**IMPACT OF STATE LAW ON LLCS**

**(By: Judith S. Lambert)**

## III. IMPACT OF STATE LAW ON LLCS

Chapter 608 of the Florida Statutes, (the "Florida Limited Liability Company Act"), provides the statutory basis for Limited Liability Companies (LLCs) in Florida. LLCs are growing in popularity and in 2007, for the first time, the number of newly formed LLCs exceeded the number of newly formed domestic for-profit corporations.[1] The reason for their growing popularity is no secret. LLCs are flexible and share many of the positive attributes of both partnerships and corporations. Members of an LLC enjoy the liability protection afforded shareholders of corporations. Yet, they are able to avoid many of the corporate formalities, and unfavorable tax consequences endured by corporations.[2]

### A. MERGERS AND CONVERSIONS

Florida Statutes section 608.403 states that a LLC may be organized under Chapter 608 for any legal purpose, subject to state statutes and regulations.[3] LLCs may be formed by Articles of Organization with the state. LLCs may also engage in mergers or conversions with other business entities. In simplified terms, a conversion is the act of changing another business entity into an LLC while a merger is the combination of two or more business entities into a single business entity. Chapter 608 of the Florida Statutes lays out the procedures for accomplishing mergers and conversions in sections 608.438 through 608.4404.[4]

I. CONVERSIONS:

a. CONVERTING "ANOTHER BUSINESS ENTITY" TO A LLC:

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[1] Florida Department of State, Division of Corporations, *Yearly Statistics* < http://www.sunbiz.org/corp_stat.html> (accessed March 21, 2008).
[2] *F.S.* §§608.427-608.4229.
[3] *F.S.* §608.403.
[4] *F.S.* §§608.438-608.4404.

Florida Statute section 608.439 allows certain "other business entities" to convert into an LLC, provided they comply with the requirements set forth in Chapter 608.[5] The statute defines an "other business entity" as *a common law or business trust or association; a real estate investment trust; a general partnership, including a limited liability partnership; a limited partnership, including a limited liability limited partnership; or any other domestic or foreign entity that is organized under a governing law or other applicable law, provided such term shall not include a domestic limited liability company*.[6] You may have noticed that corporations were not listed under the statute, but rest assured the legislature does explicitly provide for the conversion of a domestic corporation into a limited liability corporation.[7]

b. CONVERTING A DOMESTIC LLC INTO "ANOTHER BUSINESS ENTITY":

Florida Statute section 608.4401 allows a domestic LLC to convert into *...another business entity organized under the laws of this state or any other state, the United States, a foreign country, or any other foreign jurisdiction.*[8] However, the operating agreement and articles of organization control, so the practitioner should first check for any applicable provisions that may limit the ability of the LLC to convert.

c. REQUIREMENTS FOR CONVERSION:

Regardless of whether you are converting to or from a LLC, the statutes set forth requirements that must be met in order to complete the conversion. The conversion and organization processes are outlined for each type of business entity within the applicable chapters of the Florida Statutes, and you must be sure that you comply with those statutes.[v] Furthermore, if you are dealing with a foreign entity, you must take care to comply with the statutes and regulations set by the foreign jurisdiction.

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[5] *F.S.* §608.439.
[6] *Id.*
[7] *F.S.* §607.1112.
[8] *F.S.* §608.4401.

Florida Statute section 608.439 sets forth the requirements for converting another business entity into a domestic LLC, requiring that you file with the Department of State a properly executed certificate of conversion and articles of organization. *Id*. The certificate of conversion must contain the name of the converting entity, the date of its organization, its jurisdiction, delayed effective date (if applicable), and the name of the LLC to be formed.[9] The Division of Corporations provides a recommended form on its website located at www.sunbiz.org. Both the certificate of conversion and the articles of organization must be approved by the requirements established for the converting entity.

"Another entity" will be converted to an LLC upon the filing of the certificate of conversion or upon the delayed effective date as set forth in the articles.[10] However, *the existence of the limited liability company shall be deemed to have commenced when the other entity commenced its existence in the jurisdiction in which the other entity was first organized*.[11] Since the newly formed LLC is deemed to exist from the time that the original entity commenced its existence, the original entity is not required to dissolve.

Florida Statute 608.4401 is the applicable statute to consult should you wish to convert a domestic LLC to another business entity form.[vii] In order to convert the LLC, you must develop a conversion plan and obtain approval by the members or managers. Section 608.4402 mandates a specific notice procedure that requires written notice be given to all LLC members of any meeting or other action with respect to the approval of a conversion plan.[12] In general, the notice must be given between thirty to sixty days before the meeting or action.[13] The practitioner should always check to see that the articles of organization or operating agreement do not require a greater than majority vote, but generally speaking the conversion plan must be approved by a majority vote of the members. If the LLC is converting to a partnership or limited partnership, then the

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[9] *F.S.* §608.439.
[10] *Id.*
[11] *Id.*
[12] *F.S.* §608.4402.
[13] *Id.*

members must also vote to determine which type of partner they wish to become. The certificate of conversion must meet the aforementioned requirements set forth in Section 608.439(3), and again there are standard forms located on the Division of Corporations website at www.sunbiz.org.

d. WHAT ARE THE EFFECTS OF A CONVERSION?

Florida Statutes section 608.439(5) states that *the conversion of any other entity into a domestic limited liability company shall not affect any obligations or liabilities of the other entity incurred prior to its conversion into a domestic limited liability company or the personal liability of any person incurred prior to such conversion.* Additionally, all rights, privileges and powers that the other entity possessed at the time of conversion vest with the newly formed LLC.[14] All of the property and debts of the converted entity vests in the newly formed LLC.[15]

e. FILING FEES

The state of Florida mandates filing fees to convert an LLC or other business entity, and there are associated fees for organizing the new business entity. The current filing fee for converting an LLC into a domestic profit corporation is $105.00, plus the costs of obtaining certified copies or a certificate of status.[16] The current filing for converting "another business entity" into a Florida LLC is $150.00, plus the costs of a certified copy ($30.00), and a certificate of status ($5.00). The current filing fee for converting a Florida LLC into an "other business entity" is $25.00, plus the costs of a certified copy ($30.00), and a certificate of status ($5.00).

## II. MERGERS:

A merger is the combination of two or more entities into one single entity. Florida Statute section 608.438(2) specifically allows a Florida LLC to merge into one or more LLCs or other business entities, provided the articles of organization and operating

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[14] *F.S.* §608.439(6).
[15] *Id.*
[16] Florida Department of State, Division of Corporations, *Forms* < http://form.sunbiz.org/cor_llc.html> (accessed March 21, 2008).

agreement permit a merger. Domestic partnerships and corporations must comply with the applicable provisions found in Chapters 620 and 607 of the Florida Statutes, while foreign entities must comply with their jurisdictions' regulations.

a. MERGER PLAN

Like the conversion process, a merger requires a plan before it can be set into action. The plan of merger must set forth identifying information of the entities being merged; the name of the surviving or resulting LLC; terms and conditions of the merger; an explanation of how rights and obligations will be merged or distributed; and all statements required by the applicable statutes.[17] The statute also lays out provisions that may be included in the merger plan.

Generally speaking, and unless the operating agreement or articles of organization provide a greater amount, a merger plan for a Florida LLC must be approved by a majority-in-interest vote of the members.[18] The members must be given written notice of any actions or meetings regarding the approval of a merger plan. The notice must comply with the provisions of Florida Statutes section 608.4381, and must be given between 30 to 60 days before the action or meeting takes place.

b. CERTIFICATE OF MERGER

After the merger plan has been approved by the Florida LLC and by all "other business entities" involved, the surviving entity must file a certificate of merger with the Florida Department of State.[19] The certificate of merger must provide statements certifying that the merging entities have approved the merger in accordance with their respective statutes and regulations; written approval of members that will become general partners of the surviving entity (if applicable); the effective date (if it differs from the date of filing); and additional information for surviving entities that will be formed in a foreign jurisdiction. *Id.*

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[17] *F.S.* §608.438.
[18] *F.S.* §608.4381.
[19] *F.S.* §608.4382.

c. WHAT ARE THE EFFECTS OF A MERGER?

Every limited liability company and other business entity which is a party to the merger cease to exist, except for the surviving entity.[20] The LLC takes title to all real estate, property, and assets, while also assuming all responsibilities, obligations, liabilities and debts owed by the merging entities.[21] A merger does not affect the rights of creditors or liens associated with property owned by the merging companies, and it does nothing to interfere with existing actions or pending proceedings of the former entities. *Id.* Individuals of the converting entities, who were personally liable for debts before the merger, remain liable after the merger. *Id.*

d. FILING FEES

The current filing fees for mergers are as follows: $25.00 for each limited liability Company; $35.00 for each Corporation; $52.50 for each Limited Partnership or Limited Liability Partnership; $25.00 for each General Partnership or Limited Liability Partnership; and $25.00 for each Other Business Entity.[ix] Additionally, there is a $30.00 optional cost for a certified copy. *Id.*

**B. SINGLE MEMBER LLC**

Not all states allow for single member limited liability companies, but Florida allows one or more persons to form an LLC.[22] "Person" is defined as any individual or an entity; therefore, a single individual, corporation, partnership, or other legal entity may form a LLC.[23] A single member LLC is treated no differently than a multi-member LLC. It enjoys all of the same liability protection and pass-through tax treatment that is available to a multi-member LLC.

I. LIABILITY

[20] *F.S.* §608.4383.
[21] *Id.*
[22] *F.S.* §§608.405, 608.402.
[23] *F.S.*§608.402(25).

In recent years there have been questions raised as to the liability protection that will be afforded single member LLCs. Much of the controversy has risen as a result of a 2003 Colorado bankruptcy court decision where the court found that a single member LLC in bankruptcy was susceptible to creditors.[24] The judge found that *upon the Debtor's bankruptcy filing, she effectively transferred her membership interest to the estate…Because there are no other members in the LLC, the entire membership interest passed to the bankruptcy estate, and the Trustee has become a "substituted member.*" The court reasoned that the charging order statute was designed to protect other members, and in the case of a single member LLC there are no other members to protect. Florida has yet to follow the Colorado court, but some planners are taking precautions by adding additional members.

II. DISSOLUTION

The state legislature specifically provides a grace period to a single member LLC that no longer has any members. Florida Statute section 608.441 gives the personal representative or legal representative of the last remaining member the right to continue the LLC; and the representative has 90 days to accept membership or assign the right to continue to a designee. If the representative does not act within 90 days, then the LLC will dissolve. These are default rules and the practitioner should check the articles of organization and operating agreement for applicable provisions that may differ.

**C. SPECIAL RULES FOR REGULATED PROFESSIONS**

Chapter 621, the "Professional Service Corporation and Limited Liability Company Act," allows individuals, working within the same licensed or otherwise legally authorized profession, to join together as members of a limited liability company. Florida Statute section 621.03 defines a "professional limited liability company" (PLLC) as a *limited liability company that is organized under this act for the* ***sole and specific purpose*** *of rendering* ***professional service*** *and that has as its members* ***only other professional limited liability companies, professional corporations, or individuals*** *who*

[24] *In re Ashley Albright*, 291 B.R. 538 (Bankr. D. Co. 2003).

*themselves are duly licensed or otherwise legally authorized to render the same professional service as the limited liability company*.[25] Two main points may be taken out of this definition. First, only professionals that render the *same* professional service should form a professional LLC. And second, the LLC should have the *sole and specific purpose* of providing *professional services*. The legislature did provide an exception that allows a PLLC to invest its *funds in real estate, mortgages, stocks, bonds, or any other type of investments, or from owning real or personal property necessary for the rendering of professional services*.[26]

I. WHAT DEFINES A PROFESSIONAL?

Florida Statute 621.03 provides a definition and examples of what is considered to be a "professional service." It states that a "professional service" is one that cannot be performed without first obtaining a license or other legal authorization. Some examples of a professional service are *certified public accountants, public accountants, chiropractic physicians, dentists, osteopathic physicians, physicians and surgeons, doctors of medicine, doctors of dentistry, podiatric physicians, chiropodists, architects, veterinarians, attorneys at law, and life insurance agents.*[27]

II. WHO MAY RENDER PROFESSIONAL SERVICES?

It may seem obvious, but the formation of a PLLC does not extend the right to practice professional services to all employees of the PLLC, and does not eliminate the need to secure a license required by the state.[28] In Parker v. Panama City, the First DCA summarized this idea by stating that "Corporations organized under F.S. Chapter 621, F.S.A., are prohibited from rendering professional services except through their officers, employees and agents who are duly licensed or otherwise legally authorized to render such professional services within this state, and it is provided that the term 'employee' as used in the statute does not include 'clerks, secretaries, bookkeepers, technicians and

[25] *F.S.* §621.03. (emphasis added)
[26] *F.S.* §621.08.
[27] *F.S.* §*621.03.*
[28] *F.S.* §*621.06.*

other assistants who are not usually and ordinarily considered by custom and practice to be rendering professional services to the public for which a license or other legal authorization is required (F.S. § 621.06)".[29] Professionals of all fields should be careful to educate their employees and monitor their employees' performances to prevent them from performing unlicensed activities.

## III. LIMITED LIABILITY FOR MEMBERS

Members of a PLLC do not enjoy the same liability protection that is afforded to shareholders of a nonprofessional Corporation or members of a nonprofessional Limited Liability Company, but they are protected from ordinary business debt incurred by the PLLC.[30] However, individual members may be held liable for any negligent or wrongful acts or misconduct committed by that person, or by any person under that person's direct supervision and control, while rendering professional service on behalf of the corporation or limited liability company to the person for whom such professional services were being rendered.[31] The standard of misconduct is set by the particular industry and its accompanying regulations.[32] So although a member is liable for his or her own actions, with respect to rendering professional services, he or she will not be liable for independent actions taken by other members of the PLLC. In Gershuny, the Florida Supreme Court cited Chapter 621 of the Florida Statutes and ruled that a group of physicians "could be held personally liable in their capacity as physicians only if the negligence or wrongful act was committed by them or by someone under their direct supervision and control. Otherwise, the liability of the physicians is no greater than that of a shareholder-employee of any domestic business corporation." [33]

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[29] Parker v. Panama City, 151 So.2d. 469 (Fla. App. 1963).

[30] Porlick, Poliquin, Samara, Inc. v. Compton, 683 So.2d 545 at 549 (3rd Dist. Ct. App. 1996); see In the Matter of the Florida Bar, 133 So.2d 554 at 557 (Fla. 1961).( The Court in Porlick stated that "[b]ased on the plain language of this statute, we must conclude, as the Florida Supreme Court did, that the Professional Service Corporation Act relieves professional service corporation shareholders of personal liability for the ordinary business debts of the professional service corporation.)

[31] *F.S.* §621.07.

[32] *Id.*

[33] Gershuny v. Martin McFall Messenger Anethesia Professional Ass'n, 539 So.2d 1131 at 1132 (Fla. 1989).

IV. COMPANY LIABILITY

The PLLC may be held liable, up to the full value of the PLLC's property, for the negligent or wrongful acts or misconduct of *officers, agents, members, managers, or employees while they are engaged on behalf of the corporation or limited liability company in the rendering of professional services.*[xx] The PLLC is not liable for personal debts of its individual members, however a judgment creditor may request, and a court of competent jurisdiction may order, a charging order be placed on the debtor-member's distributive share.[34] See section B "Single Member LLC" for discussion of a possible exception.

## D. EXCEPTIONS TO LIMITED LIABILITY

Without question, one of the main advantages of forming an LLC is the personal liability protection afforded to its members. Members, managers, and managing members of a LLC are not personally liable to the LLC or on behalf of the LLC simply by being a member, manager or managing member.[35] However, this protection is not unlimited and the Florida legislature has tempered the protection by providing exceptions to the limitation of liability.

I. Managing Members and Managers:

"Managing members" and "managers" are two separate terms used to describe the managers of a LLC. The distinction between the two terms originates from the way the LLC is structured, which ultimately comes back to the operating agreement. If the LLC is designated to be run by one or more managers, then the managers are deemed "managers."[36] If the LLC is designated any other way, then a manager of the LLC is deemed a "managing member."*Id.* The duties of managers and managing members are set forth in Chapter 608, and the breach of these duties may expose the manager or managing member to liability to the LLC, other members, and third parties.

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[34] *F.S.* §608.433.
[35] *F.S.* §608.4227.
[36] *F.S.* §608.402.

Florida Statute section 608.4228 explains that a manager or managing member may not be held personally liable for damages, unless they breach or violate the duties of a manager or managing member; violate criminal law; derive improper personal benefits; commit willful misconduct;or act in a reckless manner.[37]

II. DUTY OF LOYALTY AND CARE

Florida Statute section 608.4225 provides that *each manager and managing member shall owe a duty of loyalty and a duty of care to the limited liability company and all of the members of the limited liability company.*[38] In Merovich, the Court summarizes the duty of loyalty as requiring managers and managing members to "...(1) account for and hold as trustee "any property, profit, or benefit derived in the conduct or winding up of the limited liability company or derived from a use ... of limited liability company property"; (2) refrain from dealing with the company "on behalf of a party having an interest adverse" to the company; and, (3) refrain from competing with the company in the conduct of company business "before the dissolution" of the company."[39] A manager or managing member must conduct business with good faith and fair dealing, but the statutes clearly state that a manager or managing member does not violate his/her duties simply because that person benefits from managerial actions.[xxv]

The duty of care is limited to refraining from engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law.[xxv] Breach of the aforementioned duties may give rise to criminal or civil liability.[xxv]

III. Piercing the Corporate Veil

In some circumstances, the members of a LLC may be susceptible to a claim for personal liability by setting aside the limited liability protection of the LLC. This setting aside of the limited liability is likened to piercing the corporate veil of a corporation. There is little case law concerning the piercing of the corporate veil of a LLC, but Section

[37] *F.S.* §608.4228.
[38] *F.S.* §608.4225.
[39] Merovich v. Huzenman, 911 So.2d 125 (App. 3 Dist. 2005).

608.701 specifically mandates in considering the personal liability of LLC members that *the court shall apply the case law which interprets the conditions and circumstances under which the corporate veil of a* ***corporation*** *may be pierced under the law of this state*.[40]

## E. CROSSING STATE AND INTERNATIONAL BOUNDARIES

*A foreign limited liability company may not transact business in this state until it obtains a certificate of authority from the Department of State*.[41] A foreign limited liability company is any LLC formed under the laws of any state other than Florida or under the laws of any foreign country or foreign jurisdiction.[42] The legislature does not define business transactions, but Section 608.501 goes on to provide a non-exhaustive list of activities that do not constitute a business transaction. *Id.* Some of those activities include maintaining or defending any proceeding, holding meetings concerning company affairs, selling through independent contractors, obtaining loans, and conducting isolated transactions. *Id.* Other examples of actions that may be taken without formal authorization may be found in corporate case law. [43]

### I. CONSEQUENCES FOR CONDUCTING BUSINESS WITHOUT AUTHORITY

A foreign LLC that conducts business in the state of Florida without a certificate of authority subjects itself to several monetary and non-monetary penalties. Section 608.502 authorizes the Department of State to collect penalties from the foreign LLC, which may include past due fees, penalties, and taxes which would have been due had the LLC obtained proper authorization. [44] Additionally, the Company is liable for a civil penalty of not less than $500 and not more than $1,000 for each year that it transacted business in the state without a certificate.[45] The lack of authorization does not affect the

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[40] *F.S.* §608.701. (emphasis added)
[41] *F.S.* §608.501.
[42] *F.S.* §608.402(12).
[43] *West's F.S.A*. §607.1501.
[44] *F.S.* §608.502.
[45] *Id.*

validity of the LLC's contracts, deeds, obligations, or its right to defend itself in any proceeding, but the unauthorized LLC will not be able to maintain a proceeding in any court until it obtains a certificate of authority.[46]

## II. CERTIFICATE OF AUTHORITY

A foreign LLC that wishes to conduct business in the State of Florida must submit an application to the Department of State.[47] The application must be accompanied by a certificate of existence that has been authenticated, within 90 days by a records official from the foreign jurisdiction. The application must be made using the *forms prescribed and furnished by the Department of State*. The LLC must use a name that satisfies the requirements laid out in 608.406 or obtain and file a fictitious name that meets the requirements and has been approved and adopted by the LLC's managers or managing members.[48] Once the certificate of authority has been granted, the foreign LLC has the same rights and privileges as a domestic LLC.[49] Furthermore, a member, manager, or managing member is not held personally liable simply by failing to obtain authorization.

## III. REGISTERED OFFICE & AGENT

Each foreign LLC is required to continuously keep a registered office and agent in the state of Florida.[50] The registered office may be *the same as any of its places of business*, and the registered agent may be either: *(a) an individual who resides in this state and whose business office is identical with the office; or (b) a foreign or domestic entity authorized to transact business in this state which has a business office identical with the registered office*. *Id*. The registered agent is the company's authorized agent for receipt of *service of process, notice, or demand required or permitted by law to be served on the foreign limited liability company*.[51]

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[46] *Id.*
[47] *F.S.* §608.503.
[48] *F.S.* §608.506.
[49] *F.S.* §608.505.
[50] *F.S.* §608.507.
[51] *F.S.* §608.5101.

In order to change the registered office or agent the foreign LLC must file a statement of change with the Department of State.[52]. This statement must be approved by the members under Section 608.416, unless the agent is simply changing his/her address, then the state only requires that you file the statement of change and notify the foreign LLC. Model statement of change forms are found on the Department of State website at www.sunbiz.org.[53] Should the company or the registered agent wish for the registered agent to resign, then the agent may do so by providing a signed original statement of resignation to the Department of State and mailing a copy to the LLC's principal office.[54] The registered agent may also elect to discontinue the registered office, and both resignations take effect after thirty-one days.

## IV. WITHDRAWAL OF FOREIGN LLC

In order for a foreign LLC to withdraw from the state of Florida it must first obtain a certificate of withdrawal. The foreign LLC can obtain a certificate by filing an application to the Department of State (see forms located at www.sunbiz.org). The application revokes the authority of the registered agent and names the Department of State as the agent for service of process. Once the foreign company has withdrawn, all service made on the Department of State is deemed to be effective for the foreign LLC.

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[52] *F.S.* §608.508.
[53] Florida Department of State, Division of Corporations, *Forms* < http://form.sunbiz.org/pdf/inhs18.pdf> (accessed March 21, 2008).
[54] *F.S.* §608.509.