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TomVreeman, CEO and executive director of Kandu Inc., is shown outside the clean room environment the company uses for medical device purposes.

Kandu uses new L3C law to pursue medical devices

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Class 10,000 clean room? Check. ISO certification? Check. Federal Food and Drug Administration approval? Check.

New type of business model? Yeah, that, too.

Ottawa County nonprofit Kandu Inc. has used an L3C, a new nonprofit/for-profit business hybrid in Michigan, to expand its program of jobs for those with disabilities into the medical device industry.

"It's very unique," said TomVreeman, CEO and executive director of Kandu, 4190 Sunnyside Drive, Holland.

"I think it's going to be a model that's pretty intriguing. It's opened up a whole new field, both for training people to work in a clean room environment doing assembly for high-tech firms, and be a funding source, as well. I know people in my industry have been pretty interested in seeing how we work this out."

In January, Gov. Jennifer Granholm signed a law making Michigan the second state to allow the L3C, or low-profit limited liability company, for charitable or educational purposes. An L3C may have profits that are returned to investors, but income and capital gains must be secondary to educational or charitable purposes.

Michigan Council of Foundations President and CEO Rob Collier said the advantage lies in the ability of for-profit

businesses to join forces with foundations in an L3C for economic development.

"I have received calls from a number of law firms who are interested in this concept," said Collier, who has championed laws to establish L3Cs in Lansing and in Washington, D.C. "I do believe the interest is there."

But foundations are on the sidelines until the Internal Revenue Service decides whether an L3C can qualify as a program-related investment, said Duane Tarnacki, a lawyer in Clark Hill's Detroit office who specializes in tax-exempt organizations.

In a PRI, a foundation may invest in a for-profit company, often through a low-rate loan or similar arrangement, for the purpose of societal benefit. IRS rules govern the process for foundations, and L3C laws now on the books in four states have been written to be compatible.

But Tarnacki said the IRS is moving slowly toward providing a regulatory framework for a national L3C law.

"In order to complete the picture, the IRS has to issue some kind of revenue ruling or some pronouncement that sanctions the use of L3Cs from a federal tax standpoint to optimize their use," Tarnacki said. "The Council on Foundations in Washington is working on that, trying to get some legislation passed where Congress would order the IRS to approve L3Cs or working with the IRS directly."

Tarnacki said the state law currently is useful when one nonprofit is the sole member of the L3C — as is the case for Kandu, which wholly owns its L3C medical device subsidiary — or perhaps two nonprofits are involved.

Since January, 21 entities have been registered as L3Cs in Michigan and eight are pending, according to the state Department of Energy, Labor and Economic Growth's Web site. Four of those have been in West Michigan.

"I have no idea of what the benefits are of being an L3C rather than an LLC. We were told to," said Brian Vork, executive director of 70 Times 7 Life Recovery, a two-year-old nonprofit at 97 W. 22nd St. in Holland.

When 70 Times 7 went to file the paperwork in Lansing, Vork said state officials thought the venture should become an L3C, a low-profit limited liability company.

"It was confusing. It worked out, but you never want to be first of anything going through a new process," he said.

Earlier this year, 70 Times 7 established New Day Construction to employ and teach new skills to people leaving incarceration. Vork said New Day Construction employs three men after just a few months of operation.

Another is SBNR, which stands for Spiritual But Not Religious. It is a project of Australian-born Ian Lawton, executive minister at Christ Community Church, 225 E. Exchange St., Spring Lake, and Brad VanderArk, former bass player for The Verve Pipe.

Lawton said the organization's aim is to reach people through social networking and inspire them to establish SBNR communities of their own.

"We have big ambitions in terms of building a lot of local SBNR communities," Lawton said. "It's more like a franchise model in which we give people the tools and the resources."

For 55 years, Kandu has provided training and jobs for people with disabilities. A \$10 million nonprofit organization that reported to the IRS a \$755,312 loss for the 2008 tax year, Kandu employs 250 people to fulfill contracts with businesses, mostly for assembly and packaging, Vreeman said. Kandu also has a work force development contract with Michigan Works.

"A year and a half ago, we decided to diversify the types of work we provide and looked at the medical device industry, since we're mainly involved in light manufacturing," Vreeman said. "We had the opportunity to put together a clean room environment, and we're getting our ISO certification and FDA certification to manufacture

and assemble medical devices. It's a year-long process to go through that.

"We had a potential customer with a new product and we had a couple of other potential customers with development products," he said. "We felt we needed a different business model."

Vreeman said the L3C allows KI Medical Manufacturing to enter into reciprocal relationships with customers without entangling the long-standing nonprofit, he said. KI-Med contracts with Kandu for labor.

"Industry-wise, it's a nice size of company for doing contract medical device manufacturing," he said. "There are not a lot of companies around that contract around."

KI-Med has three customers: one local and two from out-of-state. Should they reap profits, Kandu would then be buoyed by a new revenue stream, he added.