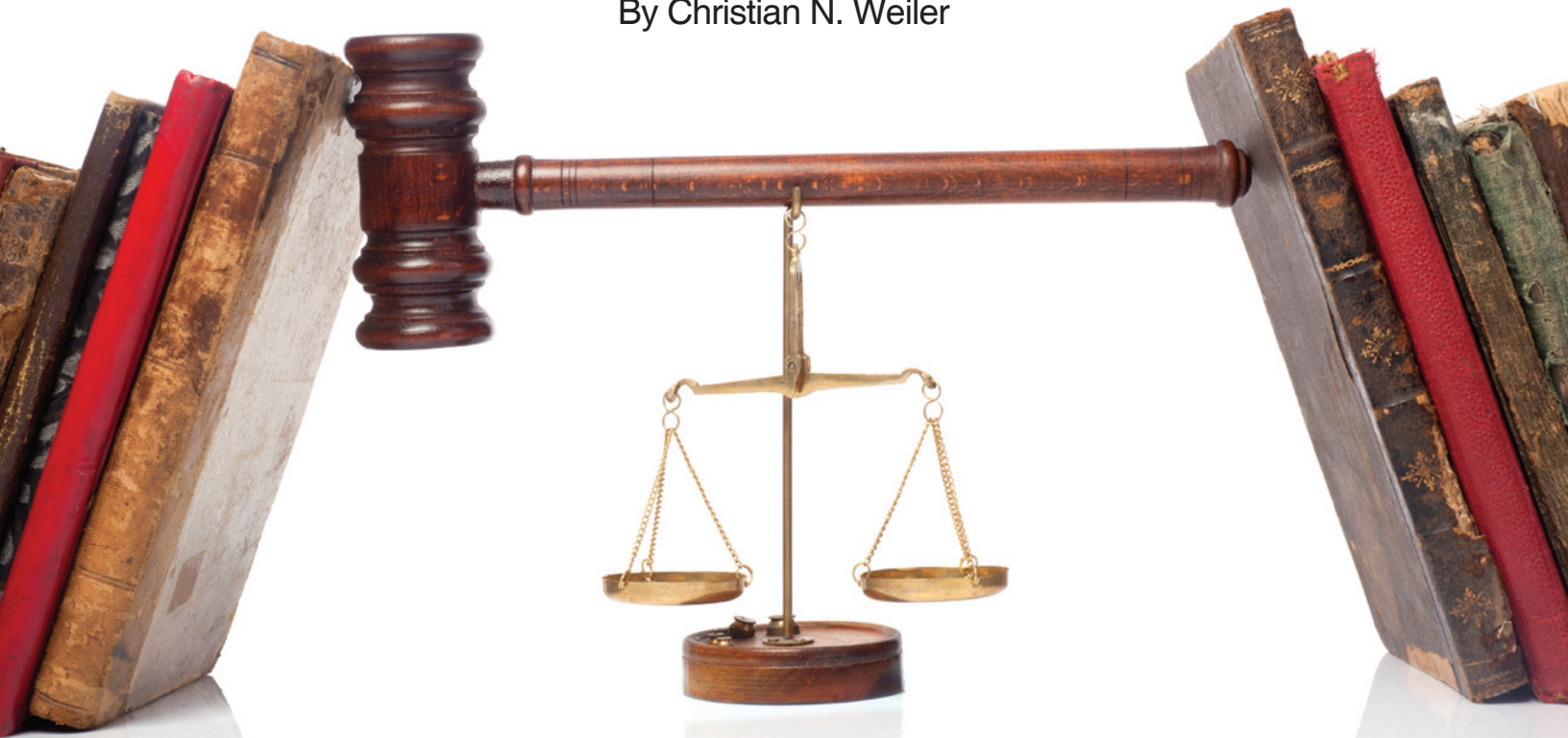


# THE LOW-PROFIT LIMITED LIABILITY COMPANY HAS ARRIVED IN LOUISIANA

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**D**uring the 2010 general session, the Louisiana Legislature enacted legislation to allow the creation of a new type of limited liability company called the “Low-Profit Limited Liability Company” or “L3C.”<sup>1</sup> An L3C is a new form or “subset” of a limited liability company and is intended to be a mixture of for-profit and tax-exempt investors. The L3C is being touted as a wonderful new opportunity for private foundations to expand investment in program-related investments.

L3C legislation was first enacted in Vermont in April 2008. In 2009, L3C legislation was enacted in Michigan, Wyoming, Utah and Illinois. As of now, L3C legislation has been adopted in approximately nine states.

The L3C concept differs from a traditional LLC in that the primary or significant purpose of the L3C cannot be to make a profit, but rather to achieve a social benefit, with profit as a secondary or ancillary purpose. The name itself, Low-Profit Limited Liability Company, is a bit of a misnomer

since the business is not restricted in how much profit it can make.

## Requirements of an L3C

Under Louisiana law, an L3C is required to set forth in its articles of organization, and at all times satisfy a business purpose in conformity with, each of the following requirements:

- (a) The entity significantly furthers

the accomplishment of one or more charitable or educational purposes within the meaning of Section 170(c)(2)(B) of the Internal Revenue Code (IRC) and would not have been formed but for the entity's relationship to the accomplishment of charitable or educational purposes.

(b) No significant purpose of the entity is the production of income or the appreciation of property provided; however, the fact that an entity produces significant income or capital appreciation shall not, in the absence of other factors, be conclusive evidence of a significant purpose involving the production of income or the appreciation of property.

(c) No purpose of the entity is to accomplish one or more political or legislative purposes within the meaning of IRC § 170(c)(2)(D).<sup>2</sup>

Within the articles of organization, an L3C must indicate whether the company is a low-profit limited liability company and is required to use the words "low-profit limited liability company" or the abbreviations "L3C" or "l3c."<sup>3</sup>

If a company organized to meet the requirements of an L3C at its formation or at any time ceases to satisfy any one of the foregoing requirements, it shall immediately cease to be a Low-Profit Limited Liability Company, but by continuing to meet all the other requirements of Louisiana law, it shall continue to exist as a limited liability company. In such event, the articles of organization shall be amended and the name of the company shall be changed to be in conformance with La. R.S. 12:1306, which requires the use of the words "limited liability company" or the abbreviations LLC or LC.<sup>4</sup>

## Potential Purposes of an L3C

According to the IRS, an L3C is not a nonprofit organization and it does not qualify as a tax-exempt organization unless all its members (*i.e.*, investors) are tax-exempt entities.<sup>5</sup>

In theory, the L3C bridges a gap between for-profit entities and certain nonprofit entities, namely entities categorized by federal law as private foundations. Under the Inter-

nal Revenue Code, a private foundation is any domestic or foreign religious, scientific or charitable organization described in IRC § 501(c)(3), other than organizations that meet one of the four requirements found in IRC § 509(a). In other words, a private foundation includes most 501(c)(3) charities, other than "public charities" and other specifically excluded charities, within the meaning of the Internal Revenue Code.

Due to the self-imposed restrictions on an L3C created by the Louisiana Legislature, a validly formed and operating L3C likely complies with the stringent requirements of IRC § 4944(c), which are otherwise known as "program-related investments" or "PRIs" and are imposed on L3Cs.

PRIs are investments made by private foundations in a for-profit venture that are in furtherance of the foundations' charitable, educational or religious activity. Historically, private foundations have carefully analyzed and limited such funding because these types of investments could jeopardize the foundation's exempt purpose, which in turn could jeopardize its qualified status with the Internal Revenue Service. A private foundation and its managers could have taxes imposed upon them for making investments in violation of IRC § 4944. The designation as an L3C is intended to eliminate this risk by labeling these types of companies as presumptively pre-qualified to receive funding from a private foundation. L3Cs provide a new opportunity for a private foundation to utilize its resources and assist in addressing social issues that ordinarily would be limited to organizations that are qualified as nonprofit entities.

Compliance with IRC § 4944(c) by an L3C opens up a new avenue of financing for those companies that focus on achieving one or more social benefits. An L3C is able to leverage a private foundation's status and access capital for its ventures, while offering in return the prospect of a positive social impact and reasonable assurance of its compliance with IRC § 4944.

## Pros and Cons of an L3C

The L3C structure limits its purpose. While it is apparent that an L3C is a "subset" of an LLC (as it is contained within the relevant portions of Chapter 22, Title 12 of the Louisiana Revised Statutes), there is

no history for this entity in Louisiana, and likewise there is little, if any, legal precedent on this entity in the United States.

As of now, L3C legislation is available in a handful of states, including Louisiana. While the Internal Revenue Service has issued a few nonbinding opinion letters, nothing definitive has been said concerning whether a private foundation's investment in a L3C will qualify as a PRI.

Louisiana law provides that the L3C status is revoked and converted to an LLC if the entity does not comply with the primary purpose requirements found in La. R.S. 12:1302. On a practical level, how is failure determined or invoked, and by whom? Similarly, what are the tax implications to the private foundation's investment upon such conversion from an L3C to an LLC?

L3Cs offer a competitive edge to those businesses established in Louisiana whose primary goal is to achieve one or more charitable or educational purposes. Only time will tell whether L3Cs can reach their full potential and serve as a conduit for investments in Louisiana through private foundations. Certainly clarity from the IRS will go a long way in helping L3Cs reach this goal.<sup>6</sup>

## FOOTNOTES

1. 2010 La. Acts, No. 417, amending Revised Statutes Title 12, Chapter 22, Parts I and II.
2. La. R.S. 12:1302 C(1).
3. La. R.S. 12:1306 A(1)(b).
4. La. R.S. 12:1302 C(2).
5. See Instructions for IRS Form 1023, Part II.
6. For more information on L3Cs, check out Americans for Community Development at [www.americansforcommunitydevelopment.org](http://www.americansforcommunitydevelopment.org).

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