

Illinois Legal Update

Insights and Developments in the Law

Summer 2007

In This Issue

Limited Liability Companies in Illinois 1

Real Property Disclosure Act 2

Student Can Sue Youth Center for Crippling Injuries.... 2

Beware of Fake Checks 3

The Internet Is a One-Way Street 3

Limited Liability Companies in Illinois

When you start a business, you can set it up in one of several forms, depending upon your circumstances, particularly with regard to liability and tax considerations.

An LLC enjoys the benefits of limited liability, similar to a corporation, but also has the tax advantages of a partnership.

The least complicated form of business ownership is the sole proprietorship. Other forms include the general partnership, in which two or more individuals join together to carry on a business, or a limited partnership, where the structure includes two types of partners. Organizing as a corporation provides the owners with insulation from personal liability. However, the organizational structure of a corporation is formal and is controlled by state and federal laws.

In recent years, a new form of business—the limited liability company (LLC)—has gained popularity as a business entity. An LLC enjoys the benefits of limited liability, similar to a corporation, but also has the tax advantages of a partnership. LLCs permit direct control of the business operations of the company without oversight by a corporate board of directors.

LLCs are commonly used in research and development businesses, technology, oil and gas, and real estate. The LLC is also appropriate for professional service firms (when allowed), such as law firms or accounting firms, closely held corporations, or family businesses.

Liability

The debts and obligations of the LLC, regardless of how they arise, are solely the debts of the LLC. A member or manager is not liable for them simply by reason of being or acting as a member or manager. Even if an LLC fails to observe company formalities, this is not a

Continued on page four.

Real Property Disclosure Act



If you have bought or sold a home in Illinois, you are most likely aware of the Residential Real

Property Disclosure Act. The Act has two main provisions.

The first is a provision requiring that everyone selling residential property with one to four dwellings on it must disclose to prospective buyers certain defects in the property by completing and signing a 22-question disclosure form. A seller must disclose all defects that he actually knows are present on the property as of the date of completing the form. Although a seller does not have to make his own investigation or inspection of the property in order to fill out the form, he must supplement the disclosure form in writing if he learns of a mistake or if he left something out on the document before the date of the closing of the sale.

Even after a supplemental disclosure, the buyer does not have a right to terminate the real estate contract unless the seller had actual knowledge of the defect at the time when he first completed the disclosure form. However, most real estate contracts provide for an inspection of the property prior to closing to determine that the property has not changed since the contract was signed. If the mistake or omission revealed is not corrected by the date of this inspection, the buyer will have the right to demand such a repair prior to the closing.

The disclosure form includes a warning that disclosures do not include previous problems with the property if the seller reasonably believes that they have been cor-

rected; it reports only the current condition of the property. This resolves the question asked by many sellers regarding their obligations in completing the disclosure form: "Do I have to include things that have been fixed such as the air conditioning?" Hopefully, this warning will encourage more buyers to use professional home inspectors to determine any potential defects in the home.

A buyer has the right to cancel the contract if the seller does not provide the disclosure form before the closing. A "seller" is defined

as every person or entity who owns the property, including a beneficiary of a trust. A person who has never occupied the property and who has never had control over the property is not considered a seller. A seller who does not comply with the Act will be responsible for paying damages to the buyer, court costs, and possibly the buyer's attorney's fees.

The second provision is relatively new and calls for the creation of a database to provide informa-

Continued on page three.

Student Can Sue Youth Center for Crippling Injuries

In a decision that has a potentially far-reaching impact on governmental liability for injuries, the Illinois Supreme Court recently allowed a suit brought by an injured student against a youth center and his school district to proceed to trial.

The suit arose out of injuries that the student suffered at the youth center during a school-sponsored extracurricular event. The student fell while trying to do a front flip on a trampoline during a "freelance" part of the class. The gymnastics class was run by an unqualified instructor who did not properly monitor the children who were using the trampoline. The fall left the student a quadriplegic.

The defendants argued that they could not be sued by the student

because state law made them immune from liability for discretionary decisions, and the way that the defendants ran the gymnastics program was a discretionary decision. The court rejected this argument, finding that the case was subject to a more specific provision of the law governing liability for hazardous recreational activities.

The court then found that the hazardous recreational activities portion of the law permitted a defendant that would otherwise be immune to be sued if it was guilty of "willful or wanton" conduct. Since the evidence showed that the defendants might have acted willfully and wantonly, the supreme court allowed the student's lawsuit to proceed to a jury trial.

Beware of Fake Checks

You have responded to a work-at-home offer in which you will be an account manager for a foreign company, depositing checks from its U.S. customers. It seems simple: You deposit the checks, take your pay out of them, and send the remainder to the foreign company. Or . . . you have reason to believe you have won a sweepstakes or lottery prize. You receive a check for your winnings, with instructions to cash it, then return a portion of the money to cover taxes or other fees. Or . . . having sold something through a newspaper ad or online, you receive a check for much more than the purchase price. Calling it an accounting error, the buyer apologizes for the mistake and asks that you return the excess amount.

If these scenarios activate your fraud antennae, there is a good reason for that. Each is a typical example of circumstances in which people are victimized by fake checks. This is a growing problem, perhaps because of the ways in which strangers are brought together for transactions by new technologies and the Internet.

Of course, the sting from the scam occurs when the victim deposits the check he receives, then withdraws funds and sends off money or merchandise before his bank discovers that the deposited check is fraudulent. Even when the bank is vigilant, that discovery could take days, or even weeks. Your first reaction might be to blame the bank, but, generally, the

depositor is on the hook, as he is considered to have taken responsibility for the funds spent or sent before the fraud is discovered.

If there is a single best piece of advice for not becoming a victim, it is to accept no check if it is accompanied by a request that you return some of the money. But if the worst happens, and you have reason to believe that you have been had by the writer of a fake check, contact your bank and the local office of the FBI.

Disclosure Act

Continued from page two.

tion about predatory lenders. Although right now the database includes only certain areas of Cook County, it requires lenders to submit certain information about borrowers, and the state determines if the borrower requires credit counseling. The purpose of this provision is to reduce the number of defaults on loans and to make sure that borrowers are not being taken advantage of by unscrupulous lenders.

The Internet Is a One-Way Street



In a victory for business interests, an Illinois court recently ruled that an Illinois resident had to go to Missouri to sue the company responsible for his injuries.

The case involved an Illinois resident who learned of the training services offered by the Missouri Bone and Joint Center (“MBJC”), and who was then injured by the MBJC in Missouri. He sued in Illinois, and the evidence showed that the MBJC gave presentations about its services and advertised in Illinois. The MBJC also main-

tained an interactive website that allowed Illinois residents to contact it to request an appointment, fill out patient surveys, and make comments. Despite these contacts, the court determined that it had no jurisdiction to hear the case because the MBJC’s contacts with Illinois were not systematic enough.

Although the law permits courts to exercise jurisdiction over companies doing business in, or having continuous contacts with, the state, the court found that the MBJC did

Continued on page four.

Resolution of legal issues depends upon many factors, including variations of facts and interpretations of Illinois law. This newsletter is not intended to provide legal advice on specific subjects, but rather to provide insight into legal developments and issues. The reader should always consult with legal counsel before taking action on matters covered by this newsletter.

LLCs

Continued from page one.

basis for imposing personal liability upon members or managers. Nevertheless, a member may assume liability for the LLC's debts and obligations if such provisions are included in the articles of organization and the member has consented to this in writing. There are specific rules under which members or managers have authority to act on behalf of an LLC when dealing with third parties.

Taxation

An LLC is allowed certain federal tax benefits not given to a traditional corporation. Specifically, the income from an LLC is taxed only once—when it is distributed to the members. Corporate income is taxed twice—once when the income is earned and again when the income is distributed as dividends to the shareholders.

Another business form not mentioned thus far is an "S corporation." Like an LLC, an S corporation is a hybrid between a partnership and a corporation, providing federal tax benefits and limited liability. However, federal tax law places certain burdens on an S corporation that it does not on an LLC. For instance, an S corporation cannot have more than 100 shareholders, while an LLC may have as many members as desired. In addition, LLC members have the flexibility of a partnership in structuring the allocation of profits, losses, and distributions in different ratios.

Management

The management of an LLC is also more simplified. The LLC may elect to be managed by its

members or by a smaller number of managers, and any action of the LLC requiring the consent of members or managers may be taken with or without a meeting and the members or managers may vote on it either individually or by proxy. A member may withdraw from an LLC at will (called "dissociation"), and the LLC must purchase the interest of the dissociated member.

The stability of an LLC has been increased because there are now fewer events that cause dissolution. The dissociation of a member does not automatically result in the dissolution of the LLC or a vote to continue. An LLC dissolves only upon an event that is specifically set forth in the operating agreement. It may also dissolve by the consent of the members, the illegality of the business, or certain judicial determinations or an administrative dissolution.

Organization

An LLC may be organized to engage in any lawful business in Illinois, although the ability of an LLC to engage in the business of insurance or the practice of dentistry or medicine is limited by statute. An LLC can even be used for holding property for estate planning purposes or for accepting and executing trusts by fiduciaries.

An LLC may have only a single member. This means that a corporation may form an LLC as a wholly owned subsidiary, or an individual may form a wholly owned LLC to separate assets used in a business. Partnerships may now convert into an LLC, and other business entities, including other LLCs, can now merge with one another. An LLC may have a per-

petual life, which means that it can exist beyond the lifetime of the original owner(s).

Choosing the best business form is not an easy decision. Although the LLC offers many advantages, you should always seek competent legal, business, and tax advice before making such a decision.

Internet

Continued from page three.

not have such contacts. In doing so, it rejected other cases finding the level of interactivity of websites an important factor, and distinguishing between "passive" websites (i.e., those not allowing people viewing them to initiate any contact with the company) and "active" websites (i.e., those like the MBJC's that permit a two-way dialogue between companies and consumers).

The court ruled that passive websites were similar to radio or magazine advertising, while active websites resembled communications by telephone or mail, but that in either case "[a]n ad on the Internet is no different than an ad in any other medium that provides a telephone number or other means to contact a potential defendant," and that merely advertising in Illinois is not enough to give the courts jurisdiction to hear claims against a company.

This decision is a blow to Illinois citizens who are injured by foreign companies, and will condemn many of them to go to another state if they want to sue for redress.