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## FISCAL IMPACT REPORT

**ORIGINAL DATE** 01/31/17  
**SPONSOR** Cook **LAST UPDATED** \_\_\_\_\_ **HB** 180

**SHORT TITLE** Revised Uniform LLC Act **SB** \_\_\_\_\_

**ANALYST** Daly

### REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Nonrecurring	Fund Affected
FY17	FY18	FY19		
		\$260.7	Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

### ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY17	FY18	FY19	3 Year Total Cost	Recurring or Nonrecurring	Fund Affected
<b>Total</b>		\$35.0		\$35.0	Nonrecurring	General Fund
			>\$8.5	>\$8.4	Recurring	General Fund

(Parenthesis ( ) Indicate Expenditure Decreases)

### SOURCES OF INFORMATION

LFC Files

#### Responses Received From

Administrative Office of the Courts (AOC)

Attorney General’s Office (AGO)

Secretary of State (SOS)

### SUMMARY

#### Synopsis of Bill

House Bill 180, for the Courts, Corrections and Justice Committee, repeals the Limited Liability Company Act, NMSA 1978, Sections 53-19-1 through -74 (1993, as amended through 2003) (“LLC Act”), in its entirety, and enacts the Revised Uniform Limited Liability Company Act (“Revised Act”) in its place. The Revised Act applies to all limited liability companies (“LLCs”) formed on and after July 1, 2018, except that an LLC formed prior to this date may elect to be governed by the Revised Act in accordance with its operating agreement/applicable law and after

filing an amended and restated certificate of organization with the Secretary of State (“SOS”) expressing its desire to be governed by the Revised Act.

LLCs formed prior to July 1, 2018, that do not elect to be governed by the Revised Act will continue to be governed by the LLC Act, as if that act had not been repealed, but such LLCs shall not be renewed unless so provided in the original agreement or in the manner provided in the limited liability company agreement or by law for amending a limited liability company agreement. These LLCs will nevertheless be subject to certain provisions of the Revised Act. Foreign LLCs will be governed by the Revised Act regardless of the time of formation.

The Revised Act clarifies that the SOS is responsible for many of the duties pertaining to the oversight of LLCs (as opposed to the Public Regulation Commission). It also clarifies the effect of records filed with SOS on third parties with respect to the actual and apparent authority of persons acting on behalf of the LLC and describes the rights of third parties who rely on those records when they contain inaccurate information.

The Revised Act further provides management structures for LLCs, namely, member-managed and manager-managed, and describes the duties of members and managers and the rights of third parties under each structure. The Revised Act also permits LLCs to file statements of authority with the SOS in order to place third parties on notice of the authority, restricted or otherwise, of certain members or managers of the LLC, as well as clarifies what authority those members or managers have to bind the LLC.

Other features of the Revised Act include changes to and clarification of the voting rights of members in certain circumstances; clarifies the duties of a transferee (“assignee” under the LLC Act); and places new and significant restrictions on access to and inspection of LLC records.

Additionally, the Revised Act imposes an obligation directly on the members or managers of an LLC to correct information in articles of organization that become inaccurate; allows for derivative actions to enforce a right of the LLC, when, within a reasonable time, an action is not instituted after a member or manager makes a demand. If it would be futile to wait for the members or managers to bring a derivative action following a demand, the Revised Act would permit a member to initiate the action unilaterally.

The Revised Act establishes more defined processes and limitations on provisions for apportioning distributions, profits/losses, member voting rights, dissociation (including the creation of special litigation committee procedures), service of process and allows for interest exchanges, in contrast to the LLC Act. The Revised Act further defines the processes and limitations on authorizations for mergers and conversions. Unlike the LLC Act, which permits an LLC to set a special period of time or date when it will cease doing business, the Revised Uniform Limited Liability Act only allows for a perpetual duration, requiring the limited liability company to formally dissolve or withdraw in New Mexico.

HB 180 also repeals existing law governing amendments to Articles of Incorporation, and replaces them with provisions governing restated Articles of Incorporation, and adds procedures for conversion and domestication.

The effective date of the provisions repealing the LLCA and enacting the RLLCA is July 1, 2018. The effective date of the amendments regarding amending articles of incorporation and conversion and domestication of business entities is January 1, 2018.

### **FISCAL IMPLICATIONS**

SOS reports 150,297 limited liability companies in New Mexico (134,390 domestic and 15,907 foreign) are registered in its office. Currently, there is no requirement for LLCs to file any type of report to update information such as LLC address information, member(s) or manager(s). HB 180 allows LLC's formed prior to July 1, 2018 to be governed under the original LLCA, in which case no initial or triennial report would be required.

LLC's that are formed after July 1, 2018, however, are required to file an Initial report--with a fee of \$20.00 per report-- by the end of the third calendar month following the effective date its certificate of organization. It also requires a Triennial report—with the same fee—be filed during the corresponding months of each third calendar year thereafter. An LLC may also file a Statement of Authority (with a filing fee of \$20.00), which will assist other businesses such as the financial industry and insurance industry to identify who is authorized to sign on behalf of the limited liability company.

According to SOS, in 2015 there were 12,849 new LLCs registered (11,250 Domestic and 1,599 Foreign) and in 2016 there were 13,223 new LLC's registered (11,552 Domestic and 1,671 Foreign). Beginning in FY19, these newly formed entities will be required to file an Initial report, the revenue from which is estimated as follows  $12,849$  (newly formed LLC's in 2015) +  $13,223$  (newly formed LLC's in 2016) =  $26,072 / 2 = 13,036$  (average of newly created LLC's per year) \* \$20 (for Initial report) = \$260,720 in recurring revenue for the Initial report filings beginning in FY19. That is the number that appears in the revenue table above. Additionally, beginning in FY 22, these entities will be required to file Triennial reports, which are estimated to generate an additional \$260,720 in recurring revenue each year, resulting in an estimated \$521,440 in recurring revenue for the Initial Reports and the Triennial report filings beginning in FY 22.

As to HB 180's impact on its operating budget, SOS reports the estimated cost for the vendor that maintains the SOS's Business Filing System to implement the module for electronic filing of Initial and Triennial Reports is \$35,000 in a one-time, nonrecurring cost, as shown above in the Estimated Operating Budget Impact table. It also reports an estimated recurring operating budget impact of \$8,474 annually, also reflected in the operating budget table, based on the estimated cost to print and mail out postcard reminder notices as follows:  $13,036 * \$ .65$ .

AGO notes that, although HB 180 authorizes it to maintain actions to enjoin a foreign LLC from doing business in New Mexico, and to be given notice and an opportunity to be heard in proceedings by the district courts to specify the disposition of property held for a charitable purpose by a domestic or foreign entity relative to a merger, interest exchange, conversion or domestication, it contains no appropriation to the Attorney General's Office to maintain such actions or participate in such proceedings. AOC comments that these types of proceedings could also result in an additional fiscal impact on the courts, as well as the provisions impacting the courts in the Revised Act set out below in Other Substantive Issues. The ">" symbol in the estimated operating budget impact table above represents this unknown fiscal impact on the AGO's and the AOC's operating budgets.

## SIGNIFICANT ISSUES

A series of amendments to the LLC Act since its inception may make it more difficult to understand and the Revised Act attempts to facilitate ease of understanding. The Revised Act appears to emphasize the importance of the operating agreement and provides LLCs and their officers an enhanced degree of flexibility in designing its management structure, capital and profit participation schemes, and other matters to facilitate its objectives. Generally, the Revised Act adopts an approach that favors flexibility and contractual arrangements and brings New Mexico more in line with LLC law in Delaware and several other states. HB 180 is largely based on the model act developed by the National Conference of Commissioners on Uniform State Laws, which has been approved and recommended for enactment in all states, with certain deviations to reflect particular circumstances unique to New Mexico. Several states, including Minnesota and Florida, have recently adopted versions of the Revised Act.

AGO raises these issues:

It is not clear how an LLC Act that was formed prior to July 1, 2018, and that has not elected to be subject to the RLLC Act [Revised Act] can be governed by the LLC Act despite the fact that the LLC Act would be repealed, in its entirety, by HB 180.

Both the AGO and the AOC comment on what appears to be a disconnect in HB 180. As AOC presents the issue:

Section 53-19-56 NMSA 1978 in the existing Limited Liability Company Act permits the Attorney General (AG) to maintain an action to recover civil penalties, as well as to restrain a foreign LLC from transacting business in New Mexico. While HB 180, Section 912 permits the AG to maintain an action to enjoin a foreign LLC, the section does not grant the AG the authority to bring an action to recover civil penalties.

## TECHNICAL ISSUES

The title of the bill includes the phrase “PROVIDING PENALTIES”, but there do not appear to be any penalties provided in HB 180.

## OTHER SUBSTANTIVE ISSUES

The AOC outlines other provisions of the Revised Act that impact the courts:

**Section 105(E)**: requiring the court to decide as a matter of law whether a term of an operating agreement is manifestly unreasonable.

**Section 112(F)**: requiring a final judgment of the district court establishing the right of a company to use a previously registered name in New Mexico.

**Section 204**: permitting an aggrieved person to petition the district court when a person required by the Revised Act to sign or deliver a record to the SOS for filing under that Act does not do so.

**Section 210**: permitting a person to petition the district court to compel the filing of a record by the SOS when the SOS refuses to do so. The court may decide the matter in a summary proceeding.

**Section 503**: permits a court, on application by a judgment creditor of a member or transferee, to enter a charging order against the transferable interest of the judgment debtor for the unsatisfied amount of the judgment.

**Section 702(E)**: permits the district court to order judicial supervision of the winding up

of a dissolved limited liability company, including the appointment of a person to wind up the company's activities and affairs.

**Section 706:** permits a dissolved limited liability company to file an application with the district court for a determination of the amount and form of security to be provided for payment of claims. Permits the court to appoint a guardian ad litem to represent all claimants whose identities are unknown.

**Section 710:** permits an LLC to seek judicial review of denial of reinstatement in the district court within 30 days after service of the notice of denial.

**Section 805:** requires a court to enforce the determination of a special litigation committee, upon required findings, to enforce the determination of the committee.

In addition, AOC provides this background concerning the uniform act that would be enacted by HB 180:

The first ULLCA was promulgated in 1996 and adopted by 12 jurisdictions. The ULLCA was revised in 2006 and amended in 2011 and 2013. The amendments were enacted as part of the Harmonization of Business Entity Acts projects and conformed ULLCA language with language of similar provisions in other uniform acts, and made additional changes and updates.

In the Uniform Law Commissioners Prefatory Note to 2011 and 2013 Harmonization Amendments, the commissioners note that the three most significant substantive changes are as follows:

- eliminating the possibility of a shelf LLC (with the attendant, complex provision requiring two filings with the filing office) and providing instead that “[a] limited liability company is formed when the company’s certificate of organization becomes effective and at least one person becomes a member,” Section 201(d);
- replacing the “ordinary care/business judgment rule” standard with the duty to “refrain from engaging in grossly negligent or reckless conduct, willful or intentional misconduct, or knowing violation of law,” Section 409(c);
- recognizing that, when an LLC has only one member, the “pick your partner” concept is inapposite and providing that, in that situation, the foreclosure of a charging order pertains to the entire ownership interest, not just the economic rights, Section 503(f).

Other substantive changes include: (i) providing a narrow exception to the rule that the amendments to the operating agreement control the rights of person dissociated as a members and of persons that had previously become transferees, Section 107(b)(2); (ii) eliminating the requirement that a domestic LLC designate and maintain an in-state office, Section 201; (iii) requiring that the annual report list the name of at least one member if the LLC is member managed and one manager if the LLC is manger-managed, Section 212(a)(4) and (5); and (iv) expressly authorizing a limited liability company to provide advancements to a person entitled to indemnification, Section 408(c).

See, *Uniform Limited Liability Company Act (2006)*, (Last Amended 2013), pp. 5 and 6, [http://www.uniformlaws.org/shared/docs/limited%20liability%20company/ULLCA\\_Final\\_2014\\_2015aug19.pdf](http://www.uniformlaws.org/shared/docs/limited%20liability%20company/ULLCA_Final_2014_2015aug19.pdf)

AOC reports that HB 180 adopts those substantive changes.