**Selecting the Proper Corporate Entity for New Businesses**

**Presentation to myLawCLE**

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**I. Choice of Business Entity**

1. Sole Proprietorship – business owned and run by one person; not a separate legal entity

i) Advantages

a) Easy to form; no formation documents to file

b) Inexpensive – no organizational documents, so no legal fees for drafting documents and no filing fees

c) Taxation – no double taxation; all income taxes handled on the owner’s personal tax returns

ii) Disadvantages

a) Unlimited personal liability

b) Cannot issue equity (e.g., stock, options) to key employee or investor

c) No continuity – business ceases to exist upon owner’s death

iii) Should generally be avoided, but may be for someone who wants to start a one-person business, quickly, cheaply, and has limited liability exposure (e.g., accountant who can get insurance to cover malpractice liability and general liability)

2. General Partnership (See NY Partnership Law) – an association of two or more individuals (or entities) to conduct a business as co-owners (“partners”).

i) Advantages

a) Easy to form; no formation documents to file; just need a partnership agreement

b) Relatively inexpensive – no organizational documents, so no filing fees; there will be some legal fees associated with the drafting of a partnership agreement; Section 130 of NY General Business Law requires partners carrying on business as a partnership to file a certificate with the county clerk in each county in which the partnership will be doing business

c) Separate legal entity – partnership interests can be issued and transferred; partnership can own real estate and other property in the partnership name and enter into contracts under partnership name

d) Taxation – no double taxation (i.e., it is a flow-through entity); partners pay income tax for their share of the partnership’s profits or losses

ii) Disadvantages

a) Unlimited personal liability – every partner in a general partnership assumes unlimited liability for the partnership’s debts and liabilities, including any tortuous acts committed by a co-partner during the ordinary course of partnership business; one partner has the authority to bind the partnership without the express written consent of all partners

b) Impractical to have outside investors – investors do not want to be general partners and subject themselves to unlimited liability

c) Fiduciary obligations – undivided loyalty, good faith and fair dealing obligation to the other partners with respect to all matters affecting the business

iii) Should generally be avoided, but may be used for two or more individuals who want to start a business quickly, cheaply and/or may be“testing the waters,” but will have limited liability exposure (e.g., an accounting firm or law firm that can insure against malpractice liability and general liability)

3. Limited Partnership (See NY Partnership Law) – an association of two or more individuals (or entities) to conduct a business as co-owners; need at least one general partner and one limited partner; general partner’s liability is unlimited and limited partner’s liability is limited to amount of investment in the business; business is managed by the general partner(s)

i) Advantages

a) Limited liability – limited partners do not have unlimited liability (unless they participate in control of the business, in which case they are deemed a general partner)

b) Facilitates outside investors – investors become limited partners with limited liability and their interests can be easily transferred. Used to see for syndications and real estate investments.

c) Pass-through tax treatment – no double taxation (i.e., flow through entity); profits and losses flow through to the partners

ii) Disadvantages

a) Unlimited liability for general partners – usually creates complex structure of corporation or LLC being the general partner to shield liability

b) Limited partners may not participate in management – otherwise limited partner may be deemed general partner and subject to unlimited personal liability

iii) Typically seen where general partner(s) do the work and the limited partners provide the capital (e.g., private equity firm or hedge fund). Practically not used since advent of Limited Liability Companies (discussed below).

4. C Corporation (See Business Corporation Law) – separate legal entity from its owners; difference between C and S corporation is a tax concept, not a corporate concept (discussed below)

i) Advantages

a) Shield against personal liability – most widely-accepted and well-established entity; so long as all corporate formalities have been complied with, shareholders will not be liable for the debts, obligations and liabilities of the corporation regardless of any management participation; shareholders’ losses will be limited to the amount of their investment

b) Attracts venture capitalists – VC funds prefer C corporations; often prohibited by their charter documents from investing in “pass-through” entities (such as S corporations and LLCs)

c) Flexible capital structure – may have different classes of stock (e.g., multiple classes of common, preferred, convertible, warrants); may issue stock options to employees; facilitates investments because of a broad range of financial instruments (e.g., preferred stock, convertible notes)

d) No publication requirements, unlike with LLCs (discussed below with LLCs)

ii) Disadvantages

a) Double taxation – corporation is taxed on its profits and then shareholders are taxed on any dividends distributed to them

b) Formalities and recordkeeping – must file a certificate of incorporation, adopt bylaws, elect board of directors, hold annual meetings of board of directors and shareholders, maintain separate books and records and bank accounts, etc.; failure could result in a court “piercing the corporate veil” and holding corporation’s shareholders personally liable for corporation’s debts, obligations and liabilities

c) More expensive to form and maintain than sole proprietorship and partnerships

iii) If doing business in another state, have to “qualify” to do business there

iv) Ideal for business that wants to limit liability and/or will be seeking venture capital funding, but does not need (or does not qualify for) S corporation pass-through tax treatment

5. S Corporation – Formed the same way as a C corporation, but S election filed with IRS; again, tax treatment is the only distinction between C corporation and S corporation (not a corporate concept).

i) Advantages

a) Shield against personal liability – so long as all corporate formalities have been complied with

b) Pass-through tax treatment – profits and losses flow directly through to the shareholders; no double taxation

c) Can be converted to C corporation relatively easily in case need to switch to a C corporation for venture capitalists

d) No publication requirements, unlike with LLCs (discussed below with LLCs)

ii) Disadvantages

a) Limitations on type and number of shareholders – must be US citizens or residents, estates, certain eligible trusts, and no more than 100 shareholders

b) May only have one class of stock

c) Same formalities and recordkeeping as C corporation

iii) Typically for those that want liability protection, pass-through tax treatment and helpful if you think they may be seeking venture capital funding in the future (chosen over LLC because easier to convert to C corporation if needed for venture capitalists down the road)

6. Limited Liability Company (NY LLC Law) – Separate legal entity; formed by filing Articles of Organization; owners are called “Members”; this is most often seen now and we will spent most of the time on this entity

i) Advantages

a) Flexibility – can operate like a corporation (create a Board of Managers), a general partnership (member-managed)

b) Limited liability for members;

c) Flow-through tax treatment is default (can elect C corporation tax treatment, but rare);

ii) Disadvantages

a) Complex partnership tax rules

b) Not attractive to venture capitalists; converting from LLC to C corporation more difficult than S corporation to C corporation

c) Limitation on capital structure – difficult to grant options and issue other types of securities (e.g., preferred membership interests)

d) NY has publication requirements for LLCs, which can be expensive; corporations do not have such publication requirements

**II. Tax**

1. C-Corporation
   1. Two levels of tax – at corporate and shareholder level
   2. One or more shareholders
   3. No restrictions on types of owners
   4. No limitation on classes of ownership interests
   5. Distributions must be proportionate to ownership
   6. Sale of substantially all assets – generally, results in double taxation
2. S-Corporation
   1. Pass through treatment – tax at shareholder level only
   2. New corporation must file S election with IRS within 2.5 months after earliest of first date on which corporation has shareholders, acquires assets or begins doing business.
   3. New York and New Jersey have their own additional S election filing requirements.
   4. 1-100 shareholders (spouses and all members of a family counted as one shareholder)
   5. Owners may not include corporations, nonresident aliens, partnerships, or certain trusts
   6. Only one class of stock allowed, but may have non-voting stock
   7. Distributions must be proportionate to stock ownership
   8. Sale of substantially all assets – one level of tax as gain or loss realized is passed through to owners
3. Limited Liability Company
   1. Default is partnership (pass through treatment) – tax at member level only
   2. Choice to be taxed like partnership or C-corporation
   3. One or more members
   4. No restrictions on types of members
   5. No limitations on classes of membership interest
   6. Distributions need not be proportionate to ownership
   7. Sale of substantially all assts – one level of tax as gain or loss realized is passed through to owners
4. Limited Partnership
   1. Tax at partner level only
   2. At least two partners required (a general partner and one or more limited partners)
   3. No restrictions on type of owners
   4. No limitations on classes of ownership interest
   5. Distributions need not be proportionate to ownership
   6. Sale of substantially all assts – one level of tax as gain or loss realized is passed through to owners
5. General Partnership
   1. Tax at partner level only
   2. At least two partners required (all general partners)
   3. No restrictions on type of owners
   4. No limitations on classes of ownership interest
   5. Distributions need not be proportionate to ownership
   6. Sale of substantially all assets – one level of tax as gain or loss realized is passed through to owners

**III. Corporations (BCL)** **–** The Business Corporations Law (BCL) is like a cookbook. All of the procedures and rules are spelled out in detail. It is often the best source to go to for corporate transactions. We highly recommend reading the statute in detail for a complete overview. Here are highlights:

1. Corporate Purposes and Powers (Article 2 of BCL)

i) Purposes (BCL 201) – A corporation may be formed to carry on any lawful business purposes; generally, purpose is stated as such in the charter; can be more specific (see ultra vires defense below); **TIP:** We usually put any lawful business purpose unless the client wants to limit; discuss with the client;

ii) General Powers (BCL 202) – See the laundry list set forth in the statute; some highlights:

a) Perpetual duration

b) Sue and be sued in court

c) Own, buy, sell, mortgage, pledge and/or lease real and/or personal property

d) Make contracts

e) Conduct its business and operate

f) All powers necessary or convenient to effect any or all of the purposes for which the corporation is formed; **TIP:** Good idea to give corporation all powers.

2. Corporate Name and Service of Process (Article 3 of BCL)

i) General (BCL 301)

a) The name must be distinguished from other businesses in NY

b) Must have “Inc.” or “Corp.”

c) Certain prohibited words

d) Can’t be misleading

ii) Reservation of Name (BCL 303) – Can reserve a name with the Secretary of State if you aren’t ready to file a Certificate of Incorporation, but we don’t usually do this

iii) Statutory designation of secretary of state as agent for service of process (BCL 304) – The secretary of state is an agent for every domestic corporation and every authorized foreign corporation for service of process; (e.g., if someone slips and falls on corporate property, they just need to serve the secretary of state with the complaint rather than find the corporate address of the corporation)

iv) Registered Agent for Service of Process (BCL 305) – Corporation may designate an agent for service of process and agent must be in NY; the address may be at the corporate office in NY or if business does not have a NY address, then can appoint a corporate service to be agent in NY

3. Formation of Corporation (Article 4 of BCL)

There are certain fixed state costs (e.g., filing fees, publication costs). Attorneys can file corporate documents to form business entities and comply with statutory requirements on their own. Some prefer to in order to save on service fees. One can also use the corporate service, which can save you time and money.

i) Incorporator files or causes to be filed the Certificate of Incorporation (see forms on DOS website)

a) BCL 402 states what the Certificate of Incorporation must contain: name, purpose, county location, aggregate number of authorized shares, classes of shares, designation of secretary of state as agent for service of process, duration of corporation if other than perpetual;

b) Certificate of Incorporation may contain designation of registered agent in addition to Secretary of State;

b) May limit personal liability of directors or shareholders for damages for any breach of duty (can’t limit acts in bad faith, intentional misconduct, a knowing violation of law)

ii) Organization Meeting (BCL 404)

a) Incorporator appoints Board of Directors and adopts by-laws (may be done without a meeting if each incorporator signs a document setting forth the actions taken). Bylaws will fix the number of directors.

iii) Biennial Statement (BCL 408) – every two years, corporation must file biennial statement, setting forth name and business address of CEO, street address of its principal executive office, address where secretary of state shall mail a copy of any process served

4. Corporate Finance (Article 5 of BCL)

i) Authorized Shares (BCL 501)

a) The number of shares stated in the certificate of incorporation that the corporation may issue; Franchise tax is a function of authorized shares and par value; **TIP:** Typically do 200 no par value to achieve a minimum franchise tax;

b) There may be more than one class authorized

c) Certificate of incorporation can define voting rights of each class (e.g., there may be a non-voting class of stock)

d) Different classes of stock may have different economic rights (e.g., preference on dividend or liquidation rights)

ii) Consideration and payment for shares (BCL 504)

a) May be paid in cash, property, past services rendered and/or an obligation to perform services having an agreed value

b) Stock may not be issued for less than its par value

iii) Rights and options to purchase shares (BCL 505)

a) Unless prohibited by the certificate of incorporation, corporation may create and issue rights or options entitling holders thereof to purchase shares from the corporation, upon terms and conditions fixed by the board

iv) Determination of stated capital (BCL 506)

a) Par value x no. of outstanding shares

b) If no par value, then consideration paid for outstanding shares

c) May not be distributed as dividends

v) Certificates representing shares (BCL 508)

a) Corporation may issue certificates or shares may be uncertificated

b) Certificates must be signed by: (i) chairman or vice chairman of the board or president or a vice-president; AND (ii) secretary or an assistant secretary or the treasurer or an assistant treasurer; may be sealed with corporate seal

c) Certificates must state that: (i) corporation is formed under laws of NY; (ii) name of the person or persons to whom issued; (iii) number and class of shares which certificate represents

d) There should be a legend on the certificate if there are transferability restrictions (e.g., per a shareholder’s agreement, per SEC regulations)

vi) Dividends or other distributions in cash or property (BCL 510)

a) Corporation may declare and pay dividends, unless corporation is or would become insolvent or payment is contrary to restrictions in certificate of incorporation

b) Dividends may be paid out of capital surplus (i.e., capital paid into company above the par value) and net profits for the fiscal year

5. Shareholders (Article 6 of BCL)

i) Owners are called “shareholders” and own shares of stock

ii) By-laws (BCL 601) (See form)

a) Initial by-laws adopted by the incorporator; thereafter, by-laws may be adopted, amended or repealed by a majority of the shareholders; by-laws may also be adopted, amended or repealed by the board when so provided in the certificate of incorporation or by-laws adopted by the shareholders;

iii) Meetings of shareholders (BCL 602)

a) Shareholder meeting shall be held annually for the election of directors and the transaction of other business; failure to meet or elect sufficient number of directors does not cause dissolution

b) Board or such persons authorized by the certificate of incorporation or by-laws may call a special meeting of the shareholders; only business related to the purpose set forth in the notice of special meeting may be conducted

c) By-laws may designate reasonable procedures for calling and conduct of a meeting of shareholders: (i) who may call and conduct the meeting, (ii) order of business to be conducted, (iii) procedures and requirements for nomination of directors, (iv) procedures for making of shareholder proposals, and (v) procedures for adjournment of meeting

iv) Special meeting for election of directors (BCL 603)

v) Notice of meetings of shareholders (BCL 605)

a) Must follow this procedure to provide prior notice of meetings; otherwise, actions taken at meetings may be invalidated

vi) Shareholder may waive notice (BCL 606)

vii) Quorum (BCL 608) – holders of a majority of the votes of shares entitled to vote constitutes a quorum; certificate of incorporation or by-laws may provide for lesser quorum, but may not be less than one-third; certificate of incorporation may (under BCL 616) provide for greater requirement; quorum not broken by subsequent withdrawal of any shareholders

viii) Proxies (BCL 609) – shareholder may authorize another person to act for him by proxy; expire automatically after eleven months, unless otherwise provided in the proxy; revocable by the shareholder, but there can be an irrevocable proxy

ix) Vote of shareholders (BCL 614) – Directors elected by plurality of votes (unless otherwise required by statute, by-laws or certificate of incorporation); corporate action (other than election of directors) needs majority vote (unless otherwise required by statute, by-laws or certificate of incorporation)

x) Written consent of shareholders, subscribers or incorporators without meeting (BCL 615) – any action may be taken without a meeting by written consent of shareholders sufficient to take such action; if less than unanimous, must give notice to non-consenting shareholders

xi) Voting Agreements; Shareholder Agreements (BCL 620) – good practice to have a shareholder agreement (we will discuss an operating agreement in the context of an LLC in greater detail below; provisions in shareholder agreements and operating agreements are comparable); frequently shareholders agree on whom they will vote for as directors and on who the directors will appoint as officers, but shareholders cannot actually bind directors as to whom they will appoint as officers

xii) Preemptive rights (BCL 622) – gives a shareholder the right to purchase pro rata shares or other securities to be issued, under same terms and conditions as proposed to be issued, in order for shareholder to maintain dividend and voting rights; for corporations formed after Sept. 1, 1963, no preemptive rights exist unless expressly provided in certificate of incorporation

xiii) Books and records; right of inspection (BCL 624) – corporation must keep correct and complete books and records of account and minutes of the proceedings of its shareholders, board and executive committee at the office of the corporation; shareholders have right, upon five days’ written demand, to examine shareholder minutes and record of shareholders; corporation may deny request if shareholder refuses to furnish the corporation with an affidavit stating that such inspection is not for a purpose contrary to the business interest of the corporation and that shareholder has not sold or offered to sell a list of shareholders of any corporation within the past five years

6. Directors and Officers (Article 7 of BCL)

i) Board of Directors responsible for the oversight and management of all corporate affairs; directors must be at least 18; certificate of incorporation or by-laws may state other qualifications (BCL 701)

ii) Number of directors (BCL 702) – one or more; default is one; may be fixed by the by-laws

iii) Election and term of directors (BCL 703) – directors elected at each annual meeting of shareholders; hold office until the expiration of their term and until successor has been elected and qualified

iv) Newly created directorships and vacancies (BCL 705) – newly created directorships may be filled by a vote of the board; vacancies due to removal may be filled only be vote of shareholders (unless certificate of incorporation or by-laws say otherwise)

v) Removal of directors (BCL 706) – may be removed for cause by vote of the shareholders; certificate of incorporation or by-laws may provide for removal of directors without cause by vote of shareholders

vi) Quorum of directors (BCL 707) – majority, unless certificate of incorporation requires greater number; certificate of incorporation or by-laws may fix quorum at less than majority, but not less than one-third

vii) Action by the board (BCL 708) – majority vote; may be taken without a meeting if unanimous written consent

viii) Greater requirement as to quorum and vote of directors (BCL 709) – certificate of incorporation can provide for greater quorum and/or voting requirements

ix) Place and time of meetings of the board (BCL 710) – may be held anywhere (within or outside NY); by-laws fixes time and place, or board can choose

x) Notice of meetings of the board (BCL 711) – regular meetings may be held without prior notice if time and place fixed by by-laws or the board; by-laws prescribe what constitutes notice; director may waive notice

xi) Officers (BCL 715) – board may elect a president, one or more vice-presidents, a secretary and a treasurer and such other officers as it may determine; any two or more offices may be held by the same person; officers have the authority to perform such duties in the management of the corporation as may be provided in the by-laws or, to the extent not so provided, by the board

xii) Removal of officers (BCL 716) – may be removed by board with or without cause

xiii) Duty of directors (BCL 717) – good faith and with that degree of care which an ordinarily prudent person in a like position would use under similar circumstances

7. Amendments and Changes (Article 8 of BCL)

i) Right to amend certificate of incorporation (BCL 801) – corporation may amend its certificate of incorporation if such amendment contains only such provisions as might be lawfully contained in an original certificate of incorporation; E.g., - change corporate name; change corporate purpose; change location and/or designation of registered office and/or agent; increase or decrease authorized shares; change par value of shares; change any other provision relating to the business of the corporation and/or rights and powers

ii) Authorization of amendment or change (BCL 803) – authorized by vote of board, followed by vote of a majority of shareholders; board alone may amend only: location and/or designation of corporation’s office and/or registered agent

iii) Certificate of amendment; contents (BCL 805) – must have the following: name of corporation and, if it has changed, the name under which it was formed; date certificate of incorporation filed; see statute for various fact patterns

iv) Certificate of change (BCL 805-A) – if just changing location and/or designation of corporation’s office and/or registered agent, then can file a certificate of change (board only authorization; no need for shareholders vote)

v) Restated certificate of incorporation (BCL 807) – instead of filing an amendment, can file an entirely restated certificate of incorporation with the provisions already amended, so long as corporation was authorized by the board and/or shareholders as required under the amendment sections of the BCL

8. Merger or Consolidation; Guarantees; Disposition of Assets; Share Exchanges (Article 9 of BCL)

i) Merger or consolidation (BCL 901) - Two or more corporations (or a corporation and another type of business entity) may merge into a single corporation or consolidate into a new corporation

ii) Plan of merger or consolidation (BCL 902) – board of each corporation must adopt a plan of merger or consolidation; see statute for required contents of such plan

iii) Authorization by shareholders (BCL 903) – after board adopts plan of merger or consolidation, board submits plan to a vote of shareholders

iv) Certificate of merger or consolidation; contents (BCL 904) – after board and shareholders adopt plan, certificate of merger must be signed on behalf of each corporation and delivered to department of state; see statute for required content of certificate of merger

v) In general, look at this chapter for the section on the type of entities you have merging into each other; the section will provide a cookbook recipe for effecting the merger

vi) Sale, lease, exchange or other disposition of assets (BCL 909) – needs majority of board (unless stated otherwise in certificate of incorporation) and 2/3 shareholder approval (unless stated otherwise in certificate of incorporation)

9. Non-Judicial Dissolution (Article 10 of BCL)

i) Authorization of dissolution (BCL 1001) – for corporation incorporated after Sept. 1, 1963, need majority of shareholders

ii) Certificate of dissolution; contents (BCL 1003) – name of corporation; date certificate of incorporation filed; name and address of each officer and director; statement that corporation elects to dissolve; manner in which dissolution was authorized

iii) Certificate of dissolution; filing (BCL 1004) – need tax clearance before NY will let a corporation dissolve

iv) Procedure after dissolution (BCL 1005) – corporation shall carry on no business, other than winding up its affairs (different rules for corporations formed pre-September 1, 1963)

10. Foreign Corporations (Article 13 of BCL)

i) Authorization of foreign corporations (BCL 1301) – foreign corporation (not incorporated in NY) must be authorized to do business in NY; if foreign corporate name is not acceptable in NY (e.g., already used by another corporation), then foreign corporation must file d/b/a

ii) Application for authority to do business; contents (BCL 1304) – application must include: name of corporation; fictitious name, if applicable; jurisdiction and date of incorporation; purposes for which formed; county within NY where office is to be located; designation of secretary of state as agent; name and address within NY of registered agent; statement that foreign corporation has not done business in NY. (If prior business was done in New York State, need New York State tax clearance.)

iii) Surrender of authority (BCL 1310) – foreign corporation may surrender its authority by filing certificate of surrender of authority; see section for required content

11. Professional Service Corporations (Article 15 of BCL)

i) Organization (BCL 1503) – one or more individuals duly authorized by law to render the same professional service within the state may organize, or cause to be organized, a professional service corporation for the purpose of rendering the same professional service; certificate of incorporation must state: the profession practiced, names and resident addresses of original shareholders, directors and officers; attach a certificate issued by the licensing authority certifying that each of the proposed shareholders, directors and officers is authorized to practice such profession

ii) Rendering of professional service (BCL 1504) – types of professions that must form a PC: engineers, architects, land architects, land surveyors, doctors, dentists, podiatrists, optometrists, ophthalmologists, veterinarians, pharmacists, nurses, physiotherapists, chiropractors, certified shorthand reporters, accountants, attorneys

iii) Professional relationships and liabilities (BCL 1505) – each shareholder, employee or agent of a professional service corporation is personally liable for any negligent or wrongful act or misconduct committed by him or by any person under his direct supervision and control while rendering professional services on behalf of the corporation (i.e., no limited liability for malpractice)

iv) Issuance of shares (BCL 1507) – only individuals who are authorized to practice the profession may be shareholders of a PC

v) Directors and officers (BCL 1508) – only individuals who are authorized to practice the profession may be directors and officers of a PC

vi) Disqualification of shareholders, directors, officers and employees (BCL 1509) – if one becomes legally disqualified to practice profession, must sever all employment with, and financial interests (other than interests as a creditor) in the PC; deemed to be an irrevocable offer by the disqualified shareholder to sell his shares to the corporation

vii) Death or disqualification of shareholder (BCL 1510) – PC shall purchase or redeem shares of a shareholder who dies or is disqualified within 6 months of appointment of executor or disqualification, at book value of such shares; may be modified by a shareholder’s agreement

viii) Transfer of shares (BCL 1511) – prohibited to non-professional

**IV. Limited Liability Company (LLCL)**

1. Formation (Article 2 of LLCL)

i) Purpose (LLCL 201) – may be formed for any lawful purpose

ii) Powers (LLCL 202) – substantially similar to corporation

iii) Formation (LLCL 203) – organizer files articles of organization; organizer need not be a member (owner); must have at least one member at the time of formation; articles of organization must contain: name of LLC, county of LLC’s office, specific date of dissolution (if any), designation of secretary of state for service of process, address where secretary of state shall mail a copy of any process served (may be in or outside of NY), name and address of registered agent (if any) (address must be in NY), if there is a registered agent: a statement that the registered agent is to be the agent of the LLC upon whom process against it may be served, any other provisions not inconsistent with law for regulation of internal affairs of LLC

iv) Limited liability company name (LLCL 204) – contains “Limited Liability Company”, “L.L.C.” or “LLC” at end; must be distinguished from the name of other business entities

v) Reservation of name (LLCL 205) – substantially similar to corporation

vi) Must publish notice. Affidavits of publication (LLCL 206) – corporate service discussed

2. Management by Members or Managers (Article 4 of LLCL)

i) Management of the limited liability company by members (LLCL 401) – management by members is default; must state otherwise in articles of organization if want manager-managed

ii) Voting rights of members (LLCL 402) – Unless stated otherwise in the operating agreement, each member votes in proportion to the member’s share of the current profits of the LLC; unless stated otherwise in operating agreement, need a majority to admit a member, approve debt, amend articles of organization, approve dissolution of LLC, approve sale of substantially all of LLC’s assets, approve merger

iii) Meetings, quorum, notice of meetings, waiver of notice, action by members without a meeting – all substantially similar to corporation

iv) Management by managers (LLCL 408) – LLC may be manager managed by stating so in articles of organization; majority vote; action may be taken by unanimous written consent without a meeting; my participate in a meeting by telephone

v) Duties of managers (LLCL 409) – must be performed in good faith and with that degree of care that an ordinarily prudent person in a like position would use under similar circumstances

vi) Qualification of mangers (LLCL 410) – manager need not be a member of the LLC

vii) Operating agreement (LLCL 417) (discussed in greater detail below) – LLCs must have an operating agreement setting forth: the business of the LLC, the conduct of its affairs and the rights, powers, preferences, limitations or responsibilities of its members, managers, employees or agents; initial operating agreement may be combined with the articles of organization

3. Contributions and Distributions (Article 5 of LLCL)

i) Form of capital contributions (LLCL 501) – may be in cash, property and/or services rendered (past or future); note that capital contributions to a corporation may only be for future services rendered (not past)

ii) Liability for contributions (LLCL 502) – member is obligated to contribute as promised, even if unable to because of death, disability or any other reason

iii) Sharing of profits and losses (LLCL 503) – as set forth in operating agreement; if not stated in operating agreement, based on value of contributions of each member

iv) Sharing of distributions (LLCL 504) – distributions shall be allocated among the members as set forth in operating agreement; if operating agreement is silent, distributions allocated on the basis of the value, as stated in the records of the LLC, of the contributions of each member

v) Distributions in kind (LLCL 505) – member has no right to demand distribution in any form other than cash (unless stated otherwise in operating agreement)

viii) Limitations on distributions (LLCL 508) – LLC shall not make a distribution if liabilities (other than liabilities to members on account of membership interests) exceed fair market value of LLC’s assets

4. Members and Membership (Article 6 of LLCL)

i) Nature of membership interest (LLCL 601) – personal property; no interest in specific property of the LLC

ii) Admission of members (LLCL 602)

a) Person becomes a member the later of 1) effective date of the initial articles of organization; or 2) date as of which the person becomes a member pursuant to this section or the operating agreement;

b) After initial articles of organization, person may become a member by acquiring membership interest pursuant to the operating agreement; if not provided in operating agreement, upon majority vote of members

c) In case of assignee of a member who has the power as provided in the operating agreement, assignee becomes member upon the exercise of assignor’s power

d) Upon merger, upon compliance with the operating agreement of the surviving LLC

iii) Assignment of membership interest (LLCL 603) – except as provided in operating agreement (1) membership interest is assignable in whole or in part; (2) assignment does not dissolve LLC or entitle assignee to participate in management or exercise any rights or powers of a member; (3) \*only effect of an assignment is to entitle assignee to receive distributions and allocations of profits and losses; and (4) a member ceases to be a member upon assignment of all of his or her membership interest (pledge or granting of a security interest does not cause the member to cease to be a member);

a) membership interests need not be certificated; however, any restrictions on the sale or transfer of membership interests must be noted conspicuously on the face or back of every certificate;

iv) Rights of assignee to become a member (LLCL 604) – Unless stated otherwise in operating agreement, assignee may not become a member without vote or written consent of a majority of membership interests (other than the assigning member); assignee that becomes a member has the rights and liabilities set forth in articles of organization, operating agreement and LLCL

v) Liability upon assignment (LLCL 605) – assignor not released from any liability to the LLC incurred prior to effectiveness of the assignment;

vi)\* Withdrawal of a member (LLCL 606) – member may only withdraw at the time or upon the happening of events specified in the operating agreement; unless stated otherwise in operating agreement, member may not withdraw prior to dissolution and winding up of LLC; operating agreement may provide that a membership interest may not be assigned prior to the dissolution and winding up of LLC;

vii) Rights of creditors of members (LLCL 607) – court may charge the membership interest of member with payment of unsatisfied amount of a judgment against the member; judgment creditor only has rights of an assignee of the membership interest (i.e., economic interest only);

viii) Powers of estate of a deceased or incompetent member (LLCL 608) – deceased member’s executor may exercise all of the member’s rights for the purpose of settling his or her estate, including nay power under the operating agreement of an assignee to become a member

ix) Liability of members, managers and agents (LLCL 609) – members and managers are not liable for any debts, obligations or liabilities of the LLC or each other;

x) Business transactions of a member with the LLC (LLCL 611) – except as provided in the operating agreement, a member may lend money to, borrow money from, act as guarantor for, provide collateral for the obligations of and transact other business with the LLC;

5. Dissolution (Article 7 of LLCL)

i) Dissolution (LLCL 701) – LLC is dissolved and its affairs shall be wound up upon the first to occur of the following:

a) latest date provided in articles of organization or operating agreement; if none specified, then existence is perpetual

b) the happening of events specified in operating agreement

c) vote or written consent of at least a majority in interest of the members (subject to operating agreement)

d) at any time there are no members, unless legal representative of last remaining member agrees in writing within 180 days to continue LLC and to the admission of the legal representative as a member

e) entry of decree of judicial dissolution

ii) Unless stated otherwise in operating agreement, death, retirement, resignation, expulsion, bankruptcy or dissolution of any member shall not cause LLC to be dissolved, unless within 180 days, majority interest of members vote or agree in writing to dissolve LLC

iii) Winding Up (LLCL 703) – unless otherwise provided in operating agreement, members may wind up LLC; persons winding up LLC may: prosecute and defend suits, settle and close LLC’s business, dispose of and convey LLC’s property, discharge LLC’s liabilities and distribute any remaining assets to members

iv)\* Distribution of assets (LLCL 704) – Upon winding up of LLC, assets distributed as follows:

a) to creditors

b) except as provided in operating agreement, to members and former members in satisfaction of liabilities for distributions

c) except as provided in operating agreement, to members first for the return of their contributions, and second respecting their membership interests, in the proportions in which the members share in distributions

v) Articles of dissolution (LLCL 705) – filed within 90 days; shall set forth: name of LLC; date of filing its articles of organization; event giving rise to the filing of articles of dissolution; and any other information the persons filing the articles determine

6. Foreign LLCs (Article 8 of LLCL)

i)\* Application for authority (LLCL 802) – must apply for authority to do business before doing business in NY; submit to state dept: certificate of existence; application for authority as foreign LLC;

a) See LLCL 802(a) for what application must set forth

b) See LLCL 802(b) for publication requirements

ii)\* Activities not constituting doing business (LLCL 803) – litigation; holding meetings of its members or managers; maintaining bank accounts; or maintaining offices or agencies only for the transfer, exchange and registration of its membership interests or appointing and maintain depositaries with relation to its membership interests

iii) Doing business without certificate of authority (LLCL 808) – may not maintain any action, suit or special proceeding in any court in NY; does not impair the validity of any contract or act or prevent the foreign LLC from defending nay action or special proceeding

7. Mergers (Article 10 of LLCL)

i) Merger or consolidation (LLCL 1001) – merger = two or more LLCs into one of the existing LLCs; consolidation = two or more LLCs combine into a new LLC

ii) Procedures for merger or consolidation – See LLCL 1002

iii) Certificate of merger or consolidation; contents – See LLCL 1003

iv) Payment of interest of dissenting members (LLCL 1005) – within 10 days after merger, surviving company must send to each dissenting former member a written offer to pay in cash the fair value of such former member’s membership interest; payment must be made within 10 days after notice of such member’s acceptance; if company and former member fail to agree on price within 90 days, 623(h), (i), (j) and (k) of BCL (procedure to enforce shareholder’s right to receive payment for shares) apply

8. Professional Service Limited Liability Companies (Article 12 of LLCL)

i) Profession = any practice as an attorney or as a licensed physician and those professions designated in title eight of the education law (e.g., chiropractor, dentist, veterinarian, physical therapist, podiatrist, optometrist, architect, accountant, psychologist, social worker)

ii) Formation (LLCL 1203) – each member must be licensed to render professional services; see LLCL 1203(b) for requirements of articles of organization; see LLCL 1203(c) for publication requirements

iii) Rendering of professional service (LLCL 1204) – may only render professional service through individuals authorized by law to render such services

iv)\* Professional relationships and liabilities (LLCL 1205) – each member, manager, employee or agent shall be personally and fully liable and accountable for any negligent or wrongful act or misconduct committed by him or her or by any person under his or her direct supervision and control while rendering professional services on behalf of the PLLC

v) Purposes of formation (LLCL 1206) – must only engage in profession(s) its members are licensed to perform; must only engage in profession(s) as set forth in articles of organization

vi) Membership of professional service limited liability companies (LLCL 1207) – a member shall only be a professional

vii) Disqualification of members, managers and employees (LLCL 1209) – if member becomes disqualified to practice profession, must sever all employment with and financial interests (other than interests as a creditor or vested rights under bona fide retirement program) in such PLLC

viii) Death, disqualification or dissolution of members (LLCL 1210) – PLLC must purchase or redeem the membership interest of a member who dies or becomes disqualified (or in the case of a PC, etc. member, dissolution)

ix) Transfer of a membership interest (LLCL 1211) – members may only transfer to other professionals

x)\* Limited liability company name (LLCL 1212) – may contain deceased person’s name only if such person’s name was part of the name of such LLC at the time of such person’s death; or such person’s name was part of the name of an existing partnership or PSC (Professional Services Corporation) and at least 2/3 of such partnership’s partners or corporation’s shareholders, become members of such PLLC.

xi) Mergers and consolidations (LLCL 1216) – PLLCs may merge or consolidate

9. Operating Agreement.

i) Name and principal office

ii) Purposes and powers

iii) Members

iv) Management/Meetings

a) Manager Managed vs. Member Managed

b) Supermajority Provisions

v) Titles (e.g., managing member)

vi) Capital Contributions/Capital Accounts

vii) Loans

viii) Duties and Services of Members

a) Restrictive Covenants

ix) Net Profits/Losses

x) Compensation

xi) Liability of Members

xii) Disability/Death/Retirement Buyouts

a) Cross Purchase v. Redemption

b) Purchase Price Determination

c) Life Insurance

d) Terms of Payment

xiii) Dissolution

xiv) Books and Records – Who Owns?

xv) Limitations on Transfer

a) Right of First Refusal

b) Bring Along/Come Along Rights