



Legislative Fiscal Bureau

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Joint Committee on Finance

Paper #343

Filing Requirements for an Annual Report of a Domestic Limited Liability Company (Financial Institutions)

[LFB 2003-05 Budget Summary: Page 173, #4]

CURRENT LAW

A domestic limited liability company (LLC) is an LLC organized under Wisconsin's laws; a foreign LLC is one organized under a law other than the laws of this state. Currently, only foreign LLCs must file an annual report with the Department of Financial Institutions.

GOVERNOR

Modify Chapter 183 of the statutes to require domestic LLCs to file an annual report with DFI.

Under the bill, each domestic LLC would be required to file its initial annual report with DFI during the first calendar quarter of the year following the calendar year in which the LLC's articles of organization became effective. For domestic LLCs in existence on the bill's general effective date, the initial report to DFI would have to be filed during the first calendar quarter of 2004. Thereafter, LLCs would be required to file each annual report during the first calendar quarter of each subsequent year. The bill directs DFI to assess a \$25 filing fee (the filing fee for foreign LLCs is \$65) and provides additional expenditure authority of \$175,000 PR in 2003-04 and \$25,000 PR in 2004-05 to fund development of capabilities to allow the Department to accept the required reports on-line.

The proposal would make other changes as outlined below:

Information Required to be Included in the Filed Annual Report. As noted, under current law as it applies to LLCs, only foreign LLCs must file an annual report with DFI. The bill

would require domestic LLCs to file an annual report with DFI, and, in the report, to include generally the same basic information about the company currently required to be present in a foreign LLC's annual report. Therefore, a domestic LLC would be required to include in its filed report: (a) the name of the LLC; (b) the address of the LLC's registered office and the name of its registered agent at that office in Wisconsin; (c) the address of the LLC's principal office; (d) the name and business address of each manager, if management of the company is vested in one or more managers; (e) the name and address of each member of the LLC; and (f) a brief description of the nature of the LLC's business. As with foreign LLC annual reports, the bill would require information presented in a domestic LLC's annual reports to be current as of the date on which the annual report is executed on behalf of the LLC, with the proviso that the name and business address of each member of the LLC would have to be current as of the close of the LLC's fiscal year immediately prior to the date by which the report is required to be filed with DFI. If an annual report failed to contain the specified information, DFI would be required to promptly notify the company in writing and return the report to it for correction.

Means of Changing the Registered Office or Registered Agent. Current law requires an LLC to continuously maintain a registered office and registered agent in Wisconsin and allows foreign LLCs to change their registered office or registered agent by submitting the new information in the annual report, with the change effective on the date the annual report is filed by DFI. The bill, in creating a requirement for domestic LLCs to file an annual report, would allow the domestic LLC to change its registered office or registered agent by submitting the new information in its annual report.

New Administrative Dissolution and Reinstatement Provisions. The bill would create new administrative dissolution and reinstatement provisions as described below.

DFI would be granted authority to initiate a proceeding to administratively dissolve any LLC that does not deliver the company's complete annual report to the Department within one year after such report is due. If DFI determined that grounds existed for dissolving an LLC stemming from the LLC's failure to file an annual report, the Department would be required to mail the LLC a written notice of the determination addressed to the registered office of the LLC. If this notice were returned to DFI as undeliverable, the Department would have to again mail the notice to the LLC. If the re-mailed notice were returned to DFI, the Department would have to provide the notice by publishing a class two notice in the official state newspaper under the provisions of Chapter 985.

Within 60 days after the date on which the notice was received or the date on which the second class two notice was published, the LLC would be required to correct each ground for dissolution or demonstrate to the reasonable satisfaction of DFI that each ground determined by the Department did not exist. If the LLC failed to meet the 60-day deadline, DFI would be required to administratively dissolve the LLC and enter a notation in its records to reflect each ground for dissolution and the effective date of dissolution. DFI would have to mail the LLC a notice of these facts and a certificate of dissolution. The notice and certificate would have to be in writing and addressed to the registered office of the LLC. The dissolution would be subject to

judicial review. If the mailed notice of facts and certificate of dissolution were returned to DFI as undeliverable, the Department would have to again mail these documents to the LLC. If the re-mailed documents were returned to DFI, the Department would have to provide the notice by publishing a class two notice in the official state newspaper. An LLC's right to exclusive use of its name would terminate on the date of the administrative dissolution.

The bill provides that, if DFI administratively dissolved an LLC for not delivering its annual report, the LLC would be dissolved and its affairs would be wound up, unless the company was subsequently reinstated by DFI or pursuant to judicial review. An LLC that has been administratively dissolved could apply to DFI for reinstatement within 30 days after the date on which the LLC was dissolved. The application would have to include all of the following: (a) the name of the LLC and the date on which it was administratively dissolved; (b) a statement that each ground for dissolution either did not exist or had been cured; and (c) a statement that the LLC had met the requirements outlined in the statutes regarding LLC names and written designations for such names.

DFI would be required to cancel the certificate of dissolution and issue a certificate of reinstatement upon determining that the application contained the information required, that the information was correct, and that all fees and penalties owed by the LLC to the Department had been paid. The certificate of reinstatement would have to state the Department's determination that these criteria had been met and the effective date of reinstatement. The Department would then be required to file the certificate and provide a copy to the LLC or its representative. When the reinstatement became effective, it would relate back to, and take effect as of, the effective date of the administrative dissolution, and the LLC would be allowed to resume carrying on its business as if the administrative dissolution had never occurred.

If DFI denied an LLC's application for reinstatement, it would be required to serve the limited liability company with a written notice of denial explaining each reason for the denial. The denial would be subject to judicial review.

Fiscal Effect of Proposal. DFI estimates that the new filing requirement would result in additional program revenues of \$1,150,000 in 2003-04 and \$2,400,000 in 2004-05. Any additional revenues that are not expended by DFI would lapse to the general fund at the end of each fiscal year. Based on the projected program revenues and additional expenditures (\$175,000 in 2003-04 and \$25,000 in 2004-05) under the bill, the administration has estimated additional lapses to the general fund of \$975,000 in the first year and \$2,375,000 in the second year.

DISCUSSION POINTS

1. As described above, the bill would require LLCs to file annually at the end of the first quarter of the calendar year. [For discussion purposes, "LLC" refers to a domestic LLC unless otherwise noted.] However, the administration has indicated that it intended to require the reports to be due quarterly throughout the year depending on the organization's date of establishment, as that would best comply with DFI's ability to process the reports. Therefore, the administration requests a

modification that would require annual reports to be filed before the end of the calendar quarter in which the anniversary date of the LLC occurs.

2. Authority to form LLCs was first effective January 1, 1994. As part of the 1995-97 biennial budget, the Governor recommended requiring both domestic and foreign LLCs to file annual reports, authorizing administrative dissolution of domestic LLCs and revocation of certificates of registration for foreign LLCs, and establishing filing fees for related documents. The Governor's recommendation was modified when enacted under 1995 Wisconsin Act 27. As a compromise, the recommendation that domestic LLCs file an annual report and the provisions regarding administrative dissolutions were deleted and the initial filing fee was increased from \$90 to \$130, beginning January 1, 1996. The annual reporting requirement, revocations of certifications of registrations, and the \$50 annual fee for foreign LLCs were retained. The \$50 fee has since been raised to \$65.

3. At the end of 2002, a total of 73,955 LLCs were on file with DFI; 17,427 of these companies were new in 2002. By the end of March, 2003, the total number of LLCs had increased to 78,210.

4. Under current law, once an LLC files an initial application with DFI, the only additional filing requirement is in the event of a change in the articles of organization or the name or address of the registered agent. The Department is unable to verify how many LLCs are complying with this requirement. As a result, DFI has no way to ascertain how many LLCs are actually in business at any given time, where they are located, or who their registered agents are.

5. The bill estimates that the new LLC annual filing requirement would result in additional program revenues of \$1,150,000 in 2003-04 and \$2,400,000 in 2004-05. The estimates are based on the Department's projections of the cumulative numbers of LLCs that will be on file with DFI at the end of calendar years 2003 and 2004. However, not all LLCs that have ever filed with DFI are still in business and would submit annual reports to the Department. Therefore, the revenue projections under the bill are overstated. However, due to the lack of more specific information on the number of LLCs currently operating in the state, it is difficult to say by how much.

6. Nonetheless, a downward adjustment in the projected revenue from the proposal is warranted. After reviewing information from DFI on returns of undeliverable mail following a mailing by the Department to registered business entities in 2002, and information from the Small Business Administration on survival rates of new businesses, it appears that the administration's estimates should be reduced by approximately 25% to reflect the fact that some LLCs that have registered with DFI are no longer operating in the state. Based on this adjustment, revenues under the proposal are reestimated at \$860,000 in 2003-04 and \$1,800,000 in 2004-05 (the reestimates are \$290,000 less in the first year and \$600,000 less in the second year than the estimates included in the bill).

7. Even though the reestimated revenue is program revenue, the reestimate would also result in reductions in DFI's estimated year-end lapses to the general fund. The reductions in the

GPR lapses are estimated at the same levels as the program revenue reductions of \$290,000 in the first year and \$600,000 in the second year.

8. It should be noted, that due to the lack of general business research specific to LLCs and a reliable base from which to identify LLCs currently in business in Wisconsin, actual revenues under the proposal could be greater or less than the reestimated figures.

9. The Department believes that the lack of accurate information on LLCs is problematic for a variety of reasons. DFI cites the "name reservation" process as one example of the difficulties that arise from lack of information on which LLCs are currently operating. Business names cannot be duplicated. Without information on whether or not an LLC is still in business, names that were once reserved by an LLC but are not in current use cannot be reused.

10. The Department also argues that the annual reporting requirement would: (a) substantially improve the quality of the records it maintains for the public and for policy-makers; (b) free up space on DFI's computer network; and (c) provide equity between business types, whether formed as corporations or LLCs.

11. The LLC as a business entity has experienced rapid growth since it was first authorized in Wisconsin in 1994. On average, the total number of registered LLCs has increased by 56% annually (from a starting point of 2,074 LLCs registered at the end of 1994 to 73,955 registered LLCs at the end of 2002). If the pattern continues, LLCs will continue to represent a significant component of new business growth in Wisconsin. DFI believes that, under these circumstances, it will become increasingly important for policy-makers and potential new businesses to have access to accurate information on the number of LLCs in business and what kinds of businesses have been successful under the LLC form of organization.

12. The following sections address issues related to the proposed contents of the annual report, the frequency of filing, and the amount of the filing fee.

Content of the Annual Report

13. It has been suggested that requiring the annual report to include the name and address of each member of the LLC would be unnecessary and burdensome. Of the surrounding states that require reports from LLCs, only two have a requirement to include names and addresses of members, and those requirements apply only in the following circumstances: (a) Michigan requires the names and addresses of all members only if the LLC is a professional LLC, which is an LLC formed to render specific professional services and whose name must contain the words "professional limited liability company;" and (b) Illinois requires members' names and addresses only when there are no managers. The administration has indicated that it would not object to deleting from the proposal the requirement to provide in the annual report the names and addresses of all LLC members.

Frequency of Filing

14. It has also been suggested that, in lieu of an annual reporting requirement, a report filed every two years might satisfy the need to update the state's LLC database without imposing the burden of an annual report on LLCs. The Department has expressed concern that, if the trend in new business formations continues to favor the LLC as a top choice for type of organization, a filing frequency greater than one year would quickly render the database inaccurate.

15. Most of Wisconsin's neighboring states (Illinois, Minnesota, and Michigan) have an annual filing requirement for LLCs. Iowa, however, does not require any report beyond the initial filing, and Indiana requires a report every two years. If the filing frequency for LLCs in Wisconsin were reduced, the revenue projections would have to be adjusted accordingly. For example, if the LLC report were required biennially, rather than annually, projected revenues would be reduced by one-half in the second year. [The bill assumes that only half of LLCs would file in the first year but that all LLCs would file in the second year].

Filing Fee

16. Another means of reducing the burden of an annual report would be to reduce the filing fee. Among neighboring states with a reporting requirement, the fees vary considerably. Illinois imposes a \$200 filing fee; Indiana charges \$15; Minnesota's filing fee is \$35; and Michigan generally charges \$15, except that the Michigan fee for a professional LLC is \$50.

17. The actual cost to DFI of processing an annual report is less than \$10 per report. [The exact per unit cost would depend on several factors, including the frequency of filing, the required report content, and the time-period to be used for recovery of DFI's one-time start-up costs.] A filing fee of \$25 would be consistent with the fee currently charged in the case of for-profit corporations. The filing fee for cooperatives and non-profit corporations is \$10.

18. As described above, the program revenue under the Governor's proposal has been reestimated at \$860,000 in 2003-04 and \$1,800,000 in 2004-05, which is \$290,000 less in the first year and \$600,000 less in the second year than the estimates included in the bill. Rather than reducing the program revenue and associated GPR-Earned from the amounts included in the bill, another option would be to increase the filing fee for the LLC annual report in order to avoid the need for reductions from the bill. Based on the assumption that 75% of LLCs on file with DFI would submit an annual report, a \$35 filing fee would result in program revenues of \$1,200,000 in 2003-04 and \$2,520,000 in 2004-05. Compared to the bill, this option would generate an additional \$50,000 in 2003-04 and \$120,000 in 2004-05. Compared to the reestimates of the Governor's proposal, raising the fee to \$35 would result in additional revenues of \$340,000 in the first year and \$720,000 in the second year.

Under this option, the GPR-Earned estimates would be increased by the same amounts as the program revenue. Compared to the bill, estimated GPR-Earned would be increased by \$50,000 in 2002-03 and by \$120,000 in 2004-05. Compared to the reestimate of the Governor's proposal,

GPR-Earned would be increased by \$340,000 in 2002-03 and by \$720,000 in 2004-05.

Effect of Changes to the Proposal on the General Fund

19. As noted, any additional revenues from the proposal not expended by DFI would lapse to the general fund at the end of each fiscal year. Therefore, while the LLC proposal would be funded with program revenue, any alternatives considered in lieu of the proposal would have an effect on the general fund. For example, if the proposal were eliminated, the estimated lapses to the general fund included in the bill of \$975,000 in 2003-04 and \$2,375,000 in 2004-05 would also be eliminated. In general, any alternative that reduced program revenue would reduce the amount of the lapse by the same amount (unless both revenue and expenditure authority were decreased, in which case the lapse would be reduced by the net change in revenue and expenditure authority).

ALTERNATIVES

Reestimation and Technical Correction of Governor's Proposal

1. Approve the Governor's recommendation, with the following modifications.

a. Reestimate the revenues that would be generated under the proposal at \$860,000 in the first year and \$1,800,000 in the second year. As compared to the bill, program revenue would be reduced by \$290,000 in the first year and \$600,000 in the second year, for a total reduction of \$890,000. In addition, the Department's estimated year-end lapses to the general fund would also be reduced by the same amounts.

<u>Alternative 1a</u>	<u>GPR</u>	<u>PR</u>
2003-05 REVENUE (Change to Bill)	- \$890,000	- \$890,000

b. As requested by the administration, require LLC annual reports to be filed before the end of the calendar quarter in which the anniversary date of the domestic LLC occurs, rather than before the end of the first calendar quarter in a year.

Change to Filing Frequency

2. Approve the Governor's proposal as modified under Alternative 1b. However, specify that the report would be required biennially, rather than annually. Estimate revenues to be \$860,000 in 2003-04 and \$900,000 in the 2004-05. As compared to the bill, this alternative would reduce revenues by \$290,000 in the first year and by \$1,500,000 in the second year. The two-year total reduction in program revenue would be \$1,790,000. In addition, the Department's estimated year-end lapses to the general fund would be reduced by the same amounts.

As compared to the modified revenue estimates under Alternative 1a, this alternative would not affect revenue or the lapse to the general fund in the first year. However, both program revenue and the lapse to the general fund would be reduced in the second year by \$900,000.

<u>Alternative 2</u>	<u>GPR</u>	<u>PR</u>
2003-05 REVENUE (Change to Bill)	- \$1,790,000	- \$1,790,000

Change to Filing Fee and Frequency

3. Approve the Governor's request as modified under Alternative 1b. In addition, change the filing fee to \$15, \$20, or \$35. A reduced fee level could be implemented with either an annual or a biennial reporting requirement. The estimated changes to program revenue and to the year-end lapses to the general fund are shown below for the various combinations of filing fee and filing frequency.

<u>Alternative</u>	<u>Fund</u>	<u>2003-05 Fiscal Effect</u>	<u>Change to Reestimated Governor's Proposal</u>	<u>Change to Bill</u>
3a -- Annual Report, \$15 Fee	PR-REV	\$1,600,000	-\$1,060,000	-\$1,950,000
	GPR-REV	1,600,000	-1,060,000	-1,950,000
3b -- Biennial Report, \$15 Fee	PR-REV	\$1,060,000	-\$1,600,000	-\$2,490,000
	GPR-REV	1,060,000	-1,600,000	-2,490,000
3c -- Annual Report, \$20 Fee	PR-REV	\$2,130,000	-\$530,000	-\$1,420,000
	GPR-REV	2,130,000	-530,000	-1,420,000
3d -- Biennial Report, \$20 Fee	PR-REV	\$1,410,000	-\$1,250,000	-\$2,140,000
	GPR-REV	1,410,000	-1,250,000	-2,140,000
3e -- Annual Report, \$35 Fee	PR-REV	\$3,720,000	\$1,060,000	\$170,000
	GPR-REV	3,720,000	1,060,000	170,000

Change to Required Content of Report

4. In addition to any of the alternatives shown above, eliminate the proposed requirement that the report include the name and address of each member of the LLC. Under this alternative, there would be no change to the revenues estimated under another alternative.

Maintain Current Law

5. Delete provision. Reduce program revenue by \$1,150,000 in 2003-04 and \$2,400,000 in 2004-05 and eliminate expenditure authority of \$175,000 PR in the first year and

\$25,000 PR in the second year.

In addition, compared to the bill, reduce the estimated year-end lapses to the general fund by \$975,000 in 2003-04 and \$2,375,000 in 2004-05. Compared to the modified lapse estimates under Alternative 1a, this alternative would reduce the lapses by \$685,000 in the first year and \$1,775,000 in the second year.

<u>Alternative 5</u>	<u>GPR</u>	<u>PR</u>
2003-05 REVENUE (Change to Bill)	- \$3,350,000	- \$3,550,000
2003-05 FUNDING (Change to Bill)	\$0	- \$200,000

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