HOUSE COMMITTEE ON APPROPRIATIONS

FISCAL NOTE

HOUSE BILL NO. 2234 **PRINTERS NO.** 3746 **PRIME SPONSOR**: Turzai

COST / (SAVINGS)

FUND	FY 2013/14	FY 2014/15
General Fund	**$0**	**$0**
Corporation Bureau Restricted Account	**$0**	**See "Fiscal Impact"**

SUMMARY: Amends Title 15 (Corporations and Unincorporated Associations) and Title 54 (Names) to provide for entity transactions. The addition of Section 7411 (Expiration) will take effect immediately. The remainder of the legislation will take effect on July 1, 2015.

ANALYSIS: This legislation reorganizes significant portions of Title 15, and provides all business entity types the ability to engage in five fundamental transaction types: mergers, interest exchanges, conversions, divisions and domestications. Likewise, the legislation consolidates provisions related to the registration of foreign business entities that do business in PA.

Title 15 Reorganization: The reorganizational provisions consolidate provisions in the preliminary chapters of Title 15 (which apply to all types of entities) and repeal similar provisions in the individual entity laws (which apply only to one type of entity). These amendments are lengthy, but largely technical. The first four chapters of Title 15 will contain the substantive provisions applicable to business entities:

- Chapter 1, which is largely based on the Uniform Business Organizations Code, addresses the filing of documents with the Department of State.
- Chapter 2 is largely based on current law and addresses the works that may appear in business names.
- Chapter 3, which is based on current law and the Model Entity Transactions Act, contains the rules regarding how each entity form approves transactions.
- Chapter 3 also consolidates the provisions allowing each type of transaction.
- Chapter 4 addresses foreign associations that do business in PA.

The legislation either repeals or makes technical changes to the remaining chapters, the substance of which will now be contained in the first four chapters.

<u>Entity Transactions:</u> The legislation allows all entity types (corporations, nonprofits, general partnerships, limited partnerships, limited liability companies, unincorporated nonprofit associations, professional associations and business trusts) to engage in fundamental transactions in accordance with provisions governing the approval of the transaction by each type of entity and provisions for each specific type of transaction. Additionally, certain "associations" and "entities" that were organized under a law other than Title 15 (e.g., certain financial institutions, certain insurance licensees, etc.) may engage in certain types of transactions (as used in the legislation, the term "association" refers to entities and businesses organized outside of Title 15, while the term "entity" refers to those formed under Title 15 or a parallel law outside of PA). Language is included to prevent the use of entity transactions for the purpose of circumventing regulation or other statutes that may require the approval of or notice to another government agency.

Each type of transaction involves the approval of a plan for the transaction by the interest holders in the entity. After approval, a statement of the transaction may be filed with the Department of State to make the transaction a public record. Transactions become effective on the date and time of delivery to the Department, unless the statement specifies a later date.

<u>Approval of Transactions:</u> As the result of the differences in governance of the various entity types, each entity type will use its own process for approving transactions:

- **Business corporations** - Approval provisions are based on the current law governing the approval of transactions for business corporations.
- **Nonprofit corporations** - Approval provisions are based on the current law governing the approval of transactions for nonprofit corporations.
- **General partnerships** - The approval is governed by the organic rules of the partnership (i.e., the partnership agreement). If the process is not provided in the organic rules, unanimous approval is required.
- **Limited partnerships** - Unanimous approval of the general partners and majority approval of the limited partners is required, unless the organic rules of the limited partnership provide otherwise.
- **Limited liability companies:**
  - Member-managed - Majority approval by the members, or a majority of each class of members, is required, unless the organic rules provide otherwise.
  - Manager-managed - The plan is adopted by the managers and submitted to the members for a majority vote, unless the organic rules provide otherwise.
- **Professional associations** - Majority approval of the associates (according to shares of ownership) is required, unless the organic rules require a higher percentage.
- **Business trusts** - Approval of all the beneficial owners is required, unless the organic rules provide otherwise.
- **Nonprofit unincorporated associations** - A majority of the votes cast at a meeting of the members is required, unless the governing principles provide otherwise.

Additionally, except for a nonprofit corporation, or if prohibited by the organic rules for the entity, a unanimous vote or consent of the entity's interest holders satisfies the approval requirements.

Types of Transactions:

Merger - A merger involves the combination of two or more entities or associations into a surviving association. Domestic entities may merge with foreign associations into a surviving association, and two or more foreign associations may merge into a surviving domestic entity.

In a merger, the property and liabilities of the merging associations vest automatically in the surviving association. The surviving association becomes the owner of all real and personal property of the merged associations and is subject to all debts and obligations of the merging associations. A merger does not give rise to a claim that a contract with a merging association is no longer in effect.

Interest exchange - An interest exchange involves the acquisition of an interest in one association by another, so that the acquiring association controls the acquired association.

In contrast to a merger, an interest exchange does not in and of itself affect the separate existence of the parties, vest in the acquiring association the property of the acquired association, or render the acquiring association liable for the liabilities of the acquired association. When the interest exchange becomes effective, the interests of the acquired association are exchanged in accordance with the plan, the acquiring association becomes the owner of the acquired association's interests as provided in the plan, and the organic rules of the acquired association are amended as provided in the statement of interest exchange (obviating the need for repetitive filings).

Conversion - A conversion involves a change in the legal form of a domestic entity or a domestic banking institution. A domestic entity may become a different form of foreign association, if allowed by the laws of the other jurisdiction.

A converted association is the same association as it was before the conversion, but it is of a different legal type. The converted association remains the owner of all real property and remains subject to the same liabilities. The converted association remains a party to all of the contracts to which the converting association was a party. Consistent with the idea that the converted association is the same association as existed before the conversion, albeit in a different form, the existence of the converted association is deemed to have commenced at the time when the converting association first existed.

Division - A division, the opposite of a merger, involves a split of a domestic entity into two or more domestic entities or foreign associations.

The division is effective in the event that the dividing association survives or does not survive the transaction. If interests in property are allocated to a resulting association as part of a division, title to those interests automatically passes to the resulting association. The liabilities of the dividing entity are allocated among the resulting associations. The filing of the statement of division with the Department is not constructive notice of the change of record title to the resulting association except in the case of a nonprofit corporation.

Domestication - Domestication involves moving an entity organized under the laws of one state to organization under the laws of another state. The entity must be the same type of entity after the transaction. A domestic entity may organize under the laws of a foreign jurisdiction, if allowed by that jurisdiction's laws.

The domesticated entity is the same entity as the domesticating entity. It merely has changed the organic law to which it is subject.

Foreign Associations: Provisions for the registration of foreign associations that do business in PA are repealed in the individual entity laws and consolidated in a new preliminary Chapter 4 (which applies broadly). The amendments are largely technical, consolidating changes. However, a foreign financial institution that is not an interstate bank will be treated like a foreign association that is not a bank, and will be required to register.

Technical Changes: Technical changes are made throughout Title 15, and minor technical changes are made in Title 54 to conform to the new and consolidated provisions.

FISCAL IMPACT: According to the Department of State, the updates to the current records management database as a result of this legislation would take about 120 hours of billable time. The technical work would include changes to the business system and the web front-end. User training and post deployment support would also be necessary. Those costs are estimated to be a one-time $82,000. Since the legislation does not take effect until July 2015, enough time should be available to make the technical changes utilizing existing funds.

The department also indicates that this legislation could generate some new, though indeterminable, revenue from the delineated fee structure for the four new filing types (statements of abandonment, interest exchange, withdrawal, and transfer of registration). Additional revenue is also expected from the $125 fee under section 133(e) for the issuance and preparation of an engrossed (gold seal) certificate, which is an increase from the $70 fee currently charged by the department. The department indicates that 5 of these certificates were issued in 2013.

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House Appropriations Committee (R)

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Estimates are calculated using the best information available. Actual costs and revenue impact incurred may vary from estimates.