

SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based only on the provisions contained in the legislation as of the latest date listed below.)

Date: March 3, 1998 Revised: _____

Subject: Limited Liability Companies

	<u>Analyst</u>	<u>Staff Director</u>	<u>Reference</u>	<u>Action</u>
1.	<u>Maclure</u>	<u>Austin</u>	<u>CM</u>	<u>Favorable</u>
2.	_____	_____	<u>WM</u>	_____
3.	_____	_____	_____	_____
4.	_____	_____	_____	_____
5.	_____	_____	_____	_____

I. Summary:

This bill provides that a limited liability company (LLC) formed under chapter 608 of the Florida Statutes or qualified to do business in Florida as a foreign LLC will not be subject to Florida's corporate income tax if the LLC is classified as a partnership for federal income tax purposes.

This bill amends the following sections of the Florida Statutes: 220.02, 220.03, 220.13, 608.406, and 608.471.

II. Present Situation:

A limited liability company (LLC) is an entity with characteristics reflective of both a corporation and a partnership. For legal purposes, an LLC is treated like a corporation and therefore affords its members certain protections from liability. For federal income tax purposes, however, an LLC may be classified as a partnership, under which the earnings or losses of the LLC are passed through to the members, rather than treating the LLC as a separate taxable entity.

The Florida Limited Liability Company Act, ss. 608.401-608.514, F.S., governs the creation and operation of LLCs in this state. Two or more persons may form an LLC by executing and filing articles of organization with the Department of State (ss. 608.405 and 608.407, F.S.). Among other elements, the act provides that, generally, neither the members nor the managers of an LLC are liable for a debt of the LLC (s. 608.436, F.S.). A foreign LLC may register its name with the department by filing an application that includes a certificate or similar document illustrating that the LLC is in good standing under the laws of the jurisdiction where it is organized (s. 608.4062, F.S.).

Section 608.406, F.S., requires that the words “limited company,” or the abbreviation “L.C.,” must be the last words in the name of any LLC formed under ch. 608, F.S. Omission of the words or the abbreviation in using an LLC name renders a person who participates in the omission, or who knowingly acquiesces in it, responsible for liability caused by the omission (s. 608.406(5), F.S.).

Under its corporate income tax code, ch. 220, F.S., Florida levies a tax of 5.5 percent on the taxpayer’s net income for the taxable year (s. 220.11, F.S.). The stated intent of the code is to impose a tax on all corporations and other artificial entities that derive from the state attributes not inherent in natural persons, such as perpetual life, transferable ownership, and limited liability for all owners (s. 220.02(1), F.S.). LLCs are specifically subject to this tax (*id.* and s. 608.471, F.S.). For federal income tax purposes, however, LLCs may be treated as partnerships, which are not subject to federal income tax. Under Florida law, partnerships of any type are specifically excluded from the definition of a corporation and are not subject to the state’s corporate income tax (s. 220.03(1)(e), F.S.).

Under the Florida corporate income tax code, a taxpayer’s net income for state tax purposes is based on the taxpayer’s adjusted federal income (s. 220.12, F.S.). In the case of an LLC, adjusted federal income means “taxable income determined *as if* such limited liability company were required to file or had filed a federal corporate income tax return under the Internal Revenue Code” (s. 220.13(2)(j), F.S.)(emphasis provided).

The U.S. Internal Revenue Service (IRS) first ruled in 1988 that under certain conditions an LLC could qualify as a partnership for purposes of the federal income tax. In determining whether an LLC was to be classified as a partnership, and therefore entitled to the pass-through tax treatment, or classified as an association taxable as a corporation, the IRS examined the nature of an organization, for example by analyzing the LLC’s articles of organization. (See, e.g., Rev. Rul. 93-53, 1993-2 C.B. 312, holding that a Florida LLC which had associates, an objective to carry on business and divide the gains from such business, centralized management, and limited liability could still be classified as a partnership because it did not possess other characteristics of a corporation, such as continuity of life and free transferability of interests.) Recently, the IRS issued new regulations allowing an LLC to elect its federal tax classification on a special tax form (61 Fed. Reg. 66584 (1996)).

Under s. 608.452, F.S., the fees relating to the creation and operation of LLCs are as follows:

- \$52.50, for furnishing a certified copy;
- \$250.00, for filing original articles of organization or articles of revocation of dissolution;
- \$250.00, for filing a supplemental affidavit declaring the amount of capital contributions of the members when there is an increase in capital contribution beyond the anticipated amount;
- \$100.00, for filing an annual report;

- \$500.00, for filing an application for reinstatement after an administrative or judicial dissolution;
- \$35.00, for filing a certificate designating a registered agent or changing a registered agent;
- \$87.50, for filing a registered agent's statement of registration from an active limited liability company;
- \$35.00, for filing a registered agent's statement of resignation from a dissolved LLC;
- \$52.50, for filing any other LLC document; and
- \$88.75, as a supplemental corporate fee under s. 607.193, F.S.

There are currently 5,867 active LLCs registered with the Florida Department of State, including both domestic LLCs and foreign LLCs authorized to conduct business in Florida.

III. Effect of Proposed Changes:

This bill provides that a limited liability company (LLC) classified as a partnership for federal income tax purposes and formed under ch. 608, F.S., or qualified to do business in this state as a foreign LLC is not subject to Florida's corporate income tax. In particular, the bill:

- Amends s. 220.02(1), F.S., relating to the legislative intent for the Florida corporate income tax code, to specify the intent that such LLCs not be subject to the tax and to specify that the code is not intended to tax any natural person who engages in business in this state as a member or manager of an LLC that is classified as a partnership for federal income tax purposes;
- Amends s. 220.03(1), F.S., relating to definitions under the corporate income tax code, to exclude LLCs that are taxable as partnerships for federal income tax purposes from the definition of the term "corporation";
- Amends s. 220.13(2), F.S., relating to the definition of "taxable income" under the corporate income tax code, to exclude the income of specified LLCs from such definition; and
- Amends s. 608.471, F.S., relating to the tax on income of LLCs, to provide that an eligible LLC's income is not subject to Florida's corporate income tax. This section is further amended to provide that an eligible LLC shall be classified as a partnership for purposes of the state corporate income tax code or shall be classified identically to its classification for federal income tax purposes.

The bill also amends s. 608.406, F.S., relating to an LLC's name, to provide that the words "limited liability company," or the abbreviation "L.L.C.," may be used at the end of an LLC's name as an alternative to the words "limited company" or the abbreviation "L.C."

The bill does not revise the filing fees applicable to LLCs.

The bill provides that the act shall take effect July 1, 1998.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

This bill has not been reviewed by the Revenue Impact Conference. However, the conference reviewed the provisions of a similar bill filed in the House of Representatives during the 1997 session and estimated that relieving eligible limited liability companies (LLCs) from state corporate income tax would result in a fiscal year 1997-98 general revenue loss of \$5.7 million and a recurring general revenue loss of \$4.1 million.

B. Private Sector Impact:

LLCs that are classified as partnerships for federal income tax purposes would not be subject to Florida's corporate income tax. The LLC may become a more financially attractive form of business organization.

C. Government Sector Impact:

To the extent removing LLCs from corporate tax liability increases the popularity of this form of business organization, the Department of State may experience a change in the current mix of business filings it receives and processes. However, the department does not anticipate that the bill will have a fiscal impact on its operations.

The Department of Revenue's workload, as it currently relates to administration of corporate income tax for LLCs, may ultimately be reduced as a result of eligible LLCs becoming exempt from such tax under this measure.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Amendments:

None.

This Senate staff analysis does not reflect the intent or official position of the bill's sponsor or the Florida Senate.
