Low-Profit Limited Liability Companies (L3Cs): Competitiveness Implications

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EXECUTIVE SUMMARY

The low-profit limited liability company (L3C) is a new form of LLC designed to attract foundation funding for social enterprise. A review of the literature and case analysis of MOOMilkCo, L3C, LLC suggests that L3Cs are an appropriate and viable business structure for social entrepreneurial ventures. Despite the low-profit nature of L3Cs themselves, their creation generates profit-maximizing investment opportunities for suppliers and partners. While the full economic effects are not yet known, L3Cs appear likely to benefit society without limiting the free market's ability to benefit individual investors and the overall economy, if certain safeguards exist.

Keywords: L3C, Social Enterprise, Corporate Social Responsibility, Economic Effect

INTRODUCTION

In 2008, Vermont introduced a new form of business entity, the L3C, or Low-profit Limited Liability Company. Like a non-profit, an L3C aims to benefit society, but it operates as a for-profit limited liability company. Over 180 L3Cs have been formed (Americans for Community Development, 2010a), eight states have passed L3Cs legislation, and other states are exploring the concept. An example of an L3C is MOOMilkCo, which seeks to help small, organic dairy farmers in an economically depressed region by profitably processing and selling the farmers' milk.

An intentionally low-profit firm represents one spot on a continuum of profit seeking by organizations (see Figure). At one end of the spectrum are traditional companies that maximize profits (i.e., focus on financial benefits for owners). At the other end are nonprofit organizations (i.e., focus on social and environmental benefits for nonowners). In the middle are firms that accept corporate social responsibility (CSR) in that they focus on the financial interests of owners as well as social and environmental interests of everyone. Profit maximization and CSR are not mutually exclusive. Managing for the triple-bottom-line of financial, social, and environmental performance can be a strategy for long-term profitability (Porter and Kramer, 2006). Advocates note that CSR attracts customers and employees, lowers costs associated with energy use and waste disposal, reduces the risk of litigation linked to toxic material, and the like. On the other hand, CSR can go beyond profitable activities such as cause marketing and initial steps at energy efficiency to activities that decrease profits (e.g., aggressive steps toward carbon neutral operations). Profit limiting CSR practices are consistent with the view that corporate obligations arise from society granting the firm a license to operate (Graafland, 2002). When CSR goals clearly trump the goal of profit maximization, the organization is operating as a social enterprise. Social enterprises emphasize a social mission like nonprofits do, but they use market-based practices to fund that social mission. In contrast, a typical nonprofit organization relies on charitable donations to fund its social mission. L3Cs are part of the emerging social enterprise movement – they use the power of the marketplace to provide social benefits instead of maximum profits.

FIGURE: PROFIT SEEKING CONTINUUM

$$\begin{array}{c}\text{Traditional Firm}\\ \text{maximizing profits}\end{array} \rightarrow \underbrace{\begin{array}{c}\text{Triple Bottom Line Firm}\\ \text{pursuing profits}\end{array} \rightarrow \text{Social Enterprise (e.g., L3C)}}_{\text{Corporate Social Responsibility (CSR)}} \rightarrow \text{Traditional Nonprofit}$$

Raising capital is a challenge for social enterprises. One source of funding is charitable foundations. The U.S. Treasury and Internal Revenue Service (IRS) require foundations to distribute five percent of their assets each year to eligible charitable organizations and projects. Foundations usually do this by awarding grants, but they can make program-related investments (PRI) in the form of low-interest loans or equity investment, as long as the investment purpose is primarily charitable, educational, or the like, rather than the significant production of income or property appreciation. The charitable mission of nonprofits matches the charitable requirement of PRIs, so foundations are confident that the IRS will view nonprofit or 501(c)3 organizations as eligible PRI recipients. Foundations are much less confident of IRS interpretation when a PRI recipient is a for-profit entity. To be safe, a foundation can secure a private letter ruling from the IRS stating that a particular investment qualifies as a PRI, but the time and expense of obtaining a ruling are major barriers to foundation investment in for-profit social enterprises (Lang, 2009).

The L3C structure was specifically invented to help for-profit social enterprises attract foundation funding. State legislatures were encouraged to create the L3C structure to conform to federal PRI requirements (i.e., a social purpose with limited intention of generating profits), so that foundations could confidently invest in an L3C without obtaining an IRS private ruling letter. In reality, state legislation alone has not eliminated the barrier of the private letter ruling. The L3C designation is a signal to foundations (and the IRS) about low-profit intention and social orientation, but foundations will not be fully confident that the IRS interprets the L3C designation as conformance with PRI requirements until federal legislation or an IRS ruling declares it so. This raises the public policy question of whether or not the federal government should declare L3Cs to be eligible recipients of foundation PRI funding.

Foundations are not the only source of capital for low-profit limited liability companies. Investors committed to socially-responsible investment (SRI) often accept lower financial return from investments that benefit society. Despite sounding like a contradiction in terms, profit-maximizing investors might invest in a low-profit firm. While it is impossible for all L3C investors to expect a market rate of return, some can due to tranching or layering of risk. Foundation PRI capital can assume high risk in the venture for low expected return, allowing other tiers of investment to be safer and more profitable. Thus, the L3C structure can attract profit-maximizing investors even though the entity emphasizes social benefits.

Not everyone is enamored with the L3C form of business. The nonprofit community fears that L3Cs will compete with nonprofits for limited foundation funds. The more important question is whether nonprofits or L3Cs are better at benefiting society. A conservative radio commentator (Limbaugh, 2010) criticized the L3C concept as rewarding an unprofitable business because someone likes its social mission. He asserted that L3Cs pervert capitalism, corrupt the private sector, and change the mission of business. Progressives would respond that profit-limiting corporate social responsibility merely corrects price distortions caused by the market's failure to capture full costs – market price captures costs to owners, but not costs borne by society (e.g., legal emissions from smoke stacks can damage the health of those downwind without cost to the factory owner). Environmental economists would add that markets operating on full costs would offer greater net economic, social and environmental benefits than when the market operates on inaccurate prices.

To recap, an L3C is an LLC seeking to maximize social benefits and profits, rather than profits alone. The L3C structure was invented to increase foundation funding of social enterprise. Federal officials face the public policy decision of whether or not to declare L3C status a sufficient indicator of eligibility for foundation PRI funding. More broadly, the public policy question, at both the state and federal levels, is whether or not the L3C structure should be an accepted business form.

This paper seeks to inform public policy makers by exploring competitiveness implications of L3Cs. Specifically, the paper examines the effect of the L3C structure on 1) investor return and 2) the aggregate economy. Interpreting competitiveness broadly, the paper also examines social benefits provided by L3Cs given that 1) investment return for socially responsible investors includes the emotional utility of supporting social causes and 2) the ultimate purpose of a competitive economy is to improve quality of life. The economic and societal effects of L3Cs are explored by reviewing the academic literature and examining the case study of MOOMilkCo, L3C, LLC.

LITERATURE REVIEW

Articles about L3C law and taxation have been published (c.f., Americans for Community Development, 2010b), but L3C has received scant attention in the management literature. Clement, Lang and Jatar (2010) explain the concept, and others mention L3Cs briefly (c.f., Isaac and Norton, 2010). The literature does address the broader topic of CSR/social enterprise and its relation to competitiveness (Vilanova, Lozano, & Arenas, 2009). Windsor's (2006) review of the CSR literature concluded that partly-conflicting research streams drawing on different disciplines have yet to produce theoretical syntheses.

To make sense of the literature, it is crucial to distinguish CSR activities intended to maximize shareholder value from those profit-limiting activities that stem from a strong sense of responsibility to benefit society. In this paper, the former – what economist Milton Friedman might call 'prudent altruism' (Windsor, 2006) – will be thought of as conservative CSR. The latter will be called voluntary CSR.

Neoclassical economists view voluntary CSR as inappropriate. Milton Friedman (1970) noted that corporate charitable donations – and by extension, other voluntary CSR activities – involve managers acting as agents for shareholders. He argued that corporate donations are an imperfect substitute for how individuals would personally contribute to social causes if their investment returns had not been reduced by CSR activities. Likewise, investors are thought to get less emotional satisfaction when charitable donations are made through an impersonal corporate intermediary as when the individual personally donates. CSR advocates respond that investors get what they want, despite intermediate managers making CSR decisions, because the investor chose not to invest in a profit-maximizing firm, which would allow for a separate personal donation (Besley & Ghatak, 2007). Why might an investor prefer a voluntary CSR firm? Corporate donations avoid double taxation of dividends and may be perceived as having fewer transaction costs than time-consuming personal donations, which themselves tend to be inefficient when they go through an intermediary nonprofit organization (Baron, 2007). From a societal perspective, it may be more efficient for firms to use CSR to reduce their external costs (e.g., greenhouse gas emissions) than for nonprofit organizations or government to fix resulting problems after-the-fact.

Neoclassical economists argue that firms should focus solely on profit maximization because the pursuit of actor self-interest is what enables Adam Smith's "invisible hand" to best serve the general welfare. The idea is that profit maximization by firms leads to the most efficient allocation of resources, which benefits the economy in aggregate, which benefits the public good by raising individual incomes and tax revenue, which in turn can be used to enhance the public good. Neoclassical economics does include a role for managerial ethics. Adam Smith accepted moral rules and saw a role for business managers as "impersonal spectators" who objectively evaluate and consider the circumstances of neighbors and the public interest (Windsor, 2006). For Friedman, profit maximization activity is to be constrained by ethical customs in the form of laws and social norms. One could view moral rules and social norms as ways to offset market distortion caused by imperfect information in the real world. With perfect information, prices would factor in the full cost of operations, including social harm or external costs borne by society.

Many neoclassicists narrowly interpret ethical customs to mean taboo behavior like fraud and deception. A broader interpretation of ethical customs is part of the revived economic perspective proposed by Jensen, McWilliams, and Siegel (c.f., Windsor, 2006); this perspective is grounded in neoclassical theory, but more broadly interprets ethical customs to include emerging social and environmental standards (e.g., standards driving shareholder activism and the sustainable consumer movement). Consider the CSR issue of sweatshop labor. Profit motivation alone inhibits the use of abusive labor practices by mega-brands that rely on reputation for commercial success. In contrast, an unknown brand competing solely on price lacks a profit motivation to avoid sweatshops. At what point should this type of firm conclude that ethical customs prohibit sweatshop labor? When the majority of people disapprove of sweatshops? When 99% of people disapprove? Or never because government regulation should establish when a ban is appropriate?

While neoclassical theory might seem to proscribe voluntary CSR, Baron (2007) argues that Friedman's objection is not to CSR per se, but to shareholder harm caused by CSR activities (i.e., the cost of voluntary CSR is a management-imposed tax on shareholders, but taxation for the common good is the sole purview of democratically-elected public officials). Baron argues that shareholders only bear the cost of voluntary CSR when it is unanticipated. To understand this point, consider a shareholder in a profit-maximizing firm, who is surprised when the firm adopts voluntary CSR. By definition, shareholder value falls. The surprised investor is harmed. Shares are now likely to be bought by socially-responsible investors. Of course committed SRI investors – like the entrepreneurs who create social enterprises – knowingly and willingly accept lower economic return to obtain satisfaction from their enterprise's contribution to society; the total utility received from their investment is not lower. Thus, Baron contends, only surprised investors are hurt by a voluntary CSR orientation. Applying Baron's logic, an L3C is compatible with the neoclassical model because there are no surprises – the CSR orientation is known from the L3C's inception. A neoclassical purist might counter that even without harm to L3C investors, overall market performance and collective societal welfare could suffer due to inefficient allocation of resources. The literature does not provide insight into how the L3C structure might cause this inefficient allocation of resources.

The discussion above examines economic benefits. What about the provision of social benefits for the public good? The persistence of social ills such as poverty, communicable diseases, and environmental degradation has fueled the social enterprise movement and led to calls for "new designs of economic institutions that can provide a stable source of capital for provision of the public good" (Isaac and Norton, 2010). Researchers who compared for-profit social enterprise to the nonprofit sector concluded that social enterprise is more efficient at public good provision than nonprofits when the public good is inherent in the production of the private good (Besley & Ghatak, 2007). Others argue that a conclusion cannot be reached because empirical results are not theoretically understood (Francois & Vlassopoulos, 2008) and accounting methods cannot adequately measure the social value provided by an entity (Quarter & Richmond, 2001).

Robert Lang, a developer of the L3C concept, offers a variety of reasons why L3Cs are valuable in the marketplace (Lang, 2009). To sustain delivery of social benefits, nonprofits require ongoing charitable donations, whereas L3Cs might only need one-time start-up funding since ongoing market operations can support the ongoing delivery of benefits. Leverage also plays a role: when foundation PRI funding absorbs investment risk, profit-maximizing investors may also invest, which inadvertently increases the total funds directed toward the delivery of social benefits. Despite the nonprofit community's fear that foundation funding of L3C's will cannibalize grants to nonprofit organizations, PRI funding of L3Cs may increase future funds available to nonprofits because repayment of PRIs increases endowment size over what it would have been if earlier PRI funds had been dispersed as a grant. L3Cs also put people to work in living-wage jobs, thus reducing their need for charitable handouts, freeing up charitable funds for other needs. In summary, L3Cs could increase the total amount of resources directed toward the public good due to self-sustaining operations, repayment of PRI foundation funds, and leverage with profit-seeking investment.

In conclusion, the literature does not provide clear guidance on whether or not public policy should encourage L3C creation and PRI funding of L3Cs. In terms of economic issues, Baron's arguments suggest that investors will not be harmed by an L3C's CSR orientation. Less clear is whether the L3Cs have unintended consequences for the overall economy. In terms of societal benefit, Lang's work suggests that L3Cs will increase the total amount of funding directed to the delivery of social benefits, and Besley and Ghatak suggest that L3Cs provide social benefits more efficiently than nonprofits. To explore these issues further, the remainder of the paper examines the case of MOOMilkCo.

THE CASE OF MOOMILKCO, L3C, LLC

In 2009, H. P. Hood Company, a Massachusetts milk processor, ended its contracts to buy organic milk from ten, small, dairy farms in northern Maine. The farmers were left without a buyer. Hood's actions illustrate a profit-maximization strategy. Hood lowered its production costs by buying lower-priced organic milk from large dairies that minimized use of grazing pasture and were located closer to Hood's New York processing facility. Thus, Hood continues to provide social benefits inherent with organic milk (i.e., fewer ecological impacts and greater farm worker safety), but stopped providing other social benefits to increase profits (i.e., no longer supporting scenic open space and family farms in economically distressed communities). A neoclassical argument can be made that Hood's change in suppliers was best for consumer prices and the U.S. economy in aggregate, but that is little comfort for Maine's farmers, communities, and economic planners.

The U.S. dairy industry has experienced unprecedented economic upheaval. Milk processor consolidation increased monopsony power in which dominant buyers force farmers to accept prices below that of a competitive market. Milk prices have fluctuated dramatically, with dairy farmers receiving the lowest wholesale prices in decades even though consumers paid high retail prices (Varney, 2009). Not surprisingly, 200 of Maine's 500 dairy farms failed in the last decade (Mack, 2010). Given this background, prospects for the ten Maine dairy farmers were grim. They could sell their organic milk at conventional milk prices, but the lower price would not cover the cost of organic production and would not sustain a reasonable livelihood even with a switch to conventional milk production. Essentially, small family farms using open-pasture agricultural practices to produce milk for the commodity market – either conventional or organic – was no longer a viable business model in northern Maine. The loss of the livelihood for farmers and their local milk hauler would have a negative ripple effect on the local communities in this economically disadvantaged region.

The Maine community – trade groups, consultants, state government – came to the farmers' rescue with a plan to create a new brand, MOOMilk, Maine's Own Organic Milk. The new brand was expected to successfully compete in the marketplace, despite a high retail price, by appealing to consumers who value local as well as organic products. The farmers retained ownership of their farms, and MOOMilkCo was created as an L3C to buy the farmers' milk and then market it as MOOMilk. The social purpose of this low-profit limited liability company is to preserve family farms, foster organic production, and contribute to the economic viability of a poor region. In terms of ownership, 45% of MOOMilkCo is owned by the farmers, who are guaranteed 90% of the profits. Investors and foundations will own 45% once $1 million has been raised. The remainder is for future employees or belongs to those who provided labor to launch the venture.

Start-up capital included a $50,000 foundation grant, about $32,000 from the farmers, and $375,000 from private SRI investors who were not expecting a market rate of return. There is no PRI funding because MOOMilk only recently began to solicit $500,000 in PRI funding and federal government action has not yet eliminated the barrier of an IRS private letter ruling. Without PRI funding, MOOMilk has not been in a position for tranching to attract market-rate investors. Insufficient capital caused a cash flow crisis, which was overcome with $100,000 in donations from local philanthropists. On the positive side, MOOMilkCo went from concept to production in less than a year, most of its planned product line has rolled out, and it is on track to be profitable in early 2011.

A successful venture will benefit the entire state by generating tax revenue: thirty farm jobs will be saved, five jobs related to in-state milk processing will be generated, and revenue will increase for in-state subcontractors that process and distribute the milk. The subcontractors invested $375,000 in their existing operations to create MOOMilk's in-state supply chain.

ANALYSIS AND DISCUSSION

What light does the MOOMilkCo, L3C case shed on the competitiveness-related issues of firm-level investor return, aggregate economic performance, and delivery of social benefits? What are the implications for public policy?

Investor Return

Current and future investors in the MOOMilk case range from farmers and SRI investors to profit-maximizing cash investors (including supply chain partners), professional service providers exchanging labor for equity, and foundations with PRI funds. The true motivations of investors are unknown, but educated guesses can be made. All investors knew from the outset that MOOMilkCo was a low-profit LLC with a social mission that would constrain profit-maximizing options (e.g., no lowering of costs by switching milk suppliers or eliminating pastures).

The farmers invested a small amount of cash and committed their milk production to the venture, thus incurring the opportunity cost of alternate income from their farm assets. The investment goal may have been profit making combined with lifestyle maintenance, but farmer actions were consistent with profit maximization. Except for one farm that opted to produce its own cheese instead of participating with MOOMilk, the farmers viewed the L3C as the best economic option.

The two supply chain partners that made internal investments would not have done so without an expectation of a successful launch by MOOMilkCo. The owners of these local, family-owned firms care about the community but also believe triple-bottom-line management leads to long-term profitability. Their MOOMilk-related investments were attractive because the partners were able to increase existing asset utilization or improve their own supply chains. A profit maximization motive would arguably have led the firms to make the same investments. Even if some level of voluntary CSR motivation was operative, this was the choice of the owners, so nothing was imposed on hapless shareholders.

PRI foundation funding has not yet been obtained, so tranching has not been possible to attract profit-maximizing cash investors. The investors who have supplied funds or time appear to be SRI-investors willing to risk a below-market return in exchange for the satisfaction received by supporting the social benefits of farm preservation, organic production, and rural economic development. Consistent with Baron's previously discussed logic, the replacement of financial return with emotional return was the choice of the SRI investors; nothing was imposed or unanticipated; no one was harmed. What would happen if management expanded MOOMilkCo's voluntary CSR activities beyond the current level? Lower future profits would not be a problem for MOOMilkCo investors; they can sell their ownership stake back to MOOMilkCo for

105% of what they invested. Without the prearranged sale price, Friedman's concern would apply. SRI investors surprised by an L3C's shift from a low-profit orientation to a super low-profit orientation would be harmed by having lower expected returns than what they agreed to when they invested.

The L3C structure was invented to foster PRI funding for social enterprise. Since MOOMilkCo is on track for profitability without PRI funding, one might wonder if the L3C structure served any purpose at all. Yes, it did. The L3C designation is a signal of MOOMilkCo's unique features. The signal highlighted the potential for risk-absorbing PRI funding, making it easier to attract private investors. MOOMilkCo's social mission was also highlighted by the signal, making it easier to attract its SRI investors, start-up foundation grant, private donations, and media attention, which in turn helped sales. In conclusion, the L3C designation is a signal that benefits investors because it decreases the likelihood that insufficient start-up capital will cause the firm to fail. Moreover, the signal adds to investor protection in that it reduces the likelihood that investors will be surprised by an L3C's low-profit orientation.

If the L3C concept fails to foster PRI funding, so L3C status only serves as a signal of voluntary CSR, other designations may be better. Two states have created Benefit Corporations or B-Corps for firms engaged in voluntary CSR. B-Corps, like L3Cs, combine the goal of profits with social and environmental goals. Unlike L3Cs, B-Corps lack the low-profit constraint. Thus, B-Corps are likely to be more attractive to SRI investors seeking higher rates of returns. A major concern about L3C and B-Corp structures is that there is currently little oversight over the firm's ongoing delivery of social benefits. A nongovernmental organization, B-lab, certifies individual businesses as meeting comprehensive standards of social and environmental performance. B-lab's certification provides a level of accountability that is currently missing with L3Cs, and thus may be a better CSR signal for consumers and SRI investors than L3C or B-Corp structures alone.

The empirical evidence provided by the MOOMilkCo case is generally consistent with Baron's contention that newly formed social enterprises do not harm investors. However, a surprised investor could be harmed when an existing LLC switches to L3C status, lowering expected returns and shareholder value. A public policy solution would be to allow LLC conversion to L3C status only when all LLC investors agree. Our analysis also revealed that initial L3C investors could be surprised and harmed if management subsequently expands voluntary CSR efforts. A pre-set selling price prevents possible harm. Finally, the MOOMilkCo's case demonstrates that L3C creation leads to investments expected to have market rate returns (i.e., farm assets) or comparable ones (e.g., equal utility for SRI investors). Just because L3Cs are low-profit entities doesn't mean suboptimal benefit for investors.

Aggregate Economic Effects

What are the effects of L3Cs on the overall economy and its ability to improve living standards? At first glance, one might think that a profit-maximizing firm would always add more to the economy than a low-profit firm. In the MOOMilkCo case, however, a profit-maximizing firm was not an option. Exiting profit-maximizing milk processors were not interested in buying the milk, venture capitalists were not interested in creating a new profit-maximizing firm to fill the void, and farmers did not see other economically-viable uses for their farm assets. For Maine's economy, a low profit firm was clearly superior to nonprofits. It's true that the SRI investors are likely to receive a lower economic return, but the existence of SRI funds and charitable grants have created profit-maximizing economic opportunities that would otherwise not exist (i.e., business expansion and job creation with supply chain partners, including farmers, and professional service providers). In conclusion, MOOMilkCo's direct effect on the economy appears to be helping rather than hurting the Maine economy. L3Cs clearly play a role in economic development, especially in economically distressed areas.

A case study looking at one firm in its infancy is unlikely to uncover the full range of effects on the aggregate economy. It's not clear, for example, the extent to which MOOMilkCo will affect the economic prospects of for-profit firms selling milk. Some insight into aggregate economic effects can be gained by considering the abstract scenario of the many L3Cs being launched. As L3Cs emerge, competition would intensify for foundation funds and SRI funds (and profit-seeking funds if tranching occurs). Likewise, an increase in L3Cs would intensify competition in the consumer marketplace, especially for products targeting the niche market of sustainability-oriented consumers. Increased competition for funding and consumers would lead to failure for less competitive firms, both L3Cs and profit maximizing firms. In short, the market would self-regulate the number and quality of L3C firms. One might ask if an L3C's ability to attract below-market-rate funding provides an unfair advantage over traditional firms. This might be true if tax subsidies were associated with L3Cs, but tax subsidies do not play a significant role: private donations to L3Cs are not tax deductable and L3Cs are taxed in the same way as regular LLCs. It's true that an L3C is more likely to receive foundation grants and PRI funds, as well as private SRI investment, but those funders could choose to direct their funds to profit-maximizing firms if they so chose. In conclusion, L3Cs represent a new type of competitor in the marketplace and is thus part of the competition for funding and consumers. This is not unfair to traditional firms because the competition is driven by the free choice of informed funders and consumers.

Another possible outcome of an increase of L3Cs in the marketplace is that their mere existence and their promotional messages may foster cultural change. Mainstream consumers could come to believe that all firms should engage in voluntary CSR. Evolving consumer expectations have already caused firms to begin managing for the triple bottom line (Windsor, 2006). If the emergence of L3Cs further shifts consumer expectations, profit-maximizing firms will engage in more activities that were once considered voluntary CSR simply to attract consumers or meet stricter regulations driven by heightened citizen expectations. Since CSR activities provide social benefits and reduce environmental harm, a rise in these activities would contribute to quality of life, which is the ultimate goal of the economy. On the other hand, an across-the-board rise in voluntary CSR means that individuals whose expectations lag the mainstream will pay more for products and receive lower investment returns. Similarly, U.S. products would be less competitive in foreign markets that have not experienced a similar shift in consumer expectations. To the extent that this scenario plays out, it is neither good nor bad because it was driven by consumer expectations and the economic principle of consumer sovereignty.

In summary, there is always a risk of unintended negative effects on the economy, but no specific L3C effects were identified in the literature or the MOOMilkCo case study. We examined the possibility of L3Cs becoming a dominant form of business, and conclude that the market would self-regulate the number of L3Cs and that any economic effect of changing cultural norms would appropriately be driven by consumer sovereignty.

Provision of the Public Good

MOOMilkCo provides social benefits. Family farms have been preserved. Organic dairy production and agricultural open space has been maintained. The ripple effect of job creation and tax revenue helps the entire state. These social benefits are partially attributable to donations and grants received by MOOMilkCo. Would the public good have been better served if the funds went to a nonprofit organization? If MOOMilkCo fails, a nonprofit would likely have provided a better outcome, although a one-time donation of the amount received by MOOMilkCo would not help a nonprofit accomplish much in the way of farm preservation, organic dairy production, or economic development. A successful MOOMilkCo, on the other hand, would accomplish much more over time than a one-time donation to a nonprofit. And, if the foundation had supplied PRI funds instead of a start-up grant, MOOMilkCo would eventually repay the foundation and those funds could be redistributed to produce even more public good.

A neoclassical objection to CSR is that managers rather than owners (or democratically-elected officials) decide which social issues to support. MOOMilkCo donors, or their foundations, chose to support an L3C rather than a nonprofit. In keeping with free market principles, this suggests that this L3C was expected to be better at generating social benefits than nonprofits. If donors believe that L3Cs in general are more effective than nonprofits, the emergence of L3Cs may encourage donors to donate a larger percentage of their wealth for the public good. Regardless of whether or not L3Cs increase the amount money directed toward charitable causes over time, the MOOMilkCo case indicates that L3C creation diverts money from nonprofit organizations, at least in the short term. This diversion is appropriate given donor sovereignty.

CONCLUSION

Public officials must decide if the Low-profit Limited Liability Company is an appropriate business structure and, if so, if L3Cs should be pre-approved as meeting PRI eligibility requirements. While the full ramifications of the L3C structure are unknown, our analysis of competitiveness issues in the literature and in the MOOMilkCo case supports L3C creation and funding. However, if investors are to be economically protected from an unanticipated expansion of voluntary CSR, then 1) no LLC should be allowed to convert to an L3C unless all LLC members approve and 2) a sales price for L3C equity must be pre-established.

Our conclusion about the attractiveness of the L3C structure is, of course, tentative. There was little academic literature on L3Cs to draw upon, and the broader CSR literature has conflicting views. Our case study has sample of one firm, so generalization to all L3Cs is inappropriate. Moreover, this paper focused on aspects of competitiveness, and largely ignored other issues of interest to public policy makers such as taxation, accountability, and legal matters. That said, this paper makes a contribution to the literature by being the first academic paper to examine the effects of the L3C structure on investors, the overall economy, and provision of social benefits enhancing quality of life. We call for future research on L3Cs, especially research drawing on empirical data and economic modeling. Research might consider how offering an L3C designation might improve state level competitiveness in terms of fostering entrepreneurial ventures, attracting foundation funding to the state, and raising fee revenue. Another area for research would be analysis of L3Cs using well known theoretical frameworks such as resource-based perspectives and stakeholder theory. A final suggestion is to investigate the relative effectiveness of alternative indicators of a firm's commitment to CSR (e.g., B-Corp).

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