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Practical Considerations for Forming LLCs in New York and Delaware

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In 2006, New York altered its publication requirements for partnerships including limited liability companies. Client alerts with titles such as "Publish or Perish!" had everyone asking questions; law firms reported that expenses associated with the new publication requirements could be significant. Three years out, this article seeks to provide practical advice regarding the formation of LLCs in New York and Delaware with a focus on how the new publication requirements might influence the choice of a jurisdiction of formation.

I am often asked, "What is the difference between forming an LLC in New York and Delaware?" Because of Delaware's business-friendly courts, I often advise my clients to form in Delaware, determine next where they will be "doing business" and proceed to qualify the entity in those jurisdictions. For those LLCs "doing business" in New York, an analysis of the publication requirements is necessary and should be done carefully to avoid unnecessary costs. Procedures in the two states are similar, but only New York has a publication requirement, which adds significant costs. Nevertheless, LLCs intending to operate in New York may wish to form there because foreign LLCs (those organized out-of-state) doing business in New York State cannot avoid publication.

BASICS

1. NEW YORK

In New York, the organizer of an LLC must choose a location for its office and file articles of organization. This location is not a street address, but merely the name of the county where the office is located. The LLC must then publish notice of formation in that county and file a certificate of publication.

A foreign LLC "doing business" in New York must file an application for authority with parallel informational and publication requirements. An LLC conducting "regular and continuous" transactions within New York, which are not incidental to interstate sales, is "doing business." Most Internet commerce should not constitute "doing business" because of its interstate nature.

A. Publication Requirements – Why?

New York's publication requirement is designed to protect the public by informing them of an LLC's membership, and thus to what extent the LLC could be held liable. The requirements have eroded, however, and a recent measure which would have forced LLCs to disclose their

ten largest members in connection with the publication process was rejected by the state legislature. As it stands, information provided by the publication requirement is of little use; no details of membership are included and the address given is a mere formality. Some have suggested that lobbying from the newspaper industry is the true cause for the requirement's survival, as newspapers receive steady income from these mandatory notices.



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B. Publication Mechanics and Practical Advice

Within 120 days of formation of a New York LLC or application of authority for a foreign LLC to do business, the LLC must file a certificate of publication with New York's Department of State. [FOOTNOTE 1] If the LLC fails to file, its authority to "carry on, conduct or transact any business" within New York is suspended.

An LLC must publish information similar to that contained in its articles of organization or application for authority. This publication must run each week for six weeks in two newspapers designated by the county clerk (one weekly newspaper and one daily) in the county where the LLC's office is located. After publication, the newspapers will provide the LLC with affidavits, which the LLC must submit with its certificate of publication.

If the LLC fails to file the certificate of publication, its authority to "carry on, conduct or transact any business" within New York is suspended. This language results from a 2006 amendment to the LLC law, which previously forbade delinquent LLCs from suing in New York State courts. The courts have not addressed this amendment, however, and because the purpose of the 2006 amendment was to set harsher penalties for noncompliance, the restriction on conducting business may still prohibit bringing suit. Furthermore, the consequences of operating without authority to conduct business are uncertain. The statutes will not void prior contracts or expose the LLC's members to liability for prior activities. What of activities in the interim? Will the LLC's members be liable for those activities? Will contracts created during that period be enforceable? Although actual penalties may not be so severe, the vagueness of the amended laws means that advising LLCs to comply with the publication requirements is the only responsible course of action.

Fortunately, compliance can be inexpensive. An LLC must publish

in the county of the office designated in its articles of organization or application for authority. This "office" can be anywhere in New York, and does not have to be a place where business activities are conducted. Because publication fees vary by county and depend on advertising rates of local newspapers, many LLCs are able to control the costs of publication by using the location of a registered agent in another county as their "office."

Some examples of six-week publication prices include:

- New York County's *New York Law Journal*: \$723.20
- Albany County's *Altamont Enterprise*: \$26.88
- Nassau County's *Mineola American*: \$160.00

2. DELAWARE

In Delaware, an LLC's organizer must file a certificate of formation with the Department of State. A foreign LLC must similarly register and authorize the Secretary of State to accept service of process on its behalf.

Delaware is known as a corporate haven for its favorable treatment of businesses. In fact, over 60 percent of the Fortune 500 companies are incorporated there. Delaware's body of case law is well developed, which gives corporations greater guidance on matters of governance and transaction liability. In addition, disputes over the internal affairs of Delaware LLCs are usually filed in Delaware's specialized Court of Chancery. Because it is a court of equity, there are no juries, and cases are heard by chancellors familiar with commercial litigation.

ADVICE

At first blush, LLC formation in New York seems costlier than in Delaware, and Delaware has certain other advantages. As stated above, I often advise my clients to form in Delaware, determine next where they will be "doing business" and proceed to qualify their entity in those jurisdictions. This is not the lowest-cost approach, but does provide the best protection of the laws.

Although New York's fees are higher than Delaware's, a foreign LLC doing business in New York will not be able to avoid the fees by forming their business outside of New York State. An LLC's members will also be taxed according to the location of income-earning activities, so forming outside of New York to avoid tax will not achieve the desired effect.

A foreign LLC doing business in Delaware, on the other hand, does not have to register until it needs to bring suit. The LLC must pay back fees, however, and an additional \$200 for each year of doing business without registration. Delaware's taxes similarly apply to LLCs based upon the location of the income-earning activity.

One wishing to form an LLC at lowest cost should therefore look first to where its business activities will occur; if the LLC will do business in only one state, then it should form in that state. If New York is chosen, the county named in the articles of organization will be the county where publication will take place and this choice will impact the publication costs. In the event an LLC will be doing business in multiple locations,

it is generally my recommendation that the entity be formed in Delaware and qualified in the appropriate jurisdictions based on the relevant jurisdiction's doing business test.

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FEE COMPARISON				
	NEW YORK		DELAWARE	
	Domestic LLC	Foreign LLC	Domestic LLC	Foreign LLC
Initial Filing/Registration Fee	\$200	\$250	\$70	\$100
Annual Filing/Franchise Tax	\$25 - \$4,500		\$250	
Certificate of Publication	\$50		N/A	
Publication	\$150 - \$1,500		N/A	
Income Tax Rates	4.00% - 8.97%		2.20% - 5.95%	

FOOTNOTE

FN1 Some LLCs are exempt from New York's publication requirement. LLCs that filed their articles of organization or applications for authority prior to Jan. 1, 1999, or those that filed on or after Jan. 1, 1999 but before June 1, 2006 and filed at least one affidavit of publication, are not required to comply with current publication requirements.