

HB

403

HB 403

Tape #

34

Date

4/24

STATE OF ALASKA

DEPARTMENT OF COMMERCE

DIVISION OF BANKING, SECURITIES, SMALL LOANS & CORPORATIONS

JAY S. HAMMOND, Governor

POUCH D - JUNEAU 99801

May 27, 1975

Honorable Senator Jalmar M. Kerttula
Chairman Senate Commerce Committee
and
Honorable Representative Robert Bradley
Chairman House Commerce Committee
Pouch V
State Capitol
Juneau, Alaska 99811

Dear Senator Kerttula and Representative Bradley:

Re: Limited Liability Companies Senate Bill 354 and
House Bill 403

If you are still considering the above bills you might want to add the enclosed letter to your files. It does not change the views I expressed in my earlier letter to you but simply adds to the explanation of the disuse of similar type associations in the State of Michigan.

Sincerely,

Miles S. Schlosberg
Miles S. Schlosberg
Director

MSS/ws

Enclosure

cc/ Robert Hartig Esq.
Senator Mike Colletta

*Should have
sent meeting
on this next
YEAR*

Miles

LAURENT K. VARNUM
CARL J. RIDDERING
OF COUNSEL

LAW OFFICES OF
VARNUM, RIDDERING, WIERENGO & CHRISTENSON
666 OLD KENT BUILDING
GRAND RAPIDS, MICHIGAN 49502

JOHN L. WIERENGO, JR.
CLIFFORD C. CHRISTENSON
F. WILLIAM HUTCHINSON
JAMES N. DEBOER, JR.
OORDON B. BOOZER
EUGENE ALREMA
PETER ARMSTRONG
ROBERT J. ELEVELD
CARL E. VER BEER
JON F. DEWITT
DONALD L. JOHNSON
DANIEL C. HOLMOEK
GARY P. SKINNER
CARL R. FLEETWOOD

DIRK HOFFIUS
J. TERRY MORAN
THOMAS J. HEIDEN
THOMAS J. MULDER
THOMAS J. BARNES
JEFFREY L. SCHAD
STEPHEN R. SAWYER

TELEPHONE 616 459-4186

RECEIVED

MAY 20 1975 May 19, 1975

DEPARTMENT OF COMMERCE
DIVISION OF BANKING
SECURITIES AND LOANS

Mr. Miles S. Schlosberg
Director of Division of Banking
Department of Commerce
State Office Building
Pouch D
Juneau, Alaska 99801

Dear Mr. Schlosberg:

It has come to our attention that you have contacted various Michigan law firms regarding the use of Michigan partnership associations. As we understand your inquiry, you generally desire information as to why there has been a lack of use of this type of entity. In this connection, we would like to offer our views on the subject.

As near as we can determine, the Michigan partnership association entity was utilized to some considerable extent prior to the 1930's. In 1931, Michigan adopted a general corporation act which was reasonably broad for its time and resolved many of the complexities of the prior law. Prior to 1931, Michigan had many different corporate acts for different business activities which were rather complex and restrictive. The partnership association was less involved and less complex. We believe that the phasing out of the use of the partnership association in the 1930's may have been attributable in part to the simplification of the State's corporate laws in 1931.

In addition, it appears from the holdings of various tax cases and from the 1939 Internal Revenue Code and regulations promulgated pursuant thereto that a partnership association was taxed as a corporation prior to the 1954 Code. The regulations under the 1954 Internal Revenue Code were substantially changed; and therefore, it is possible that such an entity could qualify, if properly structured, as a partnership for federal income tax purposes. The Internal Revenue Service has ruled that a limited partnership association formed under Ohio law, as structured, possessed more corporate than non-corporate attributes; and thus, was an association taxable

Mr. Miles S. Schlosberg
May 19, 1975
Page Two

as a corporation for federal income tax purposes. However, there have been no published rulings to our knowledge by the Internal Revenue Service relating to a partnership association that was taxable as a partnership for federal income tax purposes. Hence, the somewhat undefined status of partnership associations for federal tax purposes may have contributed to limited use of the partnership association entity.

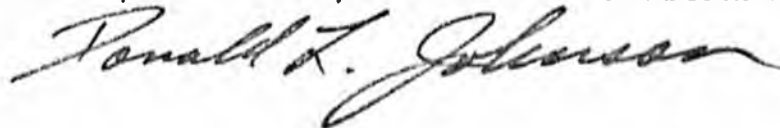
Finally, we think it is worthy to note that the limited partnership has in the past two decades or so become perhaps the most viable entity for use by persons desiring to limit their personal liability and yet receive the benefits of the pass through of tax losses. Moreover, limited partnerships were frequently structured with a shell corporation serving as the sole general partner in an effort to achieve total limited liability for partnership debts. This latter technique has been under recent attack by the Internal Revenue Service. In 1972, the Service issued notice that it would no longer rule on the validity of the limited partnership with a corporation as a sole general partner unless the corporation had a certain specified net worth. In 1974, the Service further declared that general partners had to have at least a 1% interest in all items of partnership income and expense. As a result of the Internal Revenue Service's position, limited partnerships have become somewhat less attractive to some practitioners and investors, because it is difficult to structure a limited partnership which will achieve full limited liability and at the same time assure treatment as a partnership for federal income tax purposes.

In summary, it is our view that the changes in the Michigan corporate laws in the early 1930's, the uncertainty of the tax treatment accorded a Michigan partnership association and the attractiveness of a limited partnership may well be some of the principal reasons that partnership associations have not been utilized to any great extent in recent years.

If you should desire further information concerning our views on this matter, please do not hesitate to contact the undersigned at any time.

Very truly yours,

VARNUM, RIDDERING, WIERENGO & CHRISTENSON



DLJ:ps

Department of the Treasury

135-7

Phone Contact: Philip M. Corn
Phone Number: 202-964-3553

Internal Revenue Service
Washington, DC 20224

Date: MAY 12 1975 | In reply refer to:
T:I:I:2:2



*Where the
request from my
letter*

Mr. Frank M. Burke, Jr.
Peat, Marwick, Mitchell & Co.
Suite 1500
2001 Bryan Tower
Dallas, Texas 75201

Dear Mr. Burke:

This is in response to your letter of May 1, 1975, as amended by your letter of May 2, 1975, written on behalf of the Legislature of the State of Alaska. Your inquiry concerns the manner in which the Internal Revenue Service will classify entities formed pursuant to the Alaska Limited Liability Company Act ("Act") for Federal income tax purposes if the Act is enacted into law. The Act is now pending in the Alaska Legislature as Senate Bill 354 and House Bill 403.

In the event the Act is enacted into law, the Service will consider a request for a ruling, submitted in accordance with applicable procedures, as to the classification of an entity formed pursuant to the Act. In considering any such ruling request, the Service will apply section 7701 of the Internal Revenue Code of 1954, the regulations thereunder, and any other pertinent provisions of the Code and regulations.

Sincerely yours,

Billy M. Hargrett

Chief, Individual Income Tax Branch

*Who did I send letter
to? What is a copy of it?
Kun*

COLE, HARTIG, RHODES, NORMAN, MAHONEY, & GOLTZ

A PROFESSIONAL CORPORATION

ATTORNEYS AT LAW

SUITE 201

717 K STREET

ANCHORAGE, ALASKA 99501

(907) 274-3576

HOYT M. COLE
ROBERT L. HARTIG
JAMES O. RHODES
JOHN K. NORMAN
ROBERT J. MAHONEY
KEITH A. GOLTZ
BERNARD J. DOUGHERTY

May 16, 1975

File

Honorable Bob Bradley, Chairman
House Commerce Committee
Alaska State House of Representatives
Pouch V
State Capital Building
Juneau, AK 99811

Re: Limited Liability Company Act
House Bill 403

Dear Representative Bradley:

Enclosed is a response from the Internal Revenue Service regarding House Bill 403.

As stated in the IRS letter, they will consider a ruling to classify an entity formed under the proposed Limited Liability Company Act under the provisions of Internal Revenue Code Sec. 7701 and the regulations under that section.

The regulations under Sec. 7701 present the four characteristics used to classify an entity as a corporation or a partnership for tax purposes. They are:

1. Limited Liability.
2. Centralization of Management.
- ✓ 3. Continuity of Life.
- ✓ 4. Free Transferability of Interests.

As explained in my testimony before the House Commerce Committee on April 24, 1975, the Limited Liability Company Act as drafted, would insure the lack of corporate characteristics three and four, and if the members choose to retain management in themselves, the Limited Liability Company would also lack the

Bob Bradley, Chairman
Re: House Bill 403
Limited Liability Company Act
May 16, 1975
Letter
Page 2

corporate characteristic of Centralization of Management.
Thus, under the provisions of Treasury Regulations Sec.
301.7701, the Limited Liability Company should be classified
as a partnership for Federal tax purposes.

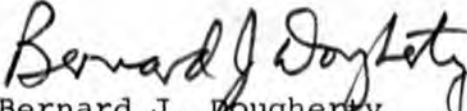
Thank you for your attention to this matter and if I can
be of any further help please contact me.

Kindest regards.

Very truly yours,

COLE, HARTIG, RHODES, NORMAN,
MAHONEY & GOLTZ

By


Bernard J. Dougherty

BJD:mg
Enclosure

PEAT, MARWICK, MITCHELL & Co.

CERTIFIED PUBLIC ACCOUNTANTS

SUITE 1500, 2001 BRYAN TOWER

DALLAS, TEXAS 75201

May 14, 1975

*File with
HB 403*

PRIVATE

The Honorable Bob Bradley
Chairman, Commerce Committee
Alaska House of Representatives
Pouch V
Juneau, Alaska 99811

Dear Representative Bradley:

Enclosed is the original of an information letter from the National Office of the Internal Revenue Service setting forth the procedure which would be followed by the Internal Revenue Service in considering the issuance of rulings with respect to the proposed Limited Liability Company Act (House Bill 403 and Senate Bill 354) presently pending before the Alaska Legislature.

This letter from the Internal Revenue Service is in response to your letter dated April 30, 1975, and your telegram dated May 6, 1975, together with the letter of Senator Jalmar Kerttula dated April 30, 1975, requesting such letter. The undersigned and Mr. Bernard Dougherty met with Mr. Phil Corn of the Internal Revenue Service in Washington, D.C. on May 2, 1975, to formally present the request of the Alaska Legislature for this letter.

I trust the enclosed letter is satisfactory for your purposes. If you have any questions, please call the undersigned or Mr. Dougherty.

Yours very truly,

PEAT, MARWICK, MITCHELL & CO.

F. M. Burke, Jr.
Frank M. Burke, Jr., Partner

FMB: jc

Encl.

cc: The Honorable Richard K. Urion
Mr. Miles S. Schlosberg
Mr. Bob Hartig

Department of the Treasury

Phone Contact: Philip M. Corn
Phone Number: 202-964-3553

Internal Revenue Service
Washington, DC 20224

Date: **MAY 12 1975** | In reply refer to:
T:I:I:2:2



▷ Mr. Frank M. Burke, Jr.
Peat, Marwick, Mitchell & Co.
Suite 1500
2001 Bryan Tower
Dallas, Texas 75201

Dear Mr. Burke:

This is in response to your letter of May 1, 1975, as amended by your letter of May 2, 1975, written on behalf of the Legislature of the State of Alaska. Your inquiry concerns the manner in which the Internal Revenue Service will classify entities formed pursuant to the Alaska Limited Liability Company Act ("Act") for Federal income tax purposes if the Act is enacted into law. The Act is now pending in the Alaska Legislature as Senate Bill 354 and House Bill 403.

In the event the Act is enacted into law, the Service will consider a request for a ruling, submitted in accordance with applicable procedures, as to the classification of an entity formed pursuant to the Act. In considering any such ruling request, the Service will apply section 7701 of the Internal Revenue Code of 1954, the regulations thereunder, and any other pertinent provisions of the Code and regulations.

Sincerely yours,

A handwritten signature in cursive script that reads "Billy M. Hargett".

Chief, Individual Income Tax Branch

STATE OF ALASKA

DEPARTMENT OF COMMERCE

DIVISION OF BANKING, SECURITIES, SMALL LOANS & CORPORATIONS

JAY S. HAMMOND, Governor

POUCH D—JUNEAU 99801

May 5, 1975

The Honorable Robert Bradley
Chairman of the House Commerce Committee
Pouch V
State Capitol
Juneau, Alaska 99801

Dear Representative Bradley:

Re: House Bill No. 403

During my testimony on April 24, on House Bill No. 403 concerning limited liability companies I stated that it was the position of the Department of Commerce that the bill did not appear bad but that several issues should be considered before the bill was passed:

1. Why had the State of Pennsylvania repealed similar legislation and why were statutes providing for similar organizations largely unused in the three states in which they currently existed, Ohio, Michigan and New Jersey?
2. How would the Internal Revenue Service tax limited liability companies created under the bill.

I have spoken to tax lawyers in Ohio and Pennsylvania concerning Question 1. The reason that their laws are in disuse or repealed is because organizations set up thereunder have been treated as corporations and denied partnership tax treatment by the Internal Revenue Service. The legislation in Michigan and New Jersey is very similar in its salient tax respects and I have no reason to doubt that organizations set up under the Michigan or New Jersey law will be treated similarly. However, House Bill No. 403 differs from the laws of the four latter states in that the other states require centralized management, i.e. the election of Boards of Directors and a General Manager, whereas HB 403 does not require centralized management. Centralized management is one of the four factors the Internal Revenue Service considers in determining whether or not an organization should be taxed as a corporation or partnership. It is likely that organizations set up under HB 403, lacking central management, would not be taxed as corporations.

The answer to question number 2 will hopefully be obtained by you from the Internal Revenue Service. The lawyers I spoke to were not

May 5, 1975

inclined to speculate as to tax treatment under HB 403 except to agree that the absence of centralized management distinguished HB 403 and made it more likely that the IRS would accord HB 403 type organizations partnership tax status.

If HB 403 is passed and limited liability companies are accorded partnership tax status by the IRS then Alaska would have pioneered a new and very useful business organization. I submitted the intradepartmental comment sheet because we found numerous minor and technical difficulties. The bill's proponents, Messrs. Hartig and Dougherty have met with Mr. Ladwig of this division in an attempt to resolve these problems. We will appreciate your giving us the opportunity to comment upon any revised bill that results. Based on the foregoing we respectfully change our position from "not in favor" to "in favor".

Yours truly,



Miles S. Schlosberg
Director

MSS:kb

cc Langhorne A. Motley
Commissioner of Commerce
Robert Hartig
Bernard Dougherty

ADDITIONAL COMMENTS ON HB 403

(Supplement to Ladwig's
comments of April 17, 1975.) *WJS*

Why did Pennsylvania repeal in 1966 and why has New Jersey let it become dormant.

Will it really be taxed as a partnership. Wouldn't it be more efficient to have an IRS opinion first if it is at all possible. However this is a legislator's concern for efficiency, not mine. Has the IRS route been explored?

It would be wasteful to gear up our Division to handle this new creation unless the IRS deaches it as a partnership.

TO: Banking

DATE: April 17, 1975

(~~SENATE~~ - HOUSE) BILL 403

RE: An Act relating to limited liability companies.

Check One:

1. TOP PRIORITY - in favor of. _____
2. FAVOR - in favor of, but not top priority. _____
3. OK - no definite stand. _____
4. NOT IN FAVOR - _____ X _____
5. TOP PRIORITY - "Strongly Opposed" _____
6. BILL DOES NOT PERTAIN TO DIVISION _____

COMMENTS: (Justification must be stated for the above line checked - continue on another page if needed.)

This writer is not in favor of the proposed bill as written for the following reasons:

1. Assuming the responsibility for administration is delegated to the Division of Banking, Securities, Small Loans & Corporations, it will have a fiscal impact upon this Division. Fiscal note attached.
2. Page 2, lines 10 and 11. To operate in jurisdictions other than Alaska may require registration in those jurisdictions similar to that required by this State of foreign corporations. Proof of existence may be required. This bill does not provide for a fee for providing certified copies of documents; or the documents themselves.
3. Page 3, line 27. The term person is defined in this bill; however no provision is made that individuals wishing to form such a company must be at least of "legal age".

(continued)

Writer's Signature: [Signature]
Writer's Title: [Title]
(DEADLINE 24 hours)

13. Page 11, line 9. Proof should be required that the company has completed its affairs before a certificate of dissolution is issued, i.e. articles of dissolution.
14. Page 11, line 13. The accounts and affairs should be settled before dissolution and be a condition precedent to issuing any certificate of dissolution other than a certificate issued by reason of involuntary dissolution.
15. Provisions should be made for an annual report to accompany the tax to allow the Commissioner to determine
 - (a) that no capital contributions have been made other than those by filed amendment and the tax thereon has been paid.
 - (b) that the company has continued to maintain the same registered agent as that of record.
16. Provisions should be made for a registered agent to resign and a new one appointed and/or changing the registered office.
17. Consideration should be given to providing limited liability companies of other jurisdictions the means to do business in Alaska.

III. ANALYSIS (See Fiscal Note Preparation Instructions, Section III)

FY 76

FY 77-80

100 - 2 positions @ 340 + 18% benefits

Assumed 5% inflation

300 - rental expense, postage, printing, xerox, etc.

400 - stationery & office supplies

500 - desks, chairs, typewriters, file cabinets

IV. ATTACHMENTS

V. DATE: 4/13/75

PREPARED BY: William W. Ladwin

Original: Legislative Finance
cc: Budget and Management
Prime Sponsor (First Legislator Named)

HB 403

BERNARD J. DOUGHERTY
ATTORNEY AT LAW

COLE, HARTIG, RHODES, NORMAN,
MAHONEY & GOLTZ
A PROFESSIONAL CORPORATION

MEMORANDUM

717 K STREET, SUITE 201
ANCHORAGE, ALASKA 99501

TELEPHONE
(907) 274-3576

LIMITED LIABILITY COMPANY

The limited liability company has predecessors in New Jersey, Pennsylvania, Michigan and Ohio. In New Jersey and Ohio it was known as a "limited partnership association" and in Pennsylvania and Michigan as a "partnership association".

The business entity which we will now call the limited liability company had its origins in the third quarter of the 19th century. It was adopted in Pennsylvania in 1874, in Michigan in 1877, in New Jersey in 1880, and in Ohio in 1881. No other states have used this form of business entity.

The reason for its creation seems to be the particularly restrictive corporation statutes common in the late part of the 19th century. At that time in the development of the corporate entity, the restrictions in some states included the limitation of business to one state, the limitation of the corporation's business to a sole purpose stated in the Articles of Incorporation and various similar confining requirements. In the early days of the development of the corporation, the case law also was extremely restrictive on what a corporation could do and how it could do it, because of the roots in the English system that a corporation, being chartered by the Crown, was authorized to do only what the Crown specifically authorized it to do.

In the early 20th century, these restrictions on corporate activity were greatly reduced and have continued to be reduced through the introduction of the Delaware corporate statute and the Model Business Corporation Act, upon which many states have based their corporation statutes. These statutes gave much greater freedom to the shareholders and the board of directors to structure the activities of the corporation to meet their particular needs. This has especially been true in the close or closely held corporation which most often is a family corporation. Indeed, some states have adopted statutes which govern the activity of such close corporations and give them wide latitude in arranging their affairs. As these new corporate statutes were adopted by the various states and the case law governing the activities of corporations began to be less restrictive, the vehicle of the limited partnership association or partnership association fell in to disuse.

In introducing the Limited Liability Company Act in the State of Alaska, it is our desire to provide to investors, and particularly real estate investors, the opportunity to utilize this new form of business entity to conduct their business affairs with less expense and fewer restrictions.

The Ohio statute proves to be not usable for these objectives because of its preclusion of dealing in real estate

from the uses of the Ohio Limited Partnership Association, (Ohio Rev. Stats. §1783.01).

Also, the statutes in the other states are substantially more restrictive than the Alaska legislation being introduced and thus provide a less useful vehicle for conduct of a business. For example, the New Jersey statute (NJ Stats. Ann. §42.3-1) requires that the principal place of business of a New Jersey limited partnership association must be established and maintained within the State of New Jersey. The Ohio and Michigan statutes, though a little less restrictive, still require that that organization shall have its principal office or principal place of business within the state. The Pennsylvania statute was repealed in 1966, except as to professions which are not permitted to incorporate in the state.

The Alaska proposed legislation does away with this requirement as to the principal office or principal place of business. The reason for this is the desire to draw to the state investors interested in organizing under the Alaska Limited Liability Company Act for business or investment in other states as well as the State of Alaska. The legislation requires a registered agent in the state which would always insure a resident on whom process can be served in suit against the limited liability company.

The legislation proposed would provide a good amount of revenue each year to the state as there are provisions in the proposed legislation for the following fees:

1. A filing fee upon formation of the Limited Liability Company, which is based on capital invested upon a sliding scale to a maximum of \$1,000;
2. An annual fee of \$100;
3. A filing fee for amendment to the Certificate of Organization of \$25.00; and
4. A filing fee of \$25.00 upon dissolution.

It is suggested that this form of business entity will draw a substantial number of investors from other states who, up to this time, have used the limited partnership, corporation or joint venture vehicle for their investments.

In the first ten months of 1974, approximately 1,300 limited partnerships were filed in the State of Texas, which requires a filing of the limited partnership within the state. In Texas this is used as a revenue measure and there is a requirement of a filing fee which rapidly reaches the maximum fee of \$2,500 at capital contributed of \$500,000. This figure would not at all be uncommon in the real estate market of today.

It is estimated that in excess of half of these limited partnerships would be drawn to use the Limited Liability Company authorized by the proposed legislation in the

State of Alaska to conduct their business or to direct their investments, thus providing this increased revenue for the State. This figure is only for the State of Texas and it is suggested that this legislation would be attractive to investors of all states and may substantially contributed to the revenue of our state.

In addition, it is hoped that in drawing investors to the state for the purpose of utilizing our Limited Liability Company Act as a vehicle for investment in other states, such investors will also use the device as an investment entity in our state, thus providing increased work for real estate personnel, title companies, and all those persons who assist in transactions concerning real estate. In addition, it will be necessary for each limited liability company to establish and maintain a registered agent in the state and it will be necessary for the state to employ a number of additional persons to file and administer the limited liability companies.

The provisions of the act enable the persons forming a limited liability company to provide for management of the limited liability company either by the members or by a manager or managers elected by the members of the limited liability company. The voting power of the members is to be in proportion to their investment in the capital of the company. As with a corporation, the liability of the limited liability

company is to be limited to assets of the company. A member would have a liability not to exceed his contribution to the company or any amount which he is committed to contribute but has not as yet contributed. Why would this vehicle be used rather than a limited partnership? Because it combines the attractive characteristics of a corporation with the attractive characteristics of a partnership.

It is hoped that in submitting a request for a private ruling from the Internal Revenue Service of the United States Treasury Department, a limited liability company could obtain partnership classification for tax purposes.

There are four characteristics in distinguishing between partnership classification and classification and taxation as an association or corporation for purposes of the Internal Revenue Code. These are: (1) centralization of management; (2) continuity of life; (3) free transferability of interests; and (4) limited liability.

In order to be taxed as an association, an entity must have more corporate characteristics than partnership characteristics. A similar problem with regard to taxation is faced by the limited partnership vehicle which would often request advanced revenue rulings to make the limited partnership attractive to an investor.

As drafted, the limited liability company obviously would always have limited liability.

It is expected that the Internal Revenue Service would rule favorably on the continuity of life characteristic because of provision 10.50.060 which states that a limited liability company shall be dissolved upon the death, retirement, resignation, expulsion, bankruptcy, dissolution of a member or occurrence of any other event which terminates the continued membership of a member in the limited liability company, unless the business of the limited liability company is continued by the consent of all the remaining members thereof. Thus, without consent of all the remaining members, the limited liability company would be dissolved upon one of the stated events.

Free transferability of interests is treated in Section 10.50.057. This section provides that a member may always transfer his interest in the limited liability company, but unless unanimous approval is obtained from the other members, the member transferring an interest, can transfer merely the profit and loss interest and not a right to share in the management of the limited liability company.

As to the characteristic of centralization of management, the provisions of the proposed legislation enable the members of the limited liability company to choose whether the limited liability company will be governed by themselves as members or by a manager or management elected by them. If the

members choose to retain management, the limited liability company would also lack the corporate characteristic of centralization of management.

Thus, it can be seen that at least two and possibly three of the corporate characteristics may be lacking in the classification of the limited liability company as a partnership or as an association for the purposes of the Internal Revenue Code.

In conclusion, a limited liability company offers the investor a business entity which combines the attractive elements of both a partnership and a corporation. It combines the limited liability offered to shareholders of a corporation with the tax treatment of a partnership.

The possibilities of increased revenue to the state have been set forth and it appears that increased revenues in excess of one million dollars may be obtained with very little increased expense incurred.

Robert L. Hartig

March 14, 1975

CORPORATION V. PARTNERSHIP V. LIMITED LIABILITY COMPANY

A. NON-TAX CONSIDERATIONS

	<u>CORPORATION</u>	<u>PARTNERSHIP</u>	<u>LIMITED LIABILITY COMPANY</u>
LIFE	Perpetual in most cases.	Agreed term, or life of any partner.	Agreed. Not to exceed 30 years.
ENTITY	Separate legal person.	Not a separate entity from individual partner.	Separate legal entity.
LIABILITY	No individual liability.	General partner individually liable for all obligations. Limited partner usually liable to the amount of capital contributed.	No individual liability.
TRANSFER OF INTEREST	In absence of restrictions interest may be sold to strangers.	New partnership agreement usually required.	May be transferred; however, if all other members do not approve of the proposed transfer by unanimous written consent, the transferee has no right to participate in the management and affairs of the company or to become a member, but is entitled only to receive his share of the profit or return of contributions.
CAPITAL	Capital may be enlisted by sale of stock.	New capital secured only by loans, increase in membership or new contributions by existing partners.	Capital is contributed in money or property at inception or during the course of operation as set out in the Certificate of Organization.
BUSINESS ACTION	Action authorized by specified percentage of directors and/or stockholders.	Unanimity of partners usually required.	Action authorized by majority in interest of the members.

	<u>CORPORATION</u>	<u>PARTNERSHIP</u>	<u>LIMITED LIABILITY COMPANY</u>
CREDIT CONSIDERATIONS	The corporation possesses credit ability apart from stock membership. Certificates of stock may be used as collateral.	Credit is coincidental with membership and partners assume joint and several responsibility. Interests in partnerships are not ordinarily accepted as basis for loan or credit.	Credit will be extended to the company on the strength of its contributed or to-be-contributed capital.
MANAGEMENT	Shareholders may invest without participation in management.	All general partners involved in management responsibility	Management of the company is in the members unless management by a manager or managers to be elected by the members is provided in the Certificate of Organization.
FLEXIBILITY	A corporation operates within its corporate franchise granted by the state or states in which it is authorized to do business.	A partnership is a contractual relationship which may be altered by unanimous agreement of the partners.	Flexibility is perhaps the Limited Liability Company's strongest point. The Certificate of Organization will contain a minimum of restrictions and the working rules of the corporation may be drafted in the form of an operating agreement.
<u>B. TAX FACTORS</u>			
TAX BURDEN	As a separate legal personality a corporation is subject to taxation, in addition to the taxation of the income received as dividends by its members. <u>Electing "Small Business Corporation"</u> . (1) Each shareholder's proportionate share of the corporation's undistributed taxable income is included in the gross income of the shareholder. The corporation pays no tax thereon. This substantially parallels the taxation of a partner's income from the partnership.	Each partner is taxed on his proportionate share of income whether distributed or not.	Private revenue ruling will be requested of the Internal Revenue Service requesting that the company be classified as a partnership for federal tax purposes. As drafted the Limited Liability Company will lack at least two and perhaps three of the characteristics of a corporation; the third centralization of management, will be lacking if management is reserved to the members.

TAX CONCERN

CORPORATION

In close corporations, gross corporate income is reduced by reasonable salaries paid to officer-stockholders. Accumulation of profits may be made up to at least \$100,000 or to such larger extent as not to constitute avoidance of surtax by the stockholders and an unreasonable accumulation in terms of the requirements of business. Corporation taxes, plus individual taxes on the compensation for services or dividends, represent the tax burden of the corporate investment, as against the individual tax paid by partners.

Electing "Small Business Corporation." Undistributed taxable income of an electing corporation is taxable proportionately to each shareholder. Subsequent distributions out of this income to the shareholders are tax free. This substantially parallels the taxation of a partner's income from the partnership.

PENSION TRUST

Corporate contributions to a pension trust, within the amount allowed by law are deductible by the corporation. Stockholder-employees may be covered to same extent as other

PARTNERSHIP

All earnings and profits are taxable to the individual partner, unaffected by accumulations of earnings. However, once so taxed, there-after any distributions of these earnings are tax exempt to the individual partner.

Members of a partnership are not employees and are not proper beneficiaries under an exempt Pension Trust. However, under the Self-Employed Individuals Tax Retirement Act of 1962,

LIMITED LIABILITY COMPANY

All earnings and taxes are taxable to the members whether distributed or not. It is contemplated that the distribution rules and basis rules now applicable to the partnership interest will also be applicable to a limited liability company.

Unknown but it is suggested that the rules now applicable to a Subchapter S corporation which impose the limits of the Keogh Plan will also be applicable.

CORPORATION

employees, so long as there is no discrimination in favor of such stockholders.

Electing "Small Business Corporation". An electing corporation's contributions to a pension trust, within the amount allowed by law, are deductible by the corporation from its taxable income.

SOCIAL SECURITY TAX

Compensation paid to stockholding officers and employees is subject to Social Security Taxes.

Electing "Small Business Corporation". Compensation paid to stockholding Officers and employees is subject to Social Security Taxes.

ASSIGNABILITY OF INTEREST OR INCOME

An unqualified transfer of stock ordinarily requiring no other person's consent, will entitle transferee to dividends or distributions

Electing "Small Business Corporation". Transferee is entitled to dividends and distributions, but the stock must be transferred to an individual or estate and the transferee must consent to the continuation of the "tax option" status.

PARTNERSHIP

partners who own more than 10% of the capital or profit interest in the partnership may, beginning in 1968, deduct the full amount of their contribution to a pension plan up to \$2500.

Partners do not pay Social Security Taxes upon their salaries from the partnership. However, they are required to pay the tax on self-employment income.

Any assignment of interest requires consent of the other partners and may create a new partnership.

LIMITED LIABILITY COMPANY

Result should be same as partnership with members paying self-employment tax and not subject to Social Security Tax.

A member's interest in Limited Liability Company may not be transferred or assigned without unanimous approval of the continuing members. Assignment of a member's interest will result in the tax falling on the transferee.

	<u>CORPORATION</u>	<u>PARTNERSHIP</u>	<u>LIMITED LIABILITY COMPANY</u>
COMMUNITY PROPERTY STATES	<p>Dividends from investments made from community property become community property.</p> <p><u>Electing "Small Business Corporation"</u>. Dividends from investments made from community property become community property.</p>	<p>Whether income is community or separate income depends upon the law of the state of domicile.</p>	<p>Same as partnership, with the results depending on the community property laws in the several states.</p>
DUAL MEMBERSHIPS	<p>Because it would be extending its credit, liability and the powers of the Board of Directors beyond legal scope, a corporation cannot be a direct member of a partnership in some states.</p> <p><u>Electing "Small Business Corporation"</u>. Stock may not be held by either a partnership or another corporation.</p>	<p>A partnership may own some or all of the stock of a corporation and so function in two capacities.</p>	<p>A Limited Liability Company enjoys flexibility in this area and may be owned by other entities or individuals and participate in other entities and business enterprises.</p>

(1) An electing "small business corporation" is a domestic corporation which does not have more than 10 shareholders and which otherwise comes within the requirements of Subchapter "S" of the Internal Revenue Code, and whose shareholders elect to include in their personal income the current taxable income of the corporation.

1. Sec. 10.50.030. (a) The word "Limited" ["limited"] or as abbreviated "Ltd." shall be the last word of the name of every limited liability company formed under the provisions of this chapter and, in addition, the limited liability company name may not

(1) contain a word or phrase which indicates or implies that it is organized for a purpose other than one or more of the purposes contained in its certificate of organization;

(2) be the same as, or deceptively similar to, the name of a limited liability company or corporation existing under the laws of this state or a foreign corporation authorized to transact business in this state, or a name the exclusive right to which is, at the time, reserved in the manner provided under the laws of this state.

(b) Omission of the word "Limited" ["limited"] in the use of the name of the limited liability company shall render any person who participates in the omission, or knowingly acquiesces in it, liable for indebtedness, damage or liability occasioned by the omission.

2. Sec 10.50.050. (a) (5) the total amount of cash and a description and agreed value of [or] property other than cash contributed;

3. Sec. 10.50.080. CONTRIBUTIONS TO CAPITAL. The contributions to capital by [of] a member to the limited liability

company may consist of cash or other property, but not services.

4. Sec. 10.50.110. LIMITED LIABILITY COMPANY PROPERTY.

Real and personal property owned or purchased by a limited liability company shall be held and owned, and conveyance made, in the limited liability company name, or in the name of any member or manager. Instruments and documents providing for the acquisition, mortgage or disposition of property of the limited liability company shall be valid and binding upon the limited liability company having a manager or managers or one or more members of a limited liability company in which management has been retained by [in] the members.

5. Sec. 10.50.140. DIVISION OF PROFITS: IMPAIRMENT OF

CAPITAL. The limited liability company may, from time to time, divide the profits of its business and distribute the same to the members of the limited liability company upon the basis stipulated in the operating agreement; provided however[,] that, after distribution is made, the assets of the limited liability company are in excess of all liabilities of the limited liability company except liabilities to members on account of their contributions.

6. Sec. 10.50.150. (d) A member of a limited liability company may have the limited liability company dissolved and its affairs wound up when

(1) the member rightfully but unsuccessfully [unseccessfully] has demanded the return of his or its contribution, or

(2) the other liabilities of the limited liability company have not been paid, or the limited liability company property is insufficient for their payment and the member would otherwise be entitled to the return of his or its contribution.

7. Sec. 10.50.160(a) A member is liable to the limited liability company

(1) for the difference between his or its contributions to capital as actually made and his or its contributions to capital as [that] stated in the certificate of organization as having been made, and

(2) for any unpaid contribution to capital which he or it agreed [in the certificate of organization] to make in the future at the time and on the conditions stated in the certificate of organization.

8. Sec. 10.50.170. INTEREST IN LIMITED LIABILITY COMPANY; TRANSFERABILITY OF INTEREST. [(a)] The interest of all members in a limited liability company constitutes the personal estate of the member, and may be transferred or assigned as provided in the operating agreement; however, if all of the other members of the limited liability company other than the member proposing to dispose of his or its

interest do not approve of the proposed transfer or assignment by unanimous written consent, the transferee [transfer] of the member's interest shall have no right to participate in the management of the business and affairs of the limited liability company, or to become a member, but shall only be entitled to receive the share of profits or other compensation by way of income, and the return of contributions, to which that member would otherwise be entitled.

9. Sec. 10.50.180. DISSOLUTION. (a) A limited liability company organized under this chapter shall be dissolved upon the occurrence of any of the following events

(1) when the period fixed for the duration of the limited liability company shall expire;

(2) by the unanimous written agreement of all members; or

(3) upon the death, retirement, resignation, expulsion, bankruptcy, dissolution of a member or occurrence of any other event which terminates the continued membership of a member in the limited liability company, unless the business of the limited liability company is reconstituted [continued] by the consent of all the remaining members under a right to do so stated in the certificate of organization of the limited liability company.

10. Sec. 10.50.200(c) The form for evidencing an amendment to the certificate of organization of a limited liability

company shall be promulgated by the commissioner and shall contain terms and provisions, consistent with this chapter, which the commissioner determines. [The amendment shall be signed and sworn to by all members, and an amendment adding a new member shall be signed also by the member to be added, and thereafter duplicate] Duplicate originals of the amendment shall be forwarded to the commissioner for filing, accompanied by the requisite filing fee.

11. Sec. 10.50.230. FEES FOR FILING DOCUMENTS AND ISSUING CERTIFICATES. The commissioner shall charge and collect for:

(1) filing the original certificate of organization, if the capital of the limited liability company is:

<u>Capital</u>	<u>Filing Fee</u>
<u>Not in excess of \$100,000:</u>	\$ <u>100</u>
<u>In excess of \$100,000 but</u> <u>not in excess of \$250,000;</u>	\$ <u>250</u>
<u>In excess of \$250,000 but</u> <u>not in excess of \$500,000:</u>	\$ <u>500</u>
<u>In excess of \$500,000 but</u> <u>not in excess of \$1,000,000:</u>	\$ <u>750</u>
<u>In excess of \$1,000,000:</u>	<u>\$1,000</u>

<u>Capital</u>	<u>Filing Fee</u>
Not in excess of \$100,000	\$ 100
\$100,000 and not exceeding \$250,000	\$ 250
Exceeding \$250,000 but not in excess of \$500,000	\$ 500
\$500,000 to \$1,000,000	\$ 750
In excess of \$1,000,000	\$1,000

(2) for amending the certificate of organization, a filing fee of \$25, together with the appropriate fee set out in (1) of this section if the amendment is to increase the amount of capital;

(3) for dissolution, \$25;

(4) an annual tax of \$100, due and payable January 2 of each year; this tax is delinquent if not paid by February 1 and an addition to the tax shall then be due of \$50.

12. Sec. 10.50.250. REGISTERED AGENT. A limited liability company is required at all times to have a registered agent whose residence is in the state. The commissioner shall be notified upon any change in the name or address of the registered agent.

13. Sec. 10.50.260. APPLICATION TO FOREIGN AND INTERSTATE COMMERCE. The provisions of this chapter shall apply to commerce with foreign nations and among the several states only as permitted by law.

14. Sec. 10.50.270. APPLICABILITY OF THIS CHAPTER. This chapter takes precedence in the event of a conflict with the provisions of the Alaska Business Corporation Act or other laws. This chapter does not affect a right accrued or established, or any liability or penalty incurred, prior to the effective date of this Act.

15. Sec. 10.50.280. DEFINITIONS. In this chapter, unless the context otherwise requires

(1) "Bankrupt" means bankrupt under the Federal Bankruptcy Act;

(2) "commissioner" means the commissioner of commerce;

(3) "court" includes every court and judge having jurisdiction in the case;

(4) "limited liability company" means a limited liability company organized and existing under this chapter;

(5) "person" includes individuals, general partnerships, limited partnerships, limited liability companies, corporations, trusts, business trusts, real estate investment trusts, estates and other associations;

(6) "real property" includes land, any interest, leasehold or estate in land and any improvements on it.

16. Sec. 10.50.290. SHORT TITLE. This Act shall be known and may be cited as the Alaska Limited Liability Company Act.

April 29, 1975

Mr. Lawrence Gibbs
Assistant Commissioner (Technical)
Internal Revenue Service
Washington, D.C.

Dear Mr. Gibbs:

Enclosed is a copy of House Bill 403 which was introduced in the Alaska House of Representatives by Representative Richard K. Urion on April 9, 1975.

On April 24, 1975, the House Commerce Committee heard testimony on the proposed legislation by Mr. Miles S. Schlosberg, Director of Banking, Securities, Small Loans, and Corporations, Department of Commerce of the State of Alaska and Bernard J. Dougherty, Attorney with Cole, Hartig, Rhodes, Norman, Mahoney & Goltz, of Anchorage, Alaska.

Before acting on this proposed legislation we ask that you and your staff review it and issue to us an information letter in accordance with Treasury Regulations Section 601.201.(a)(5).

As the testimony was presented and as we understand the legislation and its interrelation with Treasury Regulations Section 301.7701 et. seq., the Limited Liability Company Act as proposed before the Alaska Legislature should be classified as a partnership for Federal Tax purposes because it lacks the corporate characteristics of continuity of life, free transferability of interest, and if the Certificate of Organization is drafted so that management is retained by the members, the Company will lack the characteristic of centralization of management. For these reasons, the testimony was, that the Limited Liability Company should be classified as a partnership for Federal Tax purposes.

We would appreciate it if you would have your staff review the enclosed legislation and give us your views on the matter in an information letter.

Kindest regards.

Very truly yours,