

SENATE COMMERCE COMMITTEE

STATEMENT TO

SENATE, No. 742

with committee amendments

STATE OF NEW JERSEY

DATED: FEBRUARY 9, 2012

The Senate Commerce Committee reports favorably and with committee amendments Senate Bill No. 742.

This bill, the "Revised Uniform Limited Liability Company Act," repeals the "New Jersey Limited Liability Company Act," and replaces it with a more modern regulatory scheme for the creation and operation of limited liability companies in New Jersey.

The limited liability company (LLC) is a relatively new form of unincorporated business organization that provides corporate-style limited liability to its owners, while affording the owners the partnership-like capacity to structure the entity by agreement rather than as prescribed by statute. LLCs began to be widely used after IRS Revenue Ruling 88-76 upheld the taxation of LLCs as partnerships. If the LLC elects to be taxed as a partnership, the LLC does not pay federal income tax on its profits. Rather, its members are taxed on their share of the LLC's income. As a result, LLCs have become the business entity form of choice for new businesses, and far more New Jersey LLCs have been formed in recent years than corporations and limited partnerships combined.

The "Revised Uniform Limited Liability Company Act" (RULLCA), as developed by the National Conference of Commissioners on Uniform State Laws (NCCUSL), is a significant advancement in this area of the law. It is a comprehensive, fully integrated "second generation" LLC statute that takes into account the best elements of "first generation" LLC statutes (such as the "New Jersey Limited Liability Company Act" (NJLLCA), which was enacted in 1993 and became effective on January 26, 1994) and two decades of legal developments in the field. Similar to the Revised Uniform Partnership Act (RUPA), RULLCA is largely a series of "default rules" that govern the relations among the members in situations they have not addressed in their operating agreement. Under RULLCA, express provisions of the operating agreement prevail over most statutory norms.

RULLCA's structure is similar to RUPA's. Article 1 (General Provisions) contains general provisions, including definitions; Article 2 (Formation; Certificate of Formation and Other Filings) provides for

the formation of LLCs and for the filing of the appropriate documents with the Division of Revenue in the Department of the Treasury; Article 3 (Relations of Members and Managers to Persons Dealing with Limited Liability Company) governs the relations of members and managers to third parties; Article 4 (Relations of Members to Each Other and to Limited Liability Company) provides the default rules for the members' relationships with each other and with the LLC; Article 5 (Transferable Interests and Rights of Transferees and Creditors) reiterates the "pick your partner" concept that is fundamental to LLCs and sets forth the rights of transferees; Article 6 (Member's Power to Dissociate; Wrongful Dissociation) delineates the causes and consequences of an owner's dissociation from the LLC; Article 7 (Dissolution and Winding Up) sets forth the events for dissolution and liquidation of the LLC; Article 8 (Foreign Limited Liability Companies) governs foreign LLCs; Article 9 (Actions by Members) provides for direct and derivative actions by members of an LLC; Article 10 (Merger, Conversion and Domestication) governs domestication, conversion and merger transactions; Article 11 (Miscellaneous Provisions) includes several miscellaneous provisions, including transition rules for existing LLCs.

Here are some of the more significant changes and innovations in RULLCA as compared to NJLLCA:

- Perpetual duration. RULLCA eliminates the default (and often overlooked) rule that LLCs have a limited life. As is the case with corporations, RULLCA provides for LLCs to have perpetual duration.
- Permissible form of operating agreement. RULLCA permits operating agreements to be oral, written or implied based on the way an LLC has operated. This is consistent with the vast majority of states and in line with the organization of many LLCs formed in New Jersey.
- Distributions. Consistent with RUPA, unless otherwise agreed, distributions are made on a per capita basis.
- Statements of authority. As is the case under RUPA, RULLCA allows an LLC to file statements of authority with the Division of Revenue in the Department of the Treasury (and in the case of real estate, in the office where real estate records are maintained) authorizing certain people or entities to bind the LLC.
- Dissociation of a member. RULLCA eliminates a major pitfall for the unwary practitioner or layperson forming an LLC in New Jersey. Under RULLCA, a resigning owner is no longer entitled to receive the fair value of his or her LLC interest as of the date of resignation. Rather, upon resignation, the resigning owner is dissociated as a member and only has the rights of an economic interest holder.

- Remedies for deadlock and oppression. Reflecting case law developments around the country and incorporating some of the best elements of the New Jersey Business Corporation Act, Article 7 (Dissolution and Winding Up) of RULLCA provides remedies for oppressed minority owners. RULLCA permits a member to seek a court order dissolving the company on the grounds that the managers or those members in control of the company have acted or are acting in a manner that is oppressive and was, is, or will be directly harmful to the member. RULLCA also permits a member to seek (or, in its equitable discretion, a court to order in lieu of dissolution) a less drastic remedy, such as the appointment of a custodian.
- Domestication and conversion. RULLCA provides enhanced ease and flexibility for domesticating, merging and converting an entity other than a domestic limited liability company, if permitted by the law under which it was formed. Its comprehensive provisions offer streamlined methods for domestication (*e.g.*, allowing an LLC formed under the laws of another state to become a New Jersey LLC) and conversion (*e.g.*, allowing a corporation to become an LLC).

This bill will become effective 180 days after enactment, and will govern all LLCs formed after its effective date. Following the first day of the 18th month following this bill's enactment, it will apply to all New Jersey LLCs, whenever formed.

This bill was pre-filed for introduction in the 2012-2013 session pending technical review. As reported, the bill includes the changes required by technical review, which has been performed.

Committee Amendments:

The committee amendments to the bill:

- 1) add a new subsection to section 11, mirroring language in current law at N.J.S.A.42:2B-66 to provide that the act is to be liberally construed to give the maximum effect to the principle of freedom of contract and to the enforceability of LLC operating agreements;
- 2) require, in section 14, a foreign limited liability company that has a certificate of authority under section 58 of the bill to designate and continuously maintain in this State an office and an agent for service of process, rather than just an agent;
- 3) establish, in section 15, a procedure for a registered agent to change the address of the registered office of any domestic or foreign limited liability company for which the registered agent is registered agent and to change the name of any person acting as a registered agent;
- 4) require, in section 18, a certificate of formation to contain the street and mailing addresses of the initial registered office and the

name of the initial agent at that office for service of process of the company;

5) revise references (in sections 25, 26, 60, and 62) to “certificate of registration,” “certificate of standing,” and “certificate of authority,” as appropriate;

6) delete, in section 38, the definition for “serving at the request of the indemnifying company”;

7) in section 58, clarify that before doing business in the State, a foreign limited liability company must obtain a certificate of authority to transact business in this State and must promptly correct any false information on the application for a certificate of authority;

8) add to section 66, language mirroring current law at subsection d. of N.J.S.A. 42:2B-57 providing for a fine of \$200 for each year or part thereof during which a foreign limited liability company does business in the State without first obtaining a certificate of authority;

9) amend section 82 concerning domestication; and

10) make technical corrections to correct internal references and to make certain other provisions permissive, rather than directive.