profit limited liability companies not be treated the same as nonprofits? At the very least, there should be a separate chapter of the act devoted to LC3s.

Fiscal/Economic Impact

(a) Department

Budgetary: The bills will have no budgetary impact on the department.

Revenue: The bills may increase slightly the number of limited liability corporations that might otherwise be created elsewhere (e.g. Vermont).

Comments:

(b) State

Budgetary: The bills will have no budgetary impact on the state.

Revenue: The bills will have no direct impact on state revenues.

Comments:

(c) Local Government

Comments:

Other State Departments: The Treasury Department is aware of the bills

Any Other Pertinent Information: The Council of Michigan Foundations testified in support of the bills in the Senate.

Administrative Rules Impact: Neither the bills nor the act contain administrative rulemaking authority.