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Mutually Beneficial Relationship: How the Low-Profit Limited Liability Company can Build a Brand and Grow America's Wind Energy Infrastructure

Benjamin H. Nissim

NOTES

A MUTUALLY BENEFICIAL RELATIONSHIP: HOW THE LOW-PROFIT LIMITED LIABILITY COMPANY CAN BUILD A BRAND AND GROW AMERICA'S WIND ENERGY INFRASTRUCTURE

Benjamin H. Nissim*

Introduction

This Note will examine how the adoption of the Low-Profit Limited Liability Company (L3C) can facilitate the growth of the United States' wind energy infrastructure. The L3C is a hybrid legal form that has been statutorily defined in eight states. As adopted, the L3C is an amalgamation of for-profit and not-for-profit purposes. The form allows for both socially beneficial ends and positive investor returns. In theory, the L3C will help capture a growing body of socially minded investors with an interest in "doing good" and generating a profit.

This Note will begin with a discussion of the L3C. This will include looking at the ethical impetus for the L3C and its place in the greater context of corporate and not-for-profit law. The examination of the L3C will continue with a discussion of how the form serves as a vehicle for socially beneficial investment. This will involve a discussion of typical L3C governing statutes, how the L3C is designed to leverage private foundation funds, and how the form may help encourage private investment. I will also address arguments against the adoption of the L3C and why the entity has been described as superfluous. The Note will then turn to the application of the L3C to the development of the U.S.'s wind energy industry. This will include showing how the L3C may prove to be an important tool for leveraging private foundation investment, taking advantage of state and federal

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incentives, and creating a "brand" synonymous with socially beneficial ends.

I. THE L3C AND THE GROWTH OF SOCIAL ENTREPRENEURSHIP

The L3C is a legal form designed to take advantage of investor interest in social enterprise.[1] The L3C was designed by Robert Lang of the Mary Elizabeth & Gordon Mannweiler Foundation to combine the goals of social engagement and profit-making.[2] The form was developed to help harness a full spectrum of investors—from not-for-profit private foundations to institutional actors—and to overcome some of the traditional limitations of the for-profit and not-for-profit forms.[3] The L3C accomplishes this through statutory requirements and a flexible organizational structure that allows for the distribution of risks and returns. The branding of the L3C is also part of a concerted effort to capture awareness and public trust.[4] Arguments against the adoption of the L3C form arise from the lack of federal recognition, potential redundancy based on already available forms, and practical and theoretical issues of board and investor confusion resulting from the "serving two masters" problem.[5]

A. *The Emergence of a Fourth Sector*

The L3C has developed in response to the limitations of typical for-profit and not-for-profit forms. While for-profit entities are able to engage in socially beneficial projects,[6] these for-profit businesses have traditionally been limited in the extent that they can stray from the purpose of making a profit. As described in *Dodge v. Ford Motor Co.*, and in myriad decisions shaping director and officer fiduciary duties since, the purpose of a corporation is

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1. A social enterprise has been defined as "'an organization or venture that achieves its primary social or environmental mission using business methods,' typically by operating a revenue-generating business." Robert A. Katz & Antony Page, *The Role of Social Enterprise*, 35 VT. L. REV. 59, 59 (2010) (quoting *Social Enterprise: Defining the Movement*, SOC. ENTER. ALLIANCE, http://www.se-alliance.org/about_movement.cfm (last visited Jan. 2, 2013)).

2. James P. Joseph & Andras Kosaras, *New Strategies for Leveraging Foundation Assets*, 20 TAX'N EXEMPTS 22, 29 (2008).

3. *Id.*

4. Robert Lang & Elizabeth Carrott Minnigh, *The L3C, History, Basic Construct, and Legal Framework*, 35 VT. L. REV. 15, 17 (2010).

5. *See, e.g.*, Carter G. Bishop, *The Low-Profit LLC (L3C): Program Related Investment by Proxy or Perversion?*, 63 ARK. L. REV. 243 (2010); Daniel S. Kleinberger, *A Myth Deconstructed: The "Emperor's New Clothes" on the Low-Profit Limited Liability Company*, 35 DEL. J. CORP. L. 879 (2010).

6. A.P. Smith Mfg. Co. v. Barlow, 98 A.2d 581, 589–90 (N.J. 1953).

to make a profit, that is, to benefit shareholders.[7] This formulation, though applied more flexibly now than in the early twentieth century, explains the risk a for-profit entity takes by placing a socially beneficial activity above the pursuit of profits.[8] Though directors are protected by the business judgment rule, it ultimately is not in a director's or a corporation's best interest to push the boundaries of what constitutes business as usual.

Different theories have been proffered to address the disconnect between the role of for-profit entities in society and the corporation's profit-driven focus.[9] The "Contractarian" view describes a corporation as a "web of contracts."[10] The different vested interests in the corporation (shareholders, directors, clients, etc.) are born from what these differing actors have invested in the corporation. The web of contracts that results benefits society. That is, the purpose of the corporation is to make profits for the shareholder because shareholder wealth is societal wealth. Society inputs security and infrastructure and gets the return of taxes and the benefits of what is produced. The implication in this discussion is that corporations—and by extension for-profit entities as a whole—benefit society through the creation of wealth. The merits of this conclusion should not be overstated. While wealth plays a significant role, there are many different ways to benefit society beyond the use and distribution of capital.

For the purpose of this paper, the "Communitarian" model better encapsulates the multifaceted nature of societal growth and public benefit. The theory posits a quid pro quo relation-

7. Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919) ("A business corporation is organized and carried on primarily for the profit of the stockholders. The powers of the directors are to be employed for that end. The discretion of directors is to be exercised in the choice of means to attain that end, and does not extend to a change in the end itself, to the reduction of profits, or to the nondistribution of profits among stockholders in order to devote them to other purposes.").

8. Even with the broad statement of purpose typically used in corporate charters and bylaws ("to engage in any lawful activity"), a lawful activity within this paradigm is one in which shareholder value is maximized.

9. Some jurisdictions provide for "other constituency statutes," which permit a director to look at a variety of constituencies in the process of making a business judgment. However, the Delaware case of *Unocal Corp. v. Mesa Petroleum Co.* indicates that while a board may consider the needs of other constituencies, ultimately those other considerations must be balanced against the needs of the shareholders. Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 955–56 (Del. 1985).

10. *See* Michael Klausner, *The Contractarian Theory of Corporate Law: A Generation Later*, 31 J. CORP. L. 779 (2006).

ship between corporations and society.[11] Society permits corporations to exist and, in return, there is an expectation that corporations conform to norms of social responsibility. Corporations are a "web of relationships" connected to all stakeholders. This "web of relationships" leads to the idea that, while the pursuit of profits is paramount, corporations must also have a social consciousness, e.g., treating employees well, minimizing pollution, and giving to charity.[12] While these models provide an interesting structure to frame our expectations for corporate behavior, the real-world practice of for-profit entities has (in part) catalyzed the development of the L3C.

The not-for-profit world[13] is comprised of a variety of organizations that have been granted a special status because of their role in civil society.[14] That said, the not-for-profit form can also limit an organization's ability to develop and finance projects and products.[15] Section 501(c)(3) of the Internal Revenue Code requires that all entities seeking tax exemption under that provision be organized and operated exclusively for religious, charitable, scientific, or other enumerated purposes.[16] A 501(c)(3) organization[17] is also prohibited from causing earnings to inure to the benefit of any private individual.[18] These two requirements influence the scope of not-for-profit work.[19] With their

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11. David Millon, *Two Models of Corporate Social Responsibility*, 46 WAKE FOREST L. REV. 523, 526 (2011) ("[N]onshareholders should not be required to rely on their own contractual bargaining capabilities to protect their interests.").

12. *See* Paul N. Cox, *The Public, the Private and the Corporation*, 80 MARQ. L. REV. 391, 491 (1997) (explaining that communitarianism asks that legal enforcement move to "enforcement of a norm of fidelity to the interests of the dependent, and from there . . . fidelity to the unity of state conceived interests and objectives that is the norm of solidarity.").

13. This world is often referred to as the "Third Sector," distinct from the government and for-profit sectors.

14. For the purpose of this Note, I will focus on those not-for-profits colloquially known as 501(c)(3)s because they qualify for exemption from federal income tax under Internal Revenue Code § 501(c)(3) (2010).

15. *See* 26 U.S.C. § 501(c)(3) (2010); 26 C.F.R. § 1.501(c)(3)-1 (2008).

16. *See* 26 U.S.C. § 501(c)(3).

17. Entities organized under section 501(c)(3) are more commonly known as "charities." The Internal Revenue Code provides 501(c)(3) organizations with a number of benefits, including tax exemption and the ability to receive tax-deductible contributions. 26 U.S.C. § 170 (2010). This special status helps channel private (and public) funds towards socially desirable goals.

18. This prohibition applies regardless of whether the beneficiaries are insiders (known as private inurement) or outsiders (private benefit). *See* 26 U.S.C. § 501(c)(3).

19. The limitations on the way that a 501(c)(3) may be organized and operated—the purpose and the performance of that purpose—limit the type of businesses that may be brought under the 501(c)(3) umbrella. Not every

relatively narrow purpose and a dependency on outside funding, not-for-profits have been unable to take full advantage of a growing culture of socially engaged investors.

Social enterprise organizations represent a separate "fourth sector," comprised of the values and goals that drive the for-profit and not-for-profit worlds.[20] These organizations "combine charitable missions, corporate methods, and social and environmental consciousness in ways that transcend traditional business and philanthropy."[21] They are therefore meant to fill the gap between the corporate and not-for-profit models.[22] Social enterprise organizations include such entities as the L3C, the Benefit Corporation,[23] the Flexible Purpose Corporation,[24] and internationally, the Community Interest Company.[25] Like the for-profit

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organization can be this type of not-for-profit. The second requirement—the no inurement requirement—is far more significant to the discussion of the L3C. 501(c)(3)s rely on charitable donations (and the corresponding benefits to the donor as an incentive) and federal and state governments to support their missions. This reliance is born from the inability of the nonprofit to provide returns to investors or directors. While 501(c)(3)s are free to make a profit, that profit must in turn be reinvested in the organization. JAMES J. FISHMAN & STEPHEN SCHWARZ, NONPROFIT ORGANIZATIONS: CASES AND MATERIALS 445–52 (4th ed. 2010). Private inurement can be met with intermediary sanctions, significant tax assessments, and revocation of 501(c)(3) status. This reality significantly inhibits the ability of a 501(c)(3) to attract investors in support of its mission. Private benefit, or the distribution of benefits, to non-insiders is also closely regulated, though with less harsh penalties. *Id.* at 458–60.

20. THOMAS J. BILLITTERI, ASPEN INST., MIXING MISSION AND BUSINESS: DOES SOCIAL ENTERPRISE NEED A NEW LEGAL APPROACH? 2 (Jan. 2007).

21. *Id.*

22. Public institutions make up the final sector (the "second" sector).

23. Benefit Corporations share a number of similarities with the L3C. Benefit Corporations have dual missions, but their governance systems are more akin to a traditional corporation when compared to the L3C. Dana Brakman Reiser, *Benefit Corporations—A Sustainable Form of Organization?*, 46 WAKE FOREST L. REV. 591, 611–17 (2011). The Benefit Corporation is a creature of statute. This differs from a B-Company, which is a for-profit entity that has received a certification from a private company, indicating that the corporation has demonstrated "their commitment to a dual mission of making profits and promoting social good." *Id.* at 592.

24. CAL. CORP. CODE § 2500 (West 2012). The Flexible Purpose Corporation is a legal form that "allow[s] a corporation to integrate the for-profit philosophy of the traditional corporation with a *special purpose* mission that is similar to a charitable purpose." Angelica Salceda, *Flexible Purpose Corporation: California's New Corporate Form*, BERKELEY L. BLOGS (Dec. 13, 2011, 6:28 PM), http://thenetwork.berkeleylawblogs.org/2011/12/13/flexible-purpose-corporation-california%E2%80%99s-new-corporate-form/.

25. The Community Interest Company (CIC) is a British corporate model that has been "created for the use of people who want to conduct a business or other activity for community benefit, and not purely for private advantage." *Community Interest Companies*, DEP'T FOR BUS. INNOVATION & SKILLS, http://www.

firm, these firms operate with the intent to make a profit. But, this profit will come "in a manner that generates more public benefit or positive externalities than would a conventional for-profit firm."[26] They are said to operate with a "double bottom line," working to benefit both owners and society.[27] Some have argued that these so called social enterprise organizations should be afforded the same tax exemption rights as not-for-profits.[28] While that proposal fights for traction, the L3C fills the gap created by the legal limitations of the for-profit and not-for-profit dichotomy. As a hybrid entity, the L3C aims to fuse social well-being, ideals of corporate behavior, and the realities of investor behavior.

B. *Defining the Low-Profit Limited Liability Company*

The L3C is designed to bridge the gap between the for-profit and not-for-profit forms and thereby generate investment in social enterprise. The statutory definition of an L3C is typically appended to a state's limited liability company statute.[29] L3C statutes have been enacted in eight states.[30] The enacted statutes generally have consistent language.[31] The first state to pass L3C legislation was Vermont in 2008, quickly followed by

bis.gov.uk/cicregulator (last visited Jan. 2, 2013). For more information on the CIC see *id.*

26. Katz & Page, *supra* note 1, at 86.

27. This formulation shares similarities to the Communitarian theory discussed previously. *See supra* Part I.A. Andrew Savitz and Karl Weber have also argued for a "triple bottom line," looking at people, profit, *and* planet. Katz & Page, *supra* note 1, at 86 n.164.

28. BILLITTERI, *supra* note 20, at 3 (discussing Anup Malani and Eric A. Posner's argument in their paper "The Case for For-Profit Charities", *available at* Anup Malani & Eric A. Posner, *The Case for For-Profit Charities*, 93 VA. L. REV. 2017 (2007)).

29. John Tyler, *Negating the Legal Problem of Having "Two Masters": A Framework for L3C Fiduciary Duties and Accountability*, 35 VT. L. REV. 117, 141 (2010).

30. 805 ILL. COMP. STAT. 180/1-26 (2010); LA. REV. STAT. ANN. § 12:1302 (2010); ME. REV. STAT. tit. 3, § 1611 (2011); MICH. COMP. LAWS § 450.4102(m) (2010); N.C. GEN. STAT. § 57C-2-01(d) (2010); R.I. GEN. LAWS § 7-16-76 (2012); UTAH CODE ANN. § 48-3-1302 (West 2012); VT. STAT. ANN. tit. 11, § 3001 (2008); WYO. STAT. ANN. § 17-29-102(a)(ix) (2010).

31. For instance the Vermont statute reads:

"L3C," or "low-profit limited liability company" means a person organized under this chapter that is organized for a business purpose that satisfies and is at all times operated to satisfy each of the following requirements:

A. The company:

i. 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 of 1986, 26 U.S.C. § 170(c)(2)(B); and

Michigan and Wyoming.[32] L3C statutes track the statutory definition of a "program related investment" (PRI). The PRI is a tool used by private foundations to make potentially jeopardizing investments.[33] This is an explicit effort to leverage private foundation capital. The belief is that initial private foundation investments and risk acceptance will incentivize both additional private and public investments. The name "L3C" is also an attempt to create a brand.[34] In much the same way that the not-for-profit form makes use of a brand that signals a unique societal role, affixing "L3C" to the end of a company name is meant to evoke the notion of a socially responsible business.[35] According to interSector Partners, L3C, a company dedicated to promoting the adoption of the L3C, 658 L3Cs have been formed nationwide.[36]

A PRI is an investment made by a private foundation through an exception to the jeopardizing investment rule.[37] A jeopardizing investment is an investment of any amount that might "jeopardize the carrying out of any of [the foundation's] exempt purposes . . . ."[38] The IRS has further defined a jeopardizing investment as one in which managers "have failed to exercise ordinary business care and prudence, under the facts and circumstances prevailing at the time of making the investment, in providing for the long- and short-term financial needs of the foundation to carry out its exempt purposes."[39] Such an investment will result in a tax equal to 10% of the investment on the foundation *and* on any managers who willfully participated in

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ii. would not have been formed but for the company's relationship to the accomplishment of charitable or educational purposes.

B. No significant purpose of the company is the production of income or the appreciation of property; provided, however, that the fact that a person 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."

VT. STAT. ANN. tit. 11, § 3001.

32. David J. Schwister, Note, *L3Cs: The Next Big Wave in Socially Responsible Investing or Just Simply Too Good to Be True?*, 3 J. BUS. ENTREPRENEURSHIP & L. 1, 4–5 (2009).

33. *Id.* at 3.

34. Lang & Minnigh, *supra* note 4, at 17.

35. *Id.*

36. *Latest L3C Tally*, INTERSECTOR PARTNERS, L3C, http://www.intersectorl3c.com/l3c_tally.html (last visited Jan. 2, 2013).

37. 26 U.S.C. § 4944(a) (2010).

38. *Id.*

39. 26 C.F.R. § 53.4944-1 (2012).

making the investment.[40] If the investment is not corrected within the next taxable period an additional 25% tax is imposed on the foundation and a 5% tax on foundation managers who refuse to remove the investment from jeopardy.[41] These are significant penalties. The PRI exception to the jeopardizing investment tax is available for those investments "the primary purpose of which is to accomplish one or more of the purposes described in section 170(c)(2)(B), and no significant purpose of which is the production of income or the appreciation of property . . . ."[42]

While the PRI seems like an accessible way to work around the jeopardizing investment tax, its use has been limited. The effort and expense needed to ensure the investment is appropriate coupled with the stiffness of the penalty has acted as a deterrent.[43] An investment will qualify as a PRI only if three conditions are met:

1. The primary purpose of the investment is to accomplish one or more charitable purposes.
2. Neither the production of income nor the appreciation of property is a significant purpose of the investment.
3. The purposes of the investment do not include engaging in lobbying or advocacy [or other election activities].[44]

A "but-for" test is used to determine whether the investment's primary purpose is charitable. This means that the investment must primarily further the foundation's charitable purpose and "would not have been made but for such relationship between the investment and the accomplishment of the foundation's exempt activities."[45] In private letter rulings, the IRS has looked to whether there is a "nexus between the PRI and the foundation's exempt mission and inquires into the relative 'necessity' of the PRI."[46] The concern in this part of the test is whether an investment actually qualifies for the PRI. The ambiguity in the IRS's definition requires a cautious approach by foundation managers.[47] Going forward with a PRI necessitates a

40. *Id.* The tax on managers is capped at $10,000 upon the finding of a jeopardizing investment under § 4944(a). 26 U.S.C. § 4944(d)(2) (2010).

41. 26 U.S.C. § 4944(b) (2010). The tax associated with this penalty is capped at $20,000 per investment. 26 U.S.C. § 4944(d)(2).

42. 26 U.S.C. § 4944(c) (2010).

43. Benjamin N. Feit, *What IRS Private Letter Rulings Reveal About Program-Related Investments*, 23 TAX'N EXEMPTS 3 (2011).

44. 26 C.F.R. § 53.4944-3(a)(1) (2012).

45. 26 C.F.R. § 53.4944-3(a)(2)(i) (2012).

46. Feit, *supra* note 43, at 9.

47. *Id.*

strong opinion from qualified counsel or a private letter ruling by the IRS. Both of these options result in significant expenditures of time and money.[48] A foundation will likely also have to act with "expenditure responsibility" over a PRI as well. Expenditure responsibility requires a foundation to closely oversee the actions of the investment recipient to ensure that the recipient is not exposing the foundation to jeopardizing investment taxes or calling into question the foundation's exempt status.[49] This portion of the test has proven to be a significant roadblock to the widespread use of the PRI.

The "substantial purpose" test looks to whether the production of income or property is a significant purpose of the investment. The relevant factor in this test is whether "investors solely engaged in the investment for profit would be likely to make the investment on the same terms as the private foundation."[50] However, an investment will not be disqualified just because it results in income.[51] The "Low-Profit" part of the L3C's name has been described as a misnomer in this regard.[52] While PRIs, and L3Cs by extension, cannot be organized with the substantial purpose of producing a profit, this does not *preclude* the making of a profit.[53] The L3C and the private foundation can return a profit at, or above, market levels.[54] The final requirements which prohibit expenditures for political campaigns or lobbying track the regular limitations imposed on private foundations and are of less interest to this inquiry.

The L3C's enacting statute closely mirrors the language of the PRI investment requirements. This is designed to facilitate the use of PRIs.[55] The form is meant to provide certainty in a realm where foundations have felt anything but certain. The goal, therefore, is two-fold: first, to provide assurance that a program-related investment does in fact qualify as such, without having to jump through the traditional hoops foundations have had

48. *See* Bishop, *supra* note 5, at 244. See Feit, *supra* note 43, at 12, for a discussion of the IRS's increasingly liberal interpretation of what qualifies as a PRI so as to "lubricate" the process. Despite this liberal application, the expense for a private letter ruling *begins* with a $10,000 filing fee. Rev. Proc. 2012-8, 2012-1 I.R.B. 241. Naturally, legal fees and other costs can add significant additional expenses.

49. Bishop, *supra* note 5, at 244; *see also* Joseph & Kosaras, *supra* note 2, at 26.

50. 26 C.F.R. § 53.4944-3(a)(2)(iii).

51. Joseph & Kosaras, *supra* note 2, at 25.

52. Tyler, *supra* note 29, at 124.

53. *Id.*

54. *Id.*

55. *See* Lang & Minnigh, *supra* note 4, at 19.

to address[56] and second, to provide notice to foundations (and the IRS) that investors and organizations are looking for an increased emphasis on program-related investments as an alternative means for raising capital.[57]

For an L3C, PRI investments serve not only as an infusion of capital itself, but also as a tool used to leverage investments by private actors. By focusing on the PRI rules, the L3C seeks to create investment incentives.[58] With an initial PRI investment the L3C can create a tranched financing structure.[59] As the "substantial purpose" test indicates, an investment would not qualify as a PRI if it is made on the same terms as another profit-seeking investor would have made. Tranche investing helps to ensure that this qualification is met.[60] Under this investment scheme, the private foundation would make a PRI in an L3C, accepting a high-risk and below-market return for that investment.[61] Additional investments thereby become more attractive by "improving the credit rating and thereby lowering the cost of capital."[62] Distributing risk in this fashion makes the investment that much more attractive to a commercial enterprise.[63] A tranched investment scheme also allows for a clear class system in the operating agreement.[64] Having a private foundation with its own class and governing powers (e.g., voting rights, veto powers) would help ensure that the socially beneficial mission is not subsumed in the profit seeking venture. This provides an important mechanism for the L3C to raise capital and still maintain its identity.

The L3C is also a brand. The hope is that organizations will be better able to raise funds by attracting socially-conscious investors with the L3C brand. One of the key mechanisms not-for-profits use to raise money is the public's trust in the not-for-profit

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56. *See* Joseph & Kosaras, *supra* note 2, at 29.
57. *See* Feit, *supra* note 43, at 3.
58. Lang & Minnigh, *supra* note 4, at 17.
59. *Id.*
60. Bishop, *supra* note 5, at 263.
61. *Id.*
62. Kleinberger, *supra* note 5, at 884–85.
63. Tyler, *supra* note 29, at 125. It is important to note, however, that the universe in which L3Cs operate is not limited to private foundation investment. While the governing statute is based on the PRI language, the L3C does not *require* investments from a private foundation. As a separate legal entity, funding for the L3C can take many forms. As Tyler discusses, "among the LLC-derived benefits of the L3C form is the flexibility in financing and governance structures that are permitted . . . . [tranching approaches] are not likely to characterize all (or even most) L3Cs." *Id.* at 125 n.36. While the tranching model looks to take advantage of program-related investments, the potential of the form should not be viewed as limited to only that model. *Id.* at 125.
64. Lang & Minnigh, *supra* note 4, at 18.

designation.[65] It is generally understood that a not-for-profit works in those areas where for-profit entities cannot, or will not, go in the course of regular business. The public generally trusts the not-for-profit to use donated funds for a charitable purpose. In creating the L3C, Robert Lang envisioned a similar sense of security and purpose.[66] Having a positive brand associated with the L3C label should help to generate business investment and consumer trust.

Ultimately, the goal of the L3C is to engage in a level of social enterprise not achievable through traditional for-profit and not-for profit means. By aligning with foundations through the use of PRIs and providing incentives for investors interested in social enterprise, the L3C represents an opportunity for business ventures to direct themselves toward the public benefit. Though detractors argue against the efficacy of the form, this statutory innovation is a unique tool meant to address the gap created by traditional business models. Circular as it may be, the existence of the L3C speaks to the legitimacy of its purpose. As a brand and as a vehicle, the L3C embodies an important way of looking at the goals of business.

C. *The Limitations of the L3C Form: Arguments Against the Efficacy of the Low-Profit Limited Liability Company*

While authors, investors, and eight states have seen a benefit in the L3C, there remain questions about the necessity and efficacy of the form. Critiques of the L3C revolve around three main arguments: a lack of federal recognition means the L3C provides no additional benefits to the existing business entity structure, fiduciary duties created by the dual purpose of social benefit and profit are unworkable, and the goals of the form can already be executed through the LLC without the addition of an L3C statute.

The L3C statute was initially developed to mimic PRI requirements so as to facilitate private foundation investment. However, while the language may be enacted into law in individual states, Congress and the IRS have not made a formal judgment on the L3C.[67] Proponents have been unable to secure a rebuttable presumption of PRI status on L3C investments at the

65. *See* Nathalie Kylander & Christopher Stone, *The Role of Brand in the Nonprofit Sector*, 10 STAN. SOC. INNOVATION REV. 35 (2012).

66. Lang & Minnigh, *supra* note 4, at 17 ("A brand is important as a quick identifier that lets everyone know what the entity is. A nonprofit is a brand and L3Cs needed that identification.").

67. Kleinberger, *supra* note 5, at 905–07.

federal level.[68] The fact that the IRS has not disclosed an approach to the form means private foundations are likely in the same place they began—juggling the complicated and expensive rules surrounding PRIs. The response to these criticisms is that while the lack of a federal exception made for the L3C certainly dampens the enthusiasm behind it, the current state of affairs may not remain the status quo. Should states continue to seek mechanisms to drive social enterprise, a formal federal approach may emerge. Further, the funding and the social enterprise goals of an L3C are not limited to foundation investments. The L3C is merely meant to facilitate them.

Investments that are made for profit drive the second critique. The concern is that the fiduciary duties of L3C directors will be muddled as a result of their serving "two masters." Difficulties arise in ensuring that the L3C remains committed to social enterprise objectives, when dealing with SEC disclosure laws, and with expectations for directors.[69] In response, John Tyler discusses a formulation of L3C fiduciary duties that is meant to address the perceived irreconcilability of the L3C's "two masters":

> - [T]he primary purpose of the L3C operations must prioritize pursuing charitable, exempt purposes, thereby exalting charitable purpose above all other purposes; and
>
> - [R]ealizing profit and enhancing value can be purposes of the enterprise as long as they are not significant purposes, thereby subordinating profit motive and placing it not just secondary on the continuum of permissible purposes, but near the extreme end of such continuum.[70]

It is important to understand that there is an *ordering* of fiduciary duties. At its most basic, the form requires the pursuit of an exempt purpose while acknowledging that it is perfectly possible to derive a profit in the process.

In addition to considerations of whether the L3C will actually help in the development of social enterprise is the question of whether the new form is even necessary. Professor Daniel Kleinberger argues that the placement of the L3C statute as an

68. *Id.* at 907–08; *see also* J. William Callison & Allan W. Vestal, *The L3C Illusion: Why Low-Profit Limited Liability Companies Will Not Stimulate Socially Optimal Private Foundation Investment in Entrepreneurial Ventures*, 35 VT. L. REV. 273 (2010).

69. Callison & Vestal, *supra* note 68, at 287–88. While a brief discussion of these issues follows, a more fleshed out discussion of these critiques is unnecessary for this Note.

70. Tyler, *supra* note 29, at 141.

addendum to state LLC law is telling.[71] His contention is that most LLC statutes are capable of accomplishing the same goals the L3C is designed to accomplish.[72] He argues that an LLC should be able to receive PRIs and, through an operating agreement, meet social enterprise goals. The response to this point is that while there is an inherent flexibility to the LLC form, this flexibility does not necessarily negate the benefit of an L3C statute. Foremost, there is no guarantee that a state will allow an LLC to pursue a purpose other than one for-profit.[73] Additionally, as discussed, the L3C moniker as a brand is meant to provide value through driving investor interest and consumer confidence. This is lost through a reliance on existing LLC statutes.[74]

Finally, notwithstanding these issues, the continued adoption of the L3C and increased focus on social enterprise as a valid guiding principle is evidence of an interest in having such a gap-filling entity. It is possible that with the development of applications for the L3C—specific instances where the form facilitated the growth of a profitable and socially beneficial industry—awareness and acceptance of the form will develop in turn. The rest of this Note will examine how the L3C can play this role in the context of the wind energy sector.

II. Facilitating Investment in the Wind Energy Sector through the L3C

A. *The State of Wind Energy Investment*

The use of fossil fuels plays a significant role in human health and quality of life. There is a stark difference between air quality in Los Angeles or Beijing, and the air in Buford, Wyo-

71. Kleinberger, *supra* note 5, at 896–98.

72. *Id.*

73. Professor Kleinberger notes that many LLC statutes no longer require a for-profit purpose, but discusses only the Revised Uniform Limited Liability Company Act (RULLCA). This Act has been characterized with the statement: "its prognosis for becoming widely adopted looks bleak." Doug Batey, *Nebraska and Wyoming Enact the Revised Uniform LLC Act*, LLC Law Monitor (Nov. 22, 2010), http://www.llclawmonitor.com/2010/11/articles/revised-uniform-llc-act/nebraska-and-wyoming-enact-the-revised-uniform-llc-act/. However, with New Jersey's and California's recent adoption of RULLCA, the acts "prognosis" may have changed. Doug Batey, *California and New Jersey Adopt RULLCA, the Revised Uniform Limited Liability Company Act*, LLC Law Monitor (Jan. 2, 2013), http://www.llclawmonitor.com/tags/rullca/.

74. Professor Kleinberger also critiques the notion of an L3C brand. *See* Kleinberger, *supra* note 5, at 897–99. A full examination of his argument is beyond the scope of this Note.

ming.[75] The cost of oil has increased dramatically, with electricity bills following in step.[76] Whether sustainability and combating climate change is a goal or not, increasing energy output through alternative sources in order to reduce costs, improve the environment, and develop industry is a reasonable one. The development of the wind energy industry is a means to this end. Though wind power suffers from an intermittent nature, the energy is inherently clean. There are over 470 manufacturing facilities in the U.S. that develop products for the production of wind energy.[77] The wind power industry has increased its production in the U.S. by 35% over the last four years.[78] Wind energy continues to attract heavy interest from investors like Berkshire Hathaway[79] and utility companies.[80] This private investment has been buttressed by the federal government, which has emphasized alternative energy investment generally through tax policy.[81] State governments have also provided incentives and requirements to ensure the development of the alternative energy sector.[82] The L3C can provide the additional link in the chain that allows for local to utility-sized development of wind energy production, bringing public and environmental benefits to communities and actualizing state and federal policy.

The L3C may provide the tool for actors interested in the development of the wind energy sector to overcome the community and financial concerns that have limited the growth of the industry to date.[83] The nature of the L3C form and its alignment

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75. As of July 20, 2011, Buford, Wyoming had only a single resident. Everett Rosenfeld, *Meet the Only Resident of America's Smallest Town*, TIME NEWSFEED (July 20, 2011), http://newsfeed.time.com/2011/07/20/meet-the-only-resident-of-americas-smallest-town/.

76. Diane Cardwell & Clifford Krauss, *As Price of Oil Soars, Users Can Only Shiver and Cross Their Fingers*, N.Y. TIMES, Jan. 22, 2012, at A23.

77. *Industry Statistics*, AM. WIND ENERGY ASS'N, http://www.awea.org/learnabout/industrystats/index. cfm (last visited Jan. 2, 2013).

78. *Id.*

79. *See* Noah Buhayar, *Buffett Energy Firm to Buy Illinois Project in Wind Bet*, BLOOMBERG BUSINESSWEEK (Jan. 23, 2012, 3:30 PM), http://www.businessweek.com/news/2012-01-23/buffett-energy-firm-to-buy-illinois-project-in-wind-bet.html.

80. *See* EXXONMOBIL, 2012 THE OUTLOOK FOR ENERGY: A VIEW TO 2040, at 8 (2012), *available at* http://www.exxonmobil.com/Corporate/files/news_pub_eo.pdf.

81. Discussed *infra* at Part II.D.

82. *See infra* Part II.C.

83. Including the Not-In-My-Back-Yard dilemma, discussed *infra* Part II.B., communities disinclined to accept renewable energies (e.g., because the community revolves around coal mining) as well as issues plaguing the renewable energy industry generally, including reliability questions, grid limitations, and industry ossification, to name a few.

with social enterprise (as opposed to the pure profit goals of traditional energy investors) will facilitate development. As a social enterprise vehicle, the L3C brand will represent a different type of entity to local communities that may help to overcome the Not-In-My-Back-Yard (NIMBY) conundrum associated with wind energy projects. As a creature of state law, the L3C will be able to fill the gap made by state regulatory initiatives. Finally, the L3C's structure and flexibility will help in distributing federal tax benefits associated with wind energy projects. The L3C is thus well suited to be an effective tool for supply-side actors and social entrepreneurs. It can partially internalize the cumbersome externalities associated with wind energy and provide the means for private foundations to invest in socially desirable work while meeting minimum annual investment requirements.

B. *The L3C, Social Enterprise, and Community Acceptance of Wind Energy*

The relationship between humans and the environment is treated differently throughout the world. The U.S. has recognized the importance of the environment through a variety of different mechanisms, including the Environmental Protection Agency and the National Parks System.[84] Telling in the American model is that the National Environmental Policy Act requires that energy developers on federal public lands provide an "Environmental Impact Statement" (EIS). An EIS analyzes how proposed projects will affect "*the quality of the human environment*."[85] At face value this relationship appears to be one of management. The protections in place are born of the legislative and regulatory process rather than grounded in an understanding of something fundamental to the human experience. Juxtapose this approach to many international frameworks and the ethical imperative of careful natural resource stewardship through the development of alternative energy becomes more apparent. For example, over 100 countries have constitutional provisions protecting the environment.[86] The European Convention on Human Rights recognizes environmental pollution as an affront

84. The Bureau of Land Management and the U.S. Forest Service oversee more than 44% of the land that comprises the eleven westernmost states in the continental U.S. Eric S. Spengler, Note, *A Shift in the Wind: The Siting of Wind Power Projects on Public Lands in the Obama Era*, 86 IND. L.J. 1185, 1191 (2011).

85. *Id.* at 1195 (emphasis added) (quoting 42 U.S.C. § 4332(c) (2010)).

86. Helle Tegner Anker et al., *Wind Energy and the Law: A Comparative Analysis*, 27 J. ENERGY & NAT. RESOURCES L. 145, 158 n.46 (2009).

to human rights.[87] The specific obligations and imperatives laid out in international agreements such as the Kyoto Protocol (which the U.S. has not ratified) also point to an essential connection between humans and the environment. By framing the goal of increased alternative energy production as an ethical or rights-based effort the production of wind energy is aligned with the social enterprise mission of the L3C.

Conceptualizing the development of wind energy as a social imperative promoted by the L3C allows for the "L3C brand" to develop. With this, the L3C form may be able to help overcome the significant stumbling blocks associated with the Not-In-My-Back-Yard (NIMBY) dilemma. NIMBY describes the behavior of individuals who fight against the development of certain industries or facilities within proximity to their homes.[88] By no means does the L3C completely remove the difficulties of having wind turbines near residential areas, but the "good" that comes with the development of alternative energy may be more easily conceptualized by a community when the work is being done by an organization with a socially-driven mission and a local connection. Taking from the not-for-profit experience, the L3C may be able to leverage the trust generally given a not-for-profit to more easily facilitate the development of wind energy production. With careful articulation, an L3C's social enterprise goals and the production of wind energy can be aligned without betraying the underlying ethical obligations characterizing the organization and the work. In doing so, those people affected by the production of the wind energy may be more willing, or at least less opposed, to the introduction of the infrastructure in their communities.

C. *Wind Energy Is Local Energy*

State governments have actively engaged the alternative energy sector. States with the comparative advantage that allows for the development of the wind energy industry have aggressively implemented programs that facilitate growth.[89] These

87. The infringement results insofar as environmental concerns harm private property rights. *Id.* at 157–58.

88. *See generally* Tiffany Hsu, *Wind Farms Multiply, Fueling Clashes with Nearby Residents*, L.A. TIMES, July 24, 2011, http://articles.latimes.com/2011/jul/24/business/la-fi-wind-power-20110724. Some of the concerns residents express revolve around aesthetic complaints and the impact of turbines on avian life. *Id.*

89. "Utility-scale" wind projects have been installed in thirty-eight states. *State Policy*, AM. WIND ENERGY ASS'N, http://www.awea.org/issues/state_policy/index.cfm (last visited Jan. 2, 2013). Forty-six states have wind energy-specific

include general goals for attaining a certain percentage of energy provided by alternative sources. These goals are attained through the use of floors, known as Renewable Portfolio Standards (RPS) (or similarly, Renewable Portfolio Goals, or RPGs). States have also implemented their own tax credits and grants. Finally, states have worked to provide support on the demand side. As a creature of state law, the L3C is well positioned to take advantage of the incentives that individual states provide and to work at a local level.

The development of wind energy has a significant impact on a community. Operational wind farms have a definite footprint; infrastructure needs to be put in place often at great scale.[90] However, people generally favor wind power in the abstract.[91] To support alternative energy, states have adopted RPGs and RPSs. Eight states have RPGs and twenty-nine states have RPSs.[92] These goals and standards are meant to create competition within the energy industry by setting a base goal or requirement for alternative energy production by a specific date.[93] States are creating a market. These standards are flexible and are responsive to public participation.[94] The L3C is well suited to fill the gap that these standards create. As a state-based entity, the L3C can leverage private foundation money invested in engaging local community building. This should then attract other investors to help develop the project while keeping the local "feel." While for-profit corporations are also creatures of state law, the social entrepreneurship aspects of the L3C tap into the sense of "trust" charities are afforded. This may facilitate the L3C's ability to have a local, on the ground, connection with a community while fulfilling state RPS/RPG policies. Utilities forced to take part in renewable projects because of these standards have their burdens lessened while the L3C fulfills its mission of social entre-

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incentives. Corey Stephen Shoock, Note, *Blowing in the Wind: How a Two-Tiered National Renewable Portfolio Standard, a System Benefits Fund, and Other Programs Will Reshape American Energy Investment and Reduce Fossil Fuel Externalities*, 12 FORDHAM J. CORP. & FIN. L. 1011, 1023 (2007).

90. Commercial turbines can grow to 116 meters in rotor sweep diameter. *Large Commercial Wind Turbines*, WIND ENERGY: THE FACTS, http://www.wind-energy-the-facts.org/en/part-i-technology/chapter-3-wind-turbine-technology/evolution-of-commercial-wind-turbine-technology/large-commercial-wind-turbines.html (last visited Jan. 2, 2013).

91. Anker et al., *supra* note 86, at 159.

92. *Renewable Portfolio Standard Policies*, DATABASE OF STATE INCENTIVES FOR RENEWABLES & EFFICIENCY, http://www.dsireusa.org/documents/summarymaps/RPS_map.pdf (last visited Jan. 2, 2013).

93. Shoock, *supra* note 89, at 1049–53.

94. *Id.*

preneurship. That is, the gap in the market between the state standards and current capacity can be met more quickly with the assistance of L3Cs dedicated to wind energy production.

Beyond creating the market, states have also worked to *grow* the market. By providing a variety of tax credits, grants, and property tax exemptions, significant incentives have been put in place to facilitate meeting alternative energy production goals.[95] Combined with production goals set by state legislatures, these policies describe a long-term commitment to the development of the wind industry. The L3C is then able to make use of the subsidies and incentives in much the same way that they are positioned to do at the national level.[96] Of course there must be a sense of stability associated with these incentives in order to raise the significant investment required to get sizable wind projects off the ground. These RPSs imply the necessary long-term state support.

A locally positioned L3C is also well suited to develop expertise within an individual state's regulatory regime. The complicated federal regulatory framework that governs the energy industry in conjunction with compliance with work in multiple states and offshore wind farms requires a high degree of sophistication. If an L3C is positioned as a local entity working in a community or individual state, the required expertise is narrowed to the locale. By reducing red tape and increasing familiarity with a place an L3C can fulfill the charitable goals of private foundations, make use of the dual level of state and federal incentives, and effectively engage and communicate within communities. Individual state action has created what is (hopefully) a stable market by creating incentives for local action in a manner that emphasizes the L3C's strengths and provides additional impetus for the L3C's use in facilitating the growth of wind energy.

Stabilization of the demand-side market also implicates the role of the L3C. Just as energy producers have sought consistent policy and government endorsement, end-users also seek consistent beneficial treatment in their use (or creation) of alternative energy.[97] An important part of this has been the institution of

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95. *See id.* at 1047 (discussing New York State's policy of exempting wind energy power systems from property tax for fifteen years); *Summary Maps*, DATABASE OF STATE INCENTIVES FOR RENEWABLES & EFFICIENCY, http://www.dsireusa.org/summarymaps/index.cfm?ee=1&RE=1 (last visited Jan. 2, 2013).

96. *See infra* Part III.D.

97. The role of inconsistent government support or subsidy on the alternative energy market has been described as "'the blade of a saw, rising and falling each time subsidies came and went.'" Neil Peretz, *Growing the Energy Efficiency Market Through Third-Party Financing*, 30 ENERGY L.J. 377, 384 (2009)

net-metering policies.[98] Net-metering requires utility companies to purchase back the energy produced from non-utility owned sources.[99] This allows consumers to contribute the energy they produce on their own (through their own wind energy producing turbines). The utility will only charge the consumer for the net amount of consumption.[100] As a community-based organization, this is a perfect place for L3C work. By engaging energy users directly the L3C can communicate, educate, and develop small scale projects that have the dual benefit of providing a decrease in energy expenses for the consumer and reaching the social and environmental goals of the organization. This work both increases the net amount of wind energy in the system while providing a benefit to consumers. This small-scale work is a way for the L3C to directly connect with the public about the increased role wind energy can play in powering their lives, while providing the consumer with a means of immediately reducing their energy costs.

State engagement in the alternative energy field, and more specifically wind energy, has provided the market space for the L3C to take advantage of state requirements and incentives in a way that larger scale utilities cannot. The L3C is also well suited to provide education and opportunity for individuals and communities looking to take advantage of demand-side incentives. If the L3C can take advantage of the myriad opportunities an individual state provides, wind energy's share of the market will grow and we will be closer to meeting environmental, social, and economic goals.

(quoting Joshua Green, *The Elusive Green Economy*, ATLANTIC, July/August 2009, http://www.theatlantic.com/magazine/archive/2009/07/the-elusive-green-economy/307554/). Peretz also discusses how an over-reliance on these national subsidies has led to far more severe fluctuations in investment than in some European and Asian countries. *Id.* The hard floors that many states have put in place in conjunction with the L3C's social entrepreneurship and flexibility may help to overcome this issue. Be it a product of scale or its socially driven nature, the L3C can take advantage of the state stability without having to rely as heavily on federal incentives (with fewer groups of investors seeking the credits and incentives generated by the L3C) *and* provide stability in the market itself by filling it. Additionally, as private foundations do not have to rely directly on the federal incentives as a result of their tax-exempt status, they may be better suited to riding the waves of changing federal policy.

98. Forty-three states, Washington D.C., and Puerto Rico have instituted net-metering policies. *See Net Metering*, DATABASE OF STATE INCENTIVES FOR RENEWABLES & EFFICIENCY, http://www.dsireusa.org/documents/summarymaps/net_metering_map.pdf (last visited Jan. 2, 2013).

99. Shoock, *supra* note 89, at 1047–48.

100. *Id.*

D. *Federal Policy: Development Through Tax Treatment and Incentives*

Federal engagement with wind energy production has been significant. In 2008 the Department of Energy and the National Renewable Energy Laboratory released a report that outlined how 20% of U.S. energy could be acquired through wind energy by 2030.[101] The Obama Administration, through the Department of the Interior Secretary Ken Salazar, has specifically endorsed this goal.[102] The Obama Administration has also focused on the use of public lands in the West as a means for growing wind energy infrastructure.[103] And while executive branch rhetoric has been important in bringing wind energy into the public discourse, it is congressional action that has had a larger impact on the growth of the wind energy sector.[104]

Congress has used two separate tax incentives, the Production Tax Credit (PTC) and the Modified Accelerated Cost Recovery System (MACRS), to facilitate the growth of the wind energy sector. The PTC and MACRS provide tax benefits to actors investing in the nation's alternative energy infrastructure. The ability of the L3C to take advantage of these incentives may help facilitate the growth of the wind energy industry. This section will discuss the nature of the tax incentives associated with the production of wind energy. We will then consider several financing mechanisms in order to demonstrate how the L3C will be an effective tool towards reaching the 20% by 2030 goal.

E. *Tax Incentives for Investing in Wind Energy*

Under the Energy Policy Act of 1992 and subsequent amendments, producers of wind energy receive a Production Tax Credit (PTC).[105] The PTC provides an inflation adjusted tax credit per kilowatt-hour of electricity produced, over a ten-year period.[106] The PTC has been a "key driver of wind power development" for a variety of reasons: it provides a discreet incentive for companies looking to develop a project, acts as a different financial benefit not tied to power prices, and indicates a federal

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101. U.S. Dep't of Energy, Energy Efficiency and Renewable Energy, 20% Wind Energy by 2030: Increasing Wind Energy's Contribution to U.S. Electricity Supply 7 (2008), *available at* http://www.nrel.gov/wind/systems integration/pdfs/2008/20_percent_wind.pdf.

102. Spengler, *supra* note 84, at 1207.

103. *Id.* at 1208.

104. *See supra* note 97 and accompanying text.

105. 26 U.S.C.A. § 45 (West 2010).

106. *Id.* at § 45(a).

commitment to the development of the industry.[107] The interplay between these tax incentives and tax-exempt private foundations is key to the L3C stimulating wind energy investment.

The use of the PTC as a tax incentive is most limited in that the credit has expired and been renewed several times over the last twenty years.[108] The current iteration of the PTC is set to expire on December 31, 2013; however, given the Obama Administration's continued focus on alternative energy and the history of renewal of the credit over the last two decades, there is a good chance the credit will be extended.[109] This credit has played an important role in the development of investments in these wind energy systems. Given the volume of tax benefits that the PTC provides, historically, small, single-purpose entities that are developing projects have looked for investors or buyers who could swallow the tax benefits.[110] This principle should still apply for investors interested in tax benefits with the L3C. If tax credits attributable to wind energy production made by the L3C can be transferred to investors through the operating agreement (given that private foundations do not need these credits), these PTCs are a significant incentive for investment through the L3C form.[111]

While the PTC provides an incentive for the production of wind energy, the MACRS allows for recovery of portions of investments made in wind projects. This is done through accelerated income tax deductions.[112] Under MACRS, wind projects may qualify for a five-year, 200% depreciation.[113] Included under this

107. JOHN P. HARPER ET AL., WIND PROJECT FINANCING STRUCTURES: A REVIEW & COMPARATIVE ANALYSIS 2 (2007).

108. *Id.*

109. *See* 26 U.S.C.A. § 45(d)(1).

110. HARPER ET AL., *supra* note 107, at 2.

111. *See* 9 MERTENS LAW OF FED. INCOME TAX'N § 35A:26 (2012) ("The provisions of the operating agreement determine the distributive shares of income, gain, loss, deduction, and credit."). Not all states will have an LLC statute, but most (or all) will have one governing LLPs; the flexibility of the operating agreements for both forms are similar. *See* 26 U.S.C. § 702(a)(7) (2010); 26 U.S.C. § 704(a) (2010) ("A partner's distributive share of . . . credit shall, except as otherwise provided in the chapter, be determined by the partnership agreement."); Stephen L. Nelson, *What's the Difference Between an LLC and LLP?*, LLCS EXPLAINED, http://www.llcsexplained.com/Whats-the-Difference-between-an-LLC-and-LLP.htm (last visited Jan. 2, 2013). Though assigning tax credits is not unique to the L3C, the fact that private foundations likely have no use for the credits means negotiation costs associated with distributing the credits can be avoided.

112. *See* 26 U.S.C.A. § 168 (West 2010).

113. HARPER ET AL., *supra* note 107, at 3. Harper describes the depreciation as a "double declining-balance depreciation." *Id.* This depreciation allow-

provision is equipment which uses wind energy to generate electricity, heat, or cooling in structures, turbines, generators, transfer equipment, and more.[114] On average, the depreciation is valued at approximately 26% of the total installed system cost.[115] This depreciation value can act as an incentive for investment or be passed on to consumers through lesser costs (without a significant impact on returns).[116] Use of the tax deductions in this fashion would address the dual purposes of the L3C. By developing an alternative energy source and passing it on to the consumer at a lower price the L3C will be serving environmental interests and increasing community wealth. The price of the energy developed in this fashion can be stabilized while ensuring competitive returns to equity investors when coupled with the L3C's flexible risk/return allocations. MACRS is an especially productive tool for use by the L3C.

These tax benefits provide the first layer of incentives for why the L3C would be an effective vehicle for facilitating growth in the wind energy sector. If the L3C is to work in capturing private foundation PRI, the tax credits and deductions associated with the PTCs and the MACRS provide a significant incentive for social entrepreneurs to invest. The flexibility of the L3C operating agreement in allocating risk and return, the private foundation's limited need for tax benefits, and the ability of a foundation to shoulder some of the costs of the initial investment mean that this may be far more attractive for an investor or a corporation than going it alone.[117]

F. *Financial Models for Wind Energy Investment.*

Financing structures for developing wind energy projects have grown commensurate in scope with the size of the industry.

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ance has the possibility of amounting to between 90–95% of the total costs for a wind project qualifying for the depreciation. This degree of recovery may also have a buoying effect for an L3C. Given that the L3C would be able to recover so much value for the property as a tax deduction, there are opportunities to pass the incentive on to investors in the L3C, or, if possible, in a self-sustaining model allowing for further investment in additional wind energy projects.

114. 26 U.S.C.A. § 48(a)(3) (West 2009).

115. Steven Ferrey, *The New Climate Metric: The Sustainable Corporation and Energy*, 46 WAKE FOREST L. REV. 383, 395 (2011).

116. *Id.*

117. The potential branding associated with the L3C would also have a role here. Given the recent focus on income disparity and corporate growth, institutional and significant private investors taking advantage of additional tax benefits might not sit well. However, the benefit of the L3C brand would allow an investor to show the public that its intentions lie beyond the mere production of wealth and acquisition of tax benefits.

While the complexity surrounding the financing of these projects has grown, and as bigger players have joined the fray, the flexibility and the socially driven mission of the L3C remains significant for a project of any scale. An analysis of some of the more typical financing schemes shows how the L3C would facilitate the growth of the wind energy industry. The level of sophistication that follows the investment of significant funds necessarily limits the breadth of this analysis, but this initial inquiry is at least demonstrative of the capability of the L3C to provide an effective vehicle for spurring investment.

Much of the early history of wind energy development in the U.S. was marked by investor reticence. Before 1999 the market considered wind energy to be too risky.[118] This led to smaller projects suffering from a difficult debt acquisition process.[119] The emergence of strategic investors as a driving force began around the first expiration of the PTC in 1999.[120] The financing model used by these strategic investors—which were largely utility-sized projects—involved internal funding. There were few debt financing opportunities.[121] In the early 2000s the expiration of the PTC contributed to a slowing pace of wind project development. Then in 2002 institutional investors began to engage the wind energy sector. These institutional investors sought a passive role in the management of the wind projects and could not necessarily make totally efficient use of tax benefits. However, they could finance the projects in a tax-efficient manner.[122] This period also saw the growth of debt financing of a portfolio of wind projects.[123] The growth in complexity of the financing models has coincided with a tremendous growth in project scale.[124]

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118. HARPER ET AL., *supra* note 107, at 5 ("[T]he financing community generally perceived the wind market as exotic, i.e., complex, small, and risky.").

119. *Id.*

120. *Id.* at 6–7.

121. *Id.*

122. *Id.* at 7–9.

123. *Id.* at 8.

124. Consider that the U.S. had a cumulative capacity of 11,575 MW at the end of 2006. *Id.* at 1. Five years later the U.S. has a cumulative wind capacity of 49,802 MW. *See Industry Statistics*, *supra* note 77. However, this growth must be balanced against the fact that U.S. wind power capacity is only 20% of the world's installed energy power; electricity production contributes about 25% of U.S. emissions of certain air pollutants. Ferrey, *supra* note 115, at 388–89. Given the scale of the U.S.'s open land and coasts, the country's interest in extricating itself from reliance on foreign energy, and the (relative) financial stability of the country, the smaller percentage of production capacity is difficult to reconcile.

The development of these financing structures has resulted in a multitude of opportunities for the L3C to help facilitate the growth of the wind energy sector. The current state of wind energy financing might allow for the L3C to act as a project investor or as an institutional investor in its own right (depending on the ability of the company to raise capital). At the most basic level the L3C could be free to follow what has been dubbed the "corporate" structure of financing.[125] In the corporate structure one entity acts as the single developer and investor, typically through the formation of a subsidiary. This type of structure provides the most flexibility. As a result of sole ownership, all cash flows and tax benefits return to the parent company.[126] This presents a powerful argument in favor of the L3C as a model for a wind energy developer. For a private foundation a smaller-scale project within a community would address environmental concerns and economic growth.[127] For social entrepreneurs there is an opportunity to address those same public benefit concerns while retaining profits and tax benefits with the private foundations swallowing much of the risk.[128]

Another financing model that engages the L3C's strengths is the "Strategic Investor Flip." Under this structure a strategic investor and developer would jointly own the project, sharing tax benefits and cash flows pro rata. However, the investor would make most of the initial capital contribution and would receive their corresponding returns based on their investment.[129] Then, once a negotiated point is hit (typically after ten years, corresponding with the end of the PTC benefits), the percentages

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125. HARPER ET AL., *supra* note 107, at 14.

126. *Id.* at 15.

127. This model does raise private benefit concerns. *See* 26 U.S.C. § 501(c)(3) (2010). However, in *Am. Campaign Acad. v. Comm'r*, 92 T.C. 1053, 1070 (1989), the tax court revoked the tax-exempt status of a school that taught campaign strategy because the school "conducted its educational activities with the partisan objective of benefiting Republican candidates and entities." That is, because nearly all of the school's graduates went on to work on campaigns for the Republican Party, the school was operated to support the Republican Party, and was conferring a private benefit. In the context of the L3C and wind energy investment, the benefit to the social entrepreneur would remain incidental to the overall operation. The private foundation would be serving a diverse set of public interests by investing in the wind energy systems rather than acting as a feedback loop for the social entrepreneurs investing in the projects.

128. This sole proprietorship type project necessarily requires a significant capital outlay. Focusing on the smaller scale project while using this structure would likely be more feasible, as well as more fitting considering the purpose of the L3C.

129. HARPER ET AL., *supra* note 107, at 18.

"flip" towards a more favorable allocation to the developer.[130] The project developer will often also have the right to purchase ownership interests from the investor as well. An L3C acting either as an investor or developer makes sense under this model. The L3C could be beneficial if this structure were employed as both an investor and as a project developer. If the L3C is well capitalized it could provide the initial investment to get smaller projects off the ground. Because the L3C would still be able to capture profits and the PTC benefits, private investors in the L3C would be satisfied. Further, given that the developer may have the ability to buy out the investor at the end of a defined period, the L3C may be free to extricate itself to reinvest in new projects. Finally, if an L3C utilized a portfolio approach to access debt it would simultaneously overcome one of the limitations of the not-for-profit world (accessing debt) and engage a much broader range of social issues. If the L3C were the developing entity, the L3C brand would also be an important asset. The strategic investor would be able to align with a socially beneficial company. The ability of the L3C to ultimately gain control of the project as a whole would also help the L3C remain a community-based institution that provides clean energy and jobs, rather than have the project become part of a conglomerate.

The L3C has significant potential as a vehicle for facilitating growth in the alternative energy sector. If the L3C is able to generate private foundation investment, the company will be able to offset the large amount of initial private capital investment and effectively distribute risk. Foundation investment in the L3C could lower cost of capital associated with entry into the wind energy market because of the risk distribution. As a result, the L3C would be able to charge more competitively for their power—allowing wind energy to better compete with fossil fuels. While the discussion of financing structure mechanisms was necessarily brief, the belief is that the descriptions that were provided demonstrate the applicability of the L3C to this sector. The goal of socially beneficial work that might drive an investor towards an L3C would be additionally buoyed by the tax benefits available from wind energy investment. While not carrying the same social cache as a not-for-profit, the L3C may help lessen tensions in a community reticent to accept the addition of wind power generation. While many questions remain as to how the L3C will develop as a legal entity, demonstrating the benefits of the form for different industries and projects should help to promote its adoption and acceptance.

130. *Id.*

III. Conclusion

Ultimately, the ability of the Low-Profit Limited Liability Company to act as an effective vehicle for the development of the wind energy industry is contingent upon its acceptance in the many states and by the federal government. With this acceptance, the L3C can have a significant role in meeting state and federal goals for wind energy production while providing environmental and economic benefits to local communities.

The L3C channels social entrepreneurship and financial goals. The model picks up the same ethical goals as the not-for-profit sector and adds the potential for providing economic benefits that the not-for-profit world cannot. With proper oversight the L3C can retain its "soul" while bringing new investors into the fold.[131]

The L3C is also positioned to take advantage of state and federal requirements and incentives. A flexible operational agreement and private foundation involvement allows private investors to take better advantage of state and federal incentives. The form also allows the L3C to retain the feel of a community-based association—which will help to overcome some of the 'Not-In-My-Backyard' problems. The L3C can also take some of the burden off of utilities who do not want to move to alternative energy systems.

Both federal and state governments have emphasized that developing wind energy is essential to U.S. energy independence and the growth of the alternative energy industry. The L3C form can provide an effective vehicle for the development of the wind energy industry by filling gaps the government and existing industry cannot or will not. Faced with the increasingly dissatisfying notion of the nation's reliance on fossil fuels, an innovative approach that makes use of the nation's sustainable resources is essential. The L3C form is able to capture investors interested in socially desirable projects, protect the environment, and bring jobs into communities – all this while making use of private foundation funds and further energizing the wind industry. The applicability of the L3C to this type of work will hopefully further inspire states to consider the benefits of the form while facilitating the growth of the wind energy sector in the U.S.

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131. Oversight should come from the private foundations, social entrepreneurs, and management structure of the L3Cs, who are vested and invested in developing a viable bridge between the for-profit and not-for-profit worlds. The IRS will also act as a backstop as it does with other not-for-profit type entities.