



NEW YORK  
CITY BAR

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**REPORT BY THE CORPORATION LAW COMMITTEE  
RECOMMENDING ADOPTION BY NEW YORK STATE OF THE  
REVISED UNIFORM LIMITED LIABILITY COMPANY ACT**

**EXECUTIVE SUMMARY**

The Corporation Law Committee of the Association of the Bar of the City of New York recommends that New York State enact the Revised Uniform Limited Liability Company Act (“**RULLCA**”) in substantially the form approved by the National Conference of Commissioners on Uniform State Laws and the American Bar Association.

The Committee’s reasons for this recommendation are:

1. **More Advanced Statute.** RULLCA is the product of extensive study by knowledgeable experts based on their experience with the current and prior generation of limited liability company (“**LLC**”) statutes. It is a modern, flexible, user-friendly statute that is more advanced than New York’s current Limited Liability Company Law (“**NYLLCL**”), which was enacted in 1994.
2. **More Case Law Expected to Facilitate Interpretation.** As more states enact RULLCA, a body of jurisprudence will develop, providing guidance and certainty that will make formation of LLCs in states that adopt RULLCA more attractive.
3. **More Tax Revenues.** Many LLCs that conduct business in New York are currently formed in Delaware or other jurisdictions. The Committee believes that if RULLCA is enacted in New York, this State would become a more attractive jurisdiction for the formation of LLCs, which would benefit New York by generating increased tax revenues. For example, owing in large measure to the flexibility afforded by Delaware’s limited liability company statute, the number of LLCs formed in Delaware grew by almost 63% from 68,641 in fiscal 2004 to 111,820 in fiscal 2007, generating \$92.0 million in tax revenue. By contrast, the number of LLCs formed in New York grew by only 16%, from 42,798 to 49,620, during the same period. The Committee believes that this significantly smaller growth rate is attributable in part to lack of flexibility in the current New York LLC statute, as compared to the Delaware LLC statute. While distinct from the Delaware LLC statute, RULLCA would afford flexibility that the current New York LLC statute lacks.
4. **Addresses Matters Where New York’s LLC Statute is Silent.** NYLLCL is silent on a variety of important matters, requiring litigation and the development of case law over time to establish the rights and obligations of the LLC’s members and managers. RULLCA provides definitive standards to address these matters.

5. *Highlights of Certain Provisions That Improve Upon New York's LLC Statute.*

The following are specific provisions of RULLCA that illustrate a few of the benefits that adopting RULLCA would provide:

- RULLCA sets forth a clear standard of conduct for members and managers and a clear articulation of what fiduciary duties a manager owes, while at the same time giving the members the opportunity to provide by agreement for appropriate exceptions. NYLLCL currently specifies only that managers act in good faith and with a reasonable degree of care.
- RULLCA permits members of an LLC to pursue derivative claims on behalf of the LLC and establishes procedures that must be followed to pursue such claims. NYLLCL is currently silent with respect to derivative claims.
- RULLCA would permit oral operating agreements. Although the Committee would generally recommend that members commit their agreement to writing, we believe that members should be permitted to form a limited liability company without a written agreement. NYLLCL currently requires that a written agreement must be adopted within 90 days of organization, but the consequences of a failure to do so are uncertain. Removing this requirement would also mean that there would be no need to incur the cost of creating a written operating agreement for a single member LLC.
- RULLCA clarifies that LLCs may be formed for non-profit purposes, benefitting not-for-profit organizations in our State.
- RULLCA would dispense with the publication requirement for LLCs, a requirement that is unique to New York, is not applicable to corporations, and requires that persons forming LLCs must incur unnecessary costs without serving any public interest.
- RULLCA allows that an LLC may be formed before its members have been identified. Participants in sophisticated legal transactions desire at times to form entities prior to a final determination of the particular entity's owners. New York law currently permits the formation of a corporation upon the filing of the certificate of incorporation, without any requirement that the entity actually have shareholders at the time of such filing and there is no compelling reason to treat LLCs in a different manner.
- RULLCA adopts a framework for dealing with known claims and barring the assertion of unknown claims. This framework is similar to what New York provides for corporations. NYLLCL currently contains no comparable procedure for LLCs.

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**Exhibit A**

**Comparison of the Key Provisions of the Revised Uniform Limited Liability Company Act (“RULLCA”) to New York’s Limited Liability Company Law (“NYLLCL”)<sup>1</sup>**

<b>Feature</b>	<b>RULLCA</b>	<b>NYLLCL</b>	<b>Comments</b>
Purpose	§ 104(b) – A limited liability company may have any lawful purpose, regardless of whether for profit.	§ 201 – A limited liability company may be formed under this chapter for any lawful business purpose...	Unlike NYLLCL, RULLCA expressly permits the use of LLCs for not-for-profit enterprises.
Duration	§ 104(c) – A limited liability company has perpetual duration.  § 701(a) – A limited liability company is dissolved, and its activities must be wound up, upon the occurrence of any of the following:  (1) an event or circumstance that the operating agreement states causes dissolution;  [other events triggering dissolution]	§ 701(a) – A limited liability company is dissolved and its affairs shall be wound up upon the first to occur of the following:  (1) the latest date on which the limited liability company is to dissolve, if any, provided in the articles of organization, or the time specified in the operating agreement, but if no such date is provided in the articles of organization and if no such time is specified in the operating agreement, then the limited liability company shall have a perpetual existence;  [other events triggering dissolution]	Under both RULLCA and NYLLCL, an LLC continues perpetually, unless the operating agreement or statute specifies an earlier time for dissolution.
Governing Law (Domestic Limited Liability Companies)	§ 106 – The law of this state governs: (1) the internal affairs of a limited liability company; and (2) the liability of a member as member and a manager as manager for the debts, obligations, or other liabilities of a limited liability company.  §110(c)(2) – An operating agreement may not vary the law applicable under Section 106.	Silent	Because NYLLCL is silent, generally applicable conflict law rules would apply. RULLCA would provide a useful statutory clarification.
Supplemental Law	§ 107 – Unless displaced by particular provisions of this [act], the principles of law and equity supplement this [act].	Silent	The New York courts’ interpretation of NYLLCL have the same effect as RULLCA § 107.
Limited Liability Companies without Members (“Shelf-LLCs”)	§ 201 –  (a) – One or more persons may act as organizers to form a limited liability company by signing and delivering to the [Secretary of State] for filing a certificate of organization  (b) – A certificate of organization must state... (3) if the company will have no members when the [Secretary of State] files	§ 203 –  (a) One or more persons may act as an organizer or organizers to form a limited liability company by [executing and filing articles of organization with the department of state].  (c) – At the time of its formation, a limited liability company must have at least one member.	Under NYLLCL, an LLC cannot be formed without at least one member, and will generally be dissolved if there ceases to be at least one member for at least 180 days.  Under RULLCA, an LLC need not have a member at the time of formation but the certificate of organization becomes void if a second filing, stating that the company has a member, is not

<sup>1</sup> This chart compares NYLLCL to the version of RULLCA approved by the National Conference of Commissioners on Uniform State Laws. Certain of the legislative provisions have been paraphrased for clarity.

Feature	RULLCA	NYLLCL	Comments
	<p>the certificate, a statement to that effect.</p> <p>(d) – Unless the filed certificate of organization contains the statement as provided in subsection (b)(3) . . . (1) A limited liability company is formed when the [Secretary of State] has filed the certificate of organization and the company has at least one member, unless the certificate states a delayed effective date pursuant to Section 205(c).</p> <p>(e) – If a filed certificate of organization contains a statement as provided in subsection (b)(3), the following rules apply:</p> <p>(1) The certificate lapses and is void unless, within [90] days from the date the [Secretary of State] files the certificate, an organizer signs and delivers to the [Secretary of State] for filing a notice stating: (A) that the limited liability company has at least one member; and (B) the date on which a person or persons became the company’s initial member or members.</p> <p>(2) If an organizer complies with paragraph (1), a limited liability company is deemed formed as of the date of initial membership stated in the notice delivered pursuant to paragraph (1)...</p> <p>§ 701(a) – A limited liability company is dissolved, and its activities must be wound up, upon the occurrence of . . . (3) the passage of 90 consecutive days during which the company has no members...</p>	<p>(d) - A limited liability company is formed at the time of the filing of the initial articles of organization with the department of state or at any later time specified in the articles of organization, not to exceed sixty days from the date of such filing.</p> <p>§ 701(a)(4) – A limited liability company is dissolved and its affairs shall be wound up . . . at any time there are no members, provided that, unless otherwise provided in the operating agreement, the limited liability company is not dissolved and is not required to be wound up if, within one hundred eighty days or such other period as is provided for in the operating agreement after the occurrence of the event that terminated the continued membership of the last remaining member, the legal representative of the last remaining member agrees in writing to continue the limited liability company and to the admission of the legal representative of such member or its assignee to the limited liability company as a member, effective as of the occurrence of the event that terminated the continued membership of the last remaining member....</p>	<p>made within 90 days. In addition, an LLC will generally be dissolved if there ceases to be at least one member for at least 90 days.</p>
<p>Becoming a Member</p>	<p>§ 102(11) – “Member” means a person that has become a member of a limited liability company under Section 401 and has not dissociated under Section 602.</p> <p>§ 401 –</p> <p>(a) If a limited liability company is to have only one member upon formation, the person becomes a member as agreed by that person and the organizer of the company. . .</p> <p>(b) If a limited liability company is to have more than one member upon formation, those persons become members as agreed by the persons before the formation of the company. . .</p> <p>(c) If a filed certificate of organization contains the statement required by Section 201(b)(3), a person becomes an initial</p>	<p>§ 602 –</p> <p>(a) A person becomes a member of a limited liability company on the later of:</p> <p>(1) the effective date of the initial articles of organization; or</p> <p>(2) the date as of which the person becomes a member pursuant to this section or the operating agreement...</p> <p>(b) After the effective date of a limited liability company's initial articles of organization, a person may be admitted as a member:</p> <p>(1) in the case of a person acquiring a membership interest directly from the limited liability company, upon compliance with the operating agreement or, if the operating agreement does not so provide, upon</p>	<p>In the absence of a merger, consolidation or non-existence of members, RULLCA would permit membership only as provided in the operating agreement or <i>with the consent of all members</i>.</p> <p>NYLLCA would permit membership only as provided in the operating agreement or, if the operating agreement does not so provide, <i>with the approval of a majority in interest of the members in the case of a person acquiring an interest directly from the LLC</i>.</p>

Feature	RULLCA	NYLLCL	Comments
	<p>member of the limited liability company with the consent of a majority of the organizers. . .</p> <p>(d) After formation of a limited liability company, a person becomes a member:</p> <p>(1) as provided in the operating agreement;</p> <p>(2) as the result of a transaction effective under Article 10 [mergers or consolidations];</p> <p>(3) with the consent of all the members; or</p> <p>(4) if, within 90 consecutive days after the company ceases to have any members: (A) the last person to have been a member, or the legal representative of that person, designates a person to become a member; and (B) the designated person consents to become a member.</p>	<p>the vote or written consent of a majority in interest of the members;</p> <p>(2) in the case of an assignee of a membership interest of a member who has the power, as provided in the operating agreement, to grant the assignee the right to become a member, upon the exercise of that power and compliance with any conditions limiting the grant or exercise of the power; or</p> <p>(3) unless otherwise provided in an agreement of merger or consolidation or the operating agreement, in the case of a person acquiring a membership interest in a surviving or resulting limited liability company pursuant to a merger or consolidation approved in accordance with subdivision (b) of section one thousand one of this chapter, at the time provided in and upon compliance with the operating agreement of the surviving or resulting limited liability company.</p>	
Freedom of Contract	<p>Silent, although § 110 establishes certain matters that an operating agreement may not do (as discussed below). § 112(d) provides that in cases of conflict between the articles and the operating agreement, the articles control as to third parties reasonably relying thereon and the operating agreement controls as to members.</p>	<p>§ 417(a) of NYLLCL states that the operating agreement may contain any provision not inconsistent with law or articles.</p>	<p>Both statutes allow significant freedom of contract.</p>
Management by Manager	<p>§ 102(10) – “Manager-managed limited liability company” means a limited liability company that qualifies under Section 407(a) [which requires that the operating agreement expressly state that the company will be manager-managed]</p> <p>§ 407(c) – [Except as otherwise provided in the operating agreement] [i]n a manager-managed limited liability company, the following rules apply:</p> <p>(1) Except as otherwise expressly provided in this [act], any matter relating to the activities of the company is decided exclusively by the managers.</p> <p>(2) Each manager has equal rights in the management and conduct of the activities of the company.</p> <p>(3) A difference arising among managers as to a matter in the ordinary course of the activities of the company may be decided by a majority of the managers.</p> <p>(4) The consent of all members is required to:</p> <p>(A) sell, lease, exchange, or otherwise dispose of all, or substantially all, of the company’s property, with or without the</p>	<p>§ 401(a) – Unless the articles of organization provides for management of the limited liability company by a manager or managers or a class or classes of managers, management of the limited liability company shall be vested in its members...</p> <p>§ 408(b) – Except as provided in the operating agreement and in accordance with section four hundred nineteen of this article, the managers shall manage the limited liability company by the affirmative vote of a majority of the managers.</p> <p>§ 410 –</p> <p>(a) Unless otherwise provided in the operating agreement, a manager may, but need not, be a member of the limited liability company.</p> <p>(b) The operating agreement may prescribe qualifications for managers.</p> <p>§ 413 –</p> <p>(a) Except as provided in the operating</p>	<p>Under NYLLCL, unless otherwise provided in the operating agreement, managers must be elected annually by a majority in interest of members (determined based on their proportionate shares of the LLC’s current profits) and serve until a successor is elected or until removed by a majority in interest.</p> <p>In contrast, managers may be appointed (and removed) under RULLCA at any time by consent of a majority of members.</p> <p>Under both NYLLCL and RULLCA, a manager may be removed at any time without notice or cause (although removal may constitute a breach of contract).</p>

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	<p>good will, outside the ordinary course of the company’s activities; and</p> <p>(B) approve a merger, conversion, or domestication under [Article] 10;</p> <p>(C) undertake any other act outside the ordinary course of the company’s activities; and</p> <p>(D) amend the operating agreement.</p> <p>(5) A manager may be chosen at any time by the consent of a majority of the members and remains a manager until a successor has been chosen, unless the manager at an earlier time resigns, is removed, or dies, or, in the case of a manager that is not an individual, terminates. A manager may be removed at any time by the consent of a majority of the members without notice or cause.</p> <p>(6) A person need not be a member to be a manager, but the dissociation of a member that is also a manager removes the person as a manager. If a person that is both a manager and a member ceases to be a manager, the cessation does not by itself dissociate the person as a member.</p> <p>(7) A person’s ceasing to be a manager does not discharge any debt, obligation, or other liability to the limited liability company or members which the person incurred while a manager.</p>	<p>agreement, if the articles of organization provides that management shall be vested in one or more managers, the members shall vote in accordance with section four hundred two of this article [by a majority in interest, determined in proportion to each member’s share of current profits] to designate or elect annually the manager or managers of the limited liability company.</p> <p>(b) Each manager shall hold the office and have the terms (which may be unlimited) and responsibilities accorded to him or her by the members and set out in the operating agreement until his or her successor has been elected and qualified or until his or her earlier resignation or removal.</p> <p>(d) The number of managers may be increased or decreased by amendment to and in the manner provided in the operating agreement.</p> <p>§ 414 – Except as provided in the operating agreement, any or all managers of a limited liability company may be removed or replaced with or without cause by a vote of a majority in interest of the members entitled to vote thereon.</p>	
Management by Members	<p>§ 102(12) – “Member-managed limited liability company” means a limited liability company that is not a manager-managed limited liability company.</p> <p>§ 407 –</p> <p>(b) In a member-managed limited liability company, the following rules apply [unless the operating agreement states otherwise]:</p> <p>(1) The management and conduct of the company are vested in the members.</p> <p>(2) Each member has equal rights in the management and conduct of the company’s activities.</p> <p>(3) A difference arising among members as to a matter in the ordinary course of the activities of the company may be decided by a majority of the members.</p> <p>(4) An act outside the ordinary course of the activities of the company may be undertaken only with the consent of all members.</p> <p>(5) The operating agreement may be amended only with the consent of all members.</p> <p>(d) An action requiring the consent of members under this [act] may be taken without a meeting, and a member may appoint a proxy or other agent to consent or otherwise act for the member...</p> <p>(f) This [act] does not entitle a member to</p>	<p>§ 401 –</p> <p>(a) Unless the articles of organization provides for management of the limited liability company by a manager or managers or a class or classes of managers, management of the limited liability company shall be vested in its members who shall manage the limited liability company in accordance with this chapter, subject to any provisions in the articles of organization or the operating agreement and sections four hundred eighteen of this article granting or withholding the management powers or responsibilities of one or more members or classes of members.</p> <p>(b) If management of a limited liability company is vested in its members, then (i) any such member exercising such management powers or responsibilities shall be deemed to be a manager for purposes of applying the provisions of this chapter, unless the context otherwise requires, and (ii) any such member shall have and be subject to all of the duties and liabilities of a manager provided in this chapter.</p>	<p>Under both RULLCA and NYLLCL, an LLC is by default managed by its members.</p> <p>RULLCA defines a separate set of rules for member-managers and manager-managers. NYLLCL generally deems members of member-managed LLCs to be managers, and holds that members of member-managed LLCs are subject to the same duties and liabilities as manager-managers.</p>

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	remuneration for services performed for a member-managed limited liability company...	<p>§ 402 –</p> <p>(a) Except as provided in the operating agreement, in managing the affairs of the limited liability company ... or voting on any other matter that requires the vote at a meeting of the members ... each member of a limited liability company shall vote in proportion to such member's share of the current profits of the limited liability company...</p> <p>(b) Except as provided in the operating agreement, any member may vote in person or by proxy.</p> <p>(c) Except as provided in the operating agreement ... the vote of a majority in interest of the members entitled to vote thereon shall be required to [admit members, incur indebtedness or adopt/amend/restate/revoke the articles of organization or the operating agreement].</p> <p>(d) Except as provided in the operating agreement ... the vote of at least a majority in interest of the members entitled to vote thereon shall be required to [approve a dissolution, sale of substantially all of the assets, or approve a merger/consolidation].</p>	
Standard of Conduct; Fiduciary Duties	<p>§ 409 –</p> <p>(a) A member of a member-managed [or a manager of a manager-managed] limited liability company owes to the company and, subject to Section 901(b), the other members the fiduciary duties of loyalty and care stated in subsections (b) and (c).</p> <p>(b) the duty of loyalty of a member in a member-managed [or a manager in a manager-managed] limited liability company includes the duties:</p> <p>(1) to account to the company and to hold as trustee for it any property, profit, or benefit derived by the member:</p> <p>(A) in the conduct or winding up of the company's activities;</p> <p>(B) from a use by the member of the company's property; or</p> <p>(C) from the appropriation of a limited liability company opportunity;</p> <p>(2) to refrain from dealing with the company in the conduct or winding up of the company's activities as or on behalf of a person having an interest adverse to the company; and</p>	<p>§ 409 –</p> <p>(a) A manager [of a manager-managed, or member of a member-managed limited liability company] shall perform his or her duties ... in good faith and with that degree of care that an ordinarily prudent person in a like position would use under similar circumstances.</p> <p>(b) In performing his or her duties, a manager [of a manager-managed, or member of a member-managed limited liability company] shall be entitled to rely on information, opinions, reports or statements, including financial statements and other financial data, in each case prepared or presented by [various enumerated people].</p> <p>§ 401(b) – If management of a limited liability company is vested in its members, then (i) any such member exercising such management powers or responsibilities shall be deemed to be a manager for purposes of applying the provisions of this chapter, unless the context otherwise requires, and</p>	<p>RULLCA explicitly imposes a duty of loyalty on members and managers. NYLLCL requires managers to perform their duties in good faith, but otherwise imposes no duty of loyalty.</p> <p>Under RULLCA, certain elements of the duty of loyalty are specified on a non-exclusive basis. However, under NYLLCL, the requirements of the duty of loyalty are not specified and therefore left to common law (except that § 411 provides that a self-dealing transaction between the LLC and an interested manager is not void or voidable for this reason alone, even if the interested manager voted to approve such transaction; provided that such manager's relation to the transaction was disclosed to the members or managers prior to the vote on the transaction).</p> <p>NYLLCL and RULLCA both impose a duty of care on members and managers.</p>

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	<p>(3) to refrain from competing with the company in the conduct of the company’s activities before the dissolution of the company.</p> <p>(c) Subject to the business judgment rule, the duty of care of a member of a member-managed [or a manager of a manager-managed] limited liability company in the conduct and winding up of the company’s activities is to act with the care that a person in a like position would reasonably exercise under similar circumstances and in a manner the member reasonably believes to be in the best interests of the company. In discharging this duty, a member may rely in good faith upon opinions, reports, statements, or other information provided by another person that the member reasonably believes is a competent and reliable source for the information.</p> <p>(d) A member in a member-managed limited liability company or a manager-managed limited liability company shall discharge the duties under this [act] or under the operating agreement and exercise any rights consistently with the contractual obligation of good faith and fair dealing.</p> <p>(e) It is a defense to a claim under subsection (b)(2) and any comparable claim in equity or at common law that the transaction was fair to the limited liability company.</p> <p>(f) All of the members of a member-managed limited liability company or a manager-managed limited liability company may authorize or ratify, after full disclosure of all material facts, a specific act or transaction that otherwise would violate the duty of loyalty.</p>	<p>(ii) any such member shall have and be subject to all of the duties and liabilities of a manager provided in this chapter.</p>	<p>NYLLCL’s “prudent person” rule may be interpreted more strictly than the gross negligence standard under the Delaware General Corporation Law, for example, which may discourage persons from becoming managers.</p> <p>Although RULLCA imposes a similar standard, it permits the duty of care standard to be varied in the operating agreement (generally, unless manifestly unreasonable) and, in any event, reduces the risk to managers by explicitly incorporating the business judgment rule.</p> <p>RULLCA is also advantageous in that it articulates the defense of fairness (§ 409(e)).</p> <p>Both RULLCA and NYLLCL are silent as to the duties owed to a non-member assignee/transferee of a membership interest (therefore left to equity).</p>
Operating Agreement	<p>§ 102(13) – “Operating agreement” means the agreement, whether or not referred to as an operating agreement and whether oral, in a record, implied, or in any combination thereof, of all the members of a limited liability company, including a sole member, concerning the matters described in Section 110(a) [which establishes that the operating agreement governs (1) relations among and between the members as members and between the members and the limited liability company, (2) the rights and duties of the manager, (3) the activities of the company and the conduct of those activities; and (4) the means and conditions for amending the operating agreement].</p> <p>§ 110(c) – An operating agreement may not: vary a limited liability company’s capacity to sue and be sued; vary the applicable law; vary the court’s power to require certain parties to execute and file requisite documents; subject to § 110(d) through (g), eliminate the duty of loyalty, the duty of</p>	<p>§ 102(u) – “Operating agreement” means any written agreement of the members concerning the business of a limited liability company and the conduct of its affairs and complying with section four hundred seventeen of this chapter.</p> <p>§ 417(a) – Subject to the provisions of this chapter, the members of a limited liability company shall adopt a written operating agreement that contains any provisions not inconsistent with law or its articles of organization relating to (i) the business of the limited liability company, (ii) the conduct of its affairs and (iii) the rights, powers, preferences, limitations or responsibilities of its members, managers, employees or agents, as the case may be.</p> <p>The operating agreement may set forth a provision eliminating or limiting the</p>	<p>Sections 102(u) and 417(a) of the NYLLCL provide that members “shall” adopt a “written” agreement among all the members governing LLC business and affairs. Although it is implied, NYLLCL is silent as to whether a single member must adopt an operating agreement. RULLCA allows for oral and ‘sole member’ operating agreements.</p> <p>Although § 409 of NYLLCL provides a good faith and ordinarily prudent person standard of care as the statutory minimum that may not be waived, § 417(a) allows that managers may be exculpated (by eliminating or limiting personal liability) for breaches of fiduciary duties other than as a result of bad faith, intentional</p>



Feature	RULLCA	NYLLCL	Comments
	<p>care, or any other fiduciary duty or the contractual obligation of good faith and fair dealing; unreasonably restrict the duties and rights stated in § 410; vary the power of a court to decree dissolution; vary the requirement to wind up a limited liability company's business; unreasonably restrict the right of a member to maintain an action; restrict the right to approve a merger or similar transaction; or except as provided in § 112(b), restrict the rights of a person other than a member or manager.</p> <p>Duty Modification:</p> <p>§ 110(d) – If not manifestly unreasonable, the operating agreement may:</p> <p>(1) restrict or eliminate the duty:</p> <p>(A) as required in Section 409(b)(1) and (g), to account to the limited liability company and to hold as trustee for it any property, profit, or benefit derived by the member in the conduct or winding up of the company's business, from a use by the member of the company's property, or from the appropriation of a limited liability company opportunity;</p> <p>(B) as required in Section 409(b)(2) and (g), to refrain from dealing with the company in the conduct or winding up of the company's business as of or on behalf of a party having an interest adverse to the company; and</p> <p>(C) as required by Section 409(b)(3) and (g), to refrain from competing with the company in the conduct of the company's business before the dissolution of the company;</p> <p>(2) identify specific types or categories of activities that do not violate the duty of loyalty;</p> <p>(3) alter the duty of care, except to authorize intentional misconduct or knowing violation of law;</p> <p>(4) alter any other fiduciary duty, including eliminating particular aspects of that duty; and</p> <p>(5) prescribe the standards by which to measure the performance of the contractual obligation of good faith and fair dealing under Section 409(d).</p> <p>§ 110(e) – The operating agreement may specify the method by which a specific act or transaction that would otherwise violate the duty of loyalty may be authorized or ratified by one or more disinterested and independent persons after full disclosure of all material facts.</p> <p>Effect on LLC and Later Members</p> <p>§ 111 –</p>	<p>personal liability of managers to the limited liability company or its members for damages for any breach of duty in such capacity, provided that no such provision shall eliminate or limit:</p> <p>(1) the liability of any manager if a judgment or other final adjudication adverse to him or her establishes that his or her acts or omissions were in bad faith or involved intentional misconduct or a knowing violation of law or that he or she personally gained in fact a financial profit or other advantage to which he or she was not legally entitled or that with respect to a distribution the subject of subdivision (a) of section five hundred eight of this chapter his or her acts were not performed in accordance with section four hundred nine of this article; or</p> <p>(2) the liability of any manager for any act or omission prior to the adoption of a provision authorized by this subdivision.</p>	<p>misconduct, knowing violation of law, unjust enrichment and, only in the case of distributions under § 508 (i.e., those which result in the liabilities of the LLC to third parties exceeding its assets), conduct inconsistent with the negligence standards of § 409.</p> <p>RULLCA allows the duty of care and duty of loyalty to be modified (unless the modification is manifestly unreasonable) but not eliminated.</p> <p>RULLCA provides useful clarification of the effect of the operating agreement on the LLC, later members, and third parties. These issues are not addressed in NYLLCL.</p>

Feature	RULLCA	NYLLCL	Comments
	<p>(a) A limited liability company is bound by and may enforce the operating agreement, whether or not the company has itself manifested assent to the operating agreement.</p> <p>(b) A person that becomes a member of a limited liability company is deemed to assent to the operating agreement.</p> <p>(c) Two or more persons intending to become the initial members of a limited liability company may make an agreement providing that upon the formation of the company the agreement will become the operating agreement. One person intending to become the initial member of a limited liability company may assent to terms providing that upon the formation of the company the terms will become the operating agreement.</p> <p>Effect on Third Parties</p> <p>§ 112 –</p> <p>(a) An operating agreement may specify that its amendment requires the approval of a person that is not a party to the operating agreement or the satisfaction of a condition.</p> <p>(b) The obligations of a limited liability company and its members to a person in the person’s capacity as a transferee or dissociated member are governed by the operating agreement. Subject only to any court order issued under Section 503(b)(2) to effectuate a charging order, an amendment to the operating agreement made after a person becomes a transferee or dissociated member is effective with regard to any debt, obligation, or other liability of the limited liability company or its members to the person in the person’s capacity as a transferee or dissociated member.</p>		
Distributions	<p>§ 404(a) – Any distributions made by a limited liability company before its dissolution and winding up must be in equal shares among members and dissociated members, except to the extent necessary to comply with any transfer effective under Section 502 and any charging order in effect under Section 503.</p>	<p>§ 503 – The profits and losses of a limited liability company shall be allocated among the members, and among the classes of members, if any, in the manner provided in the operating agreement. If the operating agreement does not so provide, profits and losses shall be allocated on the basis of the value, as stated in the records of the limited liability company if so stated, of the contributions of each member, but not including defaulted obligations to make contributions, to the extent they have been received by or promised to the limited liability company and have not been returned to any such member.</p>	<p>Under NYLLCL, distributions are allocated based on the value of the members’ contributions as stated in the records unless the operating agreement provides otherwise.</p> <p>Under RULLCA, distributions are made per capita unless the operating agreement provides otherwise.</p>
Liability of Members and	§ 304 –	§ 609 –	Under both RULLCA and NYLLCL, the members and

Feature	RULLCA	NYLLCL	Comments
Managers	<p>(a) The debts, obligations, or other liabilities of a limited liability company, whether arising in contract, tort, or otherwise:</p> <p>(1) are solely the debts, obligations, or other liabilities of the company; and</p> <p>(2) do not become the debts, obligations, or other liabilities of a member or manager solely by reason of the member acting as a member or manager acting as a manager.</p> <p>(b) The failure of a limited liability company to observe any particular formalities relating to the exercise of its powers or management of its activities is not a ground for imposing liability on the members or managers for the debts, obligations, or other liabilities of the company.</p>	<p>(a) Neither a member of a limited liability company, a manager of a limited liability company managed by a manager or managers nor an agent of a limited liability company (including a person having more than one such capacity) is liable for any debts, obligations or liabilities of the limited liability company or each other, whether arising in tort, contract or otherwise, solely by reason of being such member, manager or agent or acting (or omitting to act) in such capacities or participating (as an employee, consultant, contractor or otherwise) in the conduct of the business of the limited liability company.</p> <p>(b) Notwithstanding the provisions of subdivision (a) of this section, all or specified members of a limited liability company may be liable in their capacity as members for all or specified debts, obligations or liabilities of a limited liability company if (1) a statement to such effect is specifically contained in the articles of organization of the limited liability company and (2) any such member so liable shall have (i) specifically consented in writing (A) to the adoption of such provisions or (B) to be bound by such provision or (ii) specifically voted for the adoption of such provision. The absence of either such statement in the articles of organization or such consent or vote of any such member shall in no way affect or impair the ability of a member to act as a guarantor or a surety for, provide collateral for or otherwise be liable for, the debts, obligations or liabilities of a limited liability company as authorized pursuant to section six hundred eleven of this article.</p>	managers are not liable for the debts, obligations or other liabilities of the LLC.
Agency	<p>§ 301 –</p> <p>(a) A member is not an agent of a limited liability company solely by reason of being a member.</p> <p>(b) A person’s status as a member does not prevent or restrict law other than this [act] from imposing liability on a limited liability company because of the person’s conduct.</p> <p>§ 302(a) – A limited liability company may deliver to the [Secretary of State] for filing a statement of authority. The statement: ...</p> <p>(2) with respect to any position that exists in or with respect to the company, may state the authority, or limitations on the authority, of all persons holding the position to: ... (B) enter into ... transactions on behalf of, or otherwise act for or bind the company.</p>	<p>Member-Managed LLCs</p> <p>§ 412(a) – Unless the articles of organization of a limited liability company provide that management shall be vested in a manager or managers, every member is an agent of the limited liability company for the purpose of its business, and the act of every member, including the execution in the name of the limited liability company of any instrument, for apparently carrying on in the usual way the business of the limited liability company, binds the limited liability company, unless (i) the member so acting has in fact no authority to act for the limited liability company in the particular matter and (ii) the person with whom he or she is dealing has knowledge of the fact that the member</p>	<p>Under NYLLCL, members of a member-managed LLC are generally held to be agents of the LLC and the actions of a member generally bind the LLC.</p> <p>Under RULLCA, members are explicitly stated not to be agents solely by reason of being members, although each member has equal rights in the management of a member-managed LLC.</p> <p>RULLCA allows for the public filing of a ‘statement of authority’ to provide confirmation of the authority of a person to bind the LLC.</p>

Feature	RULLCA	NYLLCL	Comments
		<p>has no such authority.</p> <p>Manager-Managed LLCs</p> <p>§ 412(b) – If the articles of organization of a limited liability company provide that management shall be vested in one or more managers:</p> <p>(1) no member, solely by reason of being a member, is an agent of the limited liability company for the purpose of its business except to the extent that authority has been delegated to such member by the manager or managers or by the provisions of the operating agreement; and</p> <p>(2) every manager is an agent of the limited liability company for the purpose of its business, and the act of every manager, including the execution in the name of the limited liability company of any instrument, for apparently carrying on in the usual way the business of the limited liability company binds the limited liability company, unless (A) the manager acting has in fact no authority to act for the limited liability company in the particular matter and (B) the person with whom he or she is dealing has knowledge of the fact that the manager has no such authority.</p> <p>Member-Managed and Manager-Managed LLCs</p> <p>§ 412 –</p> <p>(c) An act of a member or manager that is not apparently for the carrying on of the business of the limited liability company in the usual way does not bind the limited liability company unless authorized in fact by the limited liability company in the particular matter.</p> <p>(d) No act of a member, manager or other agent of a limited liability company in contravention of a restriction on authority shall bind the limited liability company to persons having knowledge of the restriction.</p>	
Indemnification	§ 408(a) – A limited liability company shall reimburse for any payment made and indemnify for any debt, obligation, or other liability incurred by a member of a member-managed company or the manager of a manager-managed company in the course of the member’s or manager’s activities on behalf of the company, if, in making the payment or incurring the debt, obligation, or other liability, the member or manager complied with the duties stated in Sections 405 and 409.	§ 420 – Subject to the standards and restrictions, if any, set forth in its operating agreement, a limited liability company may, and shall have the power to, indemnify and hold harmless, and advance expenses to, any member, manager or other person, or any testator or intestate of such member, manager or other person, from and against any and all claims and demands whatsoever; provided, however, that no indemnification may be made to or on	<p>Under NYLLCL, LLCs “may” indemnify members, managers, or “other persons” absent final judgment that person acted (i) in bad faith or (ii) received improper personal gain</p> <p>Under RULLCA, an LLC must indemnify members and managers for expenses or liabilities incurred in the course of that person’s activities on behalf of the LLC if fiduciary</p>

Feature	RULLCA	NYLLCL	Comments
		<p>behalf of any member, manager or other person if a judgment or other final adjudication adverse to such member, manager or other person establishes (a) that his or her acts were committed in bad faith or were the result of active and deliberate dishonesty and were material to the cause of action so adjudicated or (b) that he or she personally gained in fact a financial profit or other advantage to which he or she was not legally entitled.</p>	<p>duties and information obligations are not violated.</p>
<p>Membership Interest Assignment</p>	<p>§ 502 –</p> <p>(a) A transfer, in whole or in part, of a transferable interest:</p> <p>(1) is permissible</p> <p>(2) does not by itself cause a member’s dissociation or a dissolution and winding up of the limited liability company’s activities; and</p> <p>(3) subject to Section 504 [dealing with death of a member], does not entitle the transferee to:</p> <p>(A) participate in the management or conduct of the company’s activities; or</p> <p>(B) except as otherwise provided in subsection (c), have access to records or other information concerning the company’s activities.</p> <p>(b) A transferee has the right to receive, in accordance with the transfer, distributions to which the transferor would otherwise be entitled.</p> <p>(c) In a dissolution and winding up of a limited liability company, a transferee is entitled to an account of the company’s transactions only from the date of dissolution.</p> <p>(e) A limited liability company need not give effect to a transferee’s rights under this section until the company has notice of the transfer.</p> <p>(f) A transfer of a transferable interest in violation of a restriction on transfer contained in the operating agreement is ineffective as to a person having notice of the restriction at the time of transfer.</p> <p>(g) Except as otherwise provided in Section 602(4)(B) [dealing with expulsion of a member who transfers his entire interest], when a member transfers a transferable interest, the transferor retains the rights of a member other than the interest in distributions transferred and retains all duties and obligations of a member.</p> <p>(h) When a member transfers a transferable interest to a person that becomes a member with respect to the transferred interest, the transferee is liable for the member’s</p>	<p>§ 603 –</p> <p>(a) Except as provided in the operating agreement,</p> <p>(1) a membership interest is assignable in whole or in part;</p> <p>(2) an assignment of a membership interest does not dissolve a limited liability company or entitle the assignee to participate in the management and affairs of the limited liability company or to become or to exercise any rights or powers of a member;</p> <p>(3) the only effect of an assignment of membership interest is to entitle the assignee to receive, to the extent assigned, the distributions and allocations of profits and losses to which the assignor would be entitled; and</p> <p>(4) a member ceases to be a member and to have the power to exercise any rights or powers of a member upon assignment of all of his or her membership interest. Unless otherwise provided in the operating agreement, the pledge of, or the granting of a security interest, lien or other encumbrance in or against, any or all of the membership interest of a member shall not cause the member to cease to be a member or to cease to have the power to exercise any rights or powers of a member.</p> <p>(c) Unless otherwise provided in an operating agreement and except to the extent assumed by agreement, until the time, if any, that an assignee of a membership interest becomes a member, the assignee shall have no liability as a member solely as a result of the assignment.</p>	<p>NYLLCL and RULLCA are similar in allowing a membership interest to be assigned/transferred, thereby entitling the assignee or transferee to receive distributions. In each case, the assignee or transferee is not entitled to exercise any non-economic rights of a member (e.g. voting) and does not have the obligations of a member until he or she becomes a member.</p>

Feature	RULLCA	NYLLCL	Comments
	<p>obligations under Sections 403 and 406(c) [contributions and improper distributions] known to the transferee when the transferee becomes a member.</p>		
<p>Member Dissociation</p>	<p>§ 601(a) – A person has the power to dissociate as a member at any time, rightfully or wrongfully, by withdrawing as a member by express will...</p> <p>§ 603 –</p> <p>(a) When a person is dissociated as a member of a limited liability company: ... (3) subject to Section 504 and [Article] 10, any transferable interest owned by the person immediately before dissociation in the person’s capacity as a member is owned by the person solely as a transferee.</p> <p>(b) – A person’s dissociation as a member of a limited liability company does not of itself discharge the person from any debt, obligation, or other liability to the company or the other members which the person incurred while a member.</p>	<p>§ 606(a) – A member may withdraw as a member of a limited liability company only at the time or upon the happening of events specified in the operating agreement and in accordance with the operating agreement. Notwithstanding anything to the contrary under applicable law, unless an operating agreement provides otherwise, a member may not withdraw from a limited liability company prior to the dissolution and winding up of the limited liability company.</p>	<p>RULLCA allows a member to dissociate at any time (but the member may be liable to the LLC for damages caused by the dissociation under §601(c) if the dissociation is ‘wrongful’ – e.g., in breach of an express provision of the operating agreement).</p> <p>A member who dissociates is treated as a “transferee” – i.e., entitled only to receive distributions.</p> <p>NYLLCL only allows a member to dissociate in accordance with the operating agreement.</p>
<p>Entity Dissolution (Non-Judicial)</p>	<p>§ 701(a) – A limited liability company is dissolved, and its activities must be wound up, upon the occurrence of any of the following:</p> <p>(1) an event or circumstance that the operating agreement states causes dissolution;</p> <p>(2) the consent of all the members;</p> <p>(3) the passage of 90 consecutive days during which the company has no members....</p>	<p>§ 701 –</p> <p>(a) A limited liability company is dissolved and its affairs shall be wound up upon the first to occur of the following:</p> <p>(1) the latest date on which the limited liability company is to dissolve, if any, provided in the articles of organization, or the time specified in the operating agreement, but if no such date is provided in the articles of organization and if no such time is specified in the operating agreement, then the limited liability company shall have a perpetual existence;</p> <p>(2) the happening of events specified in the operating agreement;</p> <p>(3) subject to any requirement in the operating agreement requiring approval by any greater or lesser percentage in interest of the members or class or classes or group or groups of members, the vote or written consent of at least a majority in interest of the members or, if there is more than one class or group of members, then by at least a majority in interest of each class or group of members;</p> <p>(4) at any time there are no members, provided that, unless otherwise provided in the operating agreement, the limited liability company is not dissolved and is not required to be wound up if, within one hundred eighty days or such other period as is provided for in the operating agreement after the occurrence of the event that terminated the continued</p>	<p>RULLCA requires the unanimous consent of the members to dissolve the company, whereas NYLLCL requires only the vote of a majority in interest of the members. Each of RULLCA and NYLLCL permit the operating agreement to vary this requirement.</p>

Feature	RULLCA	NYLLCL	Comments
		<p>membership of the last remaining member, the legal representative of the last remaining member agrees in writing to continue the limited liability company and to the admission of the legal representative of such member or its assignee to the limited liability company as a member, effective as of the occurrence of the event that terminated the continued membership of the last remaining member....</p> <p>(b) Unless otherwise provided in the operating agreement, the death, retirement, resignation, expulsion, bankruptcy or dissolution of any member or the occurrence of any other event that terminates the continued membership of any member shall not cause the limited liability company to be dissolved or its affairs to be wound up, and upon the occurrence of any such event, the limited liability company shall be continued without dissolution, unless within one hundred eighty days following the occurrence of such event, a majority in interest of all of the remaining members of the limited liability company or, if there is more than one class or group of members, then by a majority in interest of all the remaining members of each class or group of members, vote or agree in writing to dissolve the limited liability company.</p>	
Entity Dissolution (Judicial)	<p>§ 701 –</p> <p>(a) A limited liability company is dissolved ...</p> <p>(4) on application by a member, the entry by [appropriate court] of an order dissolving the company on the grounds that:</p> <p>(A) the conduct of all or substantially all of the company’s activities is unlawful; or</p> <p>(B) it is not reasonably practicable to carry on the company’s activities in conformity with the certificate of organization and the operating agreement; or</p> <p>(5) on application by a member, the entry by [appropriate court] of an order dissolving the company on the grounds that the managers or those members in control of the company:</p> <p>(A) have acted, are acting, or will act in a manner that is illegal or fraudulent; or</p> <p>(B) have acted or are acting in a manner that is oppressive and was, is, or will be directly harmful to the applicant.</p>	<p>§ 701(a) – A limited liability company is dissolved ... upon ... the entry of a decree of judicial dissolution under section seven hundred two of this article.</p> <p>§ 702 – On application by or for a member, the supreme court in the judicial district in which the office of the limited liability company is located may decree dissolution of a limited liability company whenever it is not reasonably practicable to carry on the business in conformity with the articles of organization or operating agreement. A certified copy of the order of dissolution shall be filed by the applicant with the department of state within thirty days of its issuance.</p>	<p>Both RULLCA and NYLLCL allow for judicial dissolution of an LLC if it is not reasonably practicable to carry on the LLC’s activities in conformity with the articles/certificate of organization or the operating agreement.</p> <p>RULLCA also allows for dissolution on the grounds of unlawful conduct by the LLC, or illegal, fraudulent, oppressive or harmful conduct by its management. There is no comparable provision in NYLLCL.</p>
Mergers	<p>§ 1002 –</p> <p>(a) A limited liability company may merge with one or more other constituent organizations ... if:</p> <p>(1) the governing statute of each of the other organizations authorizes the merger;</p>	<p>§ 1001(b) – Pursuant to an agreement of merger or consolidation and to the extent not expressly prohibited by law, a domestic limited liability company may merge or consolidate with or into one or more domestic limited liability companies or other business entities</p>	<p>RULLCA requires the consent of all members for a merger, whereas NYLLCL requires only a majority in interest. NYLLCL permits the operating agreement to vary this requirement.</p>

Feature	RULLCA	NYLLCL	Comments
	<p>(2) the merger is not prohibited by the law of a jurisdiction that enacted any of the governing statutes; and</p> <p>(3) each of the other organizations complies with its governing statute in effecting the merger.</p> <p>§ 1003(a) – Subject to Section 1014 [Restrictions on approval of Mergers, Conversion, and Domestications and, pursuant to Section 110, the operating agreement], a plan of merger must be consented to by all the members of a constituent limited liability company.</p>	<p>formed or organized under the laws of this state or any other state or the United States or any foreign country or other foreign jurisdiction, with such domestic limited liability company or other business entity as the agreement shall provide being the surviving or resulting domestic limited liability company or other business entity.</p> <p>§ 1002(c) – The agreement of merger or consolidation shall be submitted to the members of each domestic limited liability company who are entitled to vote with respect to a merger or consolidation at a meeting called on twenty days' notice or such greater notice as the operating agreement may provide. Subject to any requirement in the operating agreement requiring approval by any greater or lesser percentage in interest of the members who are entitled to vote with respect to a merger or consolidation, which shall not be less than a majority in interest of those members who are so entitled to vote, the agreement shall be approved on behalf of each domestic limited liability company (i) by such voting interests of the members as shall be required by the operating agreement, or (ii) if no provision is made, by the members representing at least a majority in interest of the members.</p>	
Conversion	<p>§ 1006(a) – An organization other than a limited liability company or a foreign limited liability company may convert to a limited liability company, and a limited liability company may convert to an organization other than a foreign limited liability company pursuant to this section, Sections 1007 through 1009, and a plan of conversion, if:</p> <p>(1) the other organization's governing statute authorizes the conversion;</p> <p>(2) the conversion is not prohibited by the law of the jurisdiction that enacted the other organization's governing statute; and</p> <p>(3) the other organization complies with its governing statute in effecting the conversion.</p> <p>§ 1007(a) – Subject to Section 1014 [Restrictions on approval of Mergers, Conversion, and Domestications and, pursuant to Section 110, the operating agreement], a plan of conversion must be consented to by all the members of a converting limited liability company.</p>	<p>§ 1006 –</p> <p>(b) A partnership or limited partnership may be converted to a limited liability company pursuant to this section.</p> <p>(c) Subject to any requirements in the partnership agreement requiring approval by any lesser percentage in interest of partners, an agreement of conversion setting forth the terms and conditions of a conversion of a partnership to a limited liability company must be approved by all of the partners of the partnership. Subject to any requirement in the partnership agreement requiring approval by any greater or lesser percentage in interest of limited partners, which shall not be less than a majority in interest, the terms and conditions of a conversion of a limited partnership to a limited liability company must be approved (i) by such a vote of general partners as shall be required by the partnership agreement, or, if no provision is made, by all general partners, and (ii) by limited partners representing at least a majority in interest of each class of limited partners. The agreement of conversion shall be submitted to the general partners and limited partners of</p>	<p>RULLCA requires the consent of all members for a conversion, whereas NYLLCL requires only a majority in interest. NYLLCL permits the operating agreement to vary this requirement.</p> <p>Unlike NYLLCL, RULLCA allows for the conversion of a corporation to a LLC, and for the domestication of foreign LLCs.</p> <p>RULLCA also explicitly allows for the conversion of an LLC to another business entity, whereas NYLLCL does not.</p>



Feature	RULLCA	NYLLCL	Comments
		<p>a limited partnership at a regular or special meeting called on twenty days notice or such other notice as the partnership agreement may provide. A dissenting limited partner shall have the rights provided in article eight-A of the partnership law and shall not be a member of the converted limited liability company....</p>	
<p>Direct &amp; Derivative Actions</p>	<p>Direct Actions</p> <p>§ 901 –</p> <p>(a) Subject to subsection (b), a member may maintain a direct action against another member, a manager, or the limited liability company to enforce the member’s rights and otherwise protect the member’s interests, including rights and interests under the operating agreement or this [act] or arising independently of the membership relationship.</p> <p>(b) A member maintaining a direct action under this section must plead and prove an actual or threatened injury that is not solely the result of an injury suffered or threatened to be suffered by the limited liability company.</p> <p>Derivative Actions</p> <p>§ 902 – A member may maintain a derivative action to enforce a right of a limited liability company if:</p> <p>(1) the member first makes a demand on the other members in a member-managed limited liability company, or the managers of a manager-managed limited liability company, requesting that they cause the company to bring an action to enforce the right, and the managers or other members do not bring the action within a reasonable time; or</p> <p>(2) a demand under paragraph (1) would be futile.</p>	<p>Silent</p>	<p>Neither direct nor derivative suits are mentioned in NYLLCL. However, the Court of Appeals of New York held in <i>Tzolis v Wolff</i> that members of an LLC may bring derivative suits on the company’s behalf, even though there are no provisions governing such suits in NYLLCL.</p> <p>RULLCA explicitly allows a member to bring both direct and derivative actions and establishes procedures for members to follow in pursuing such actions.</p>
<p>Charging Order</p>	<p>§ 503 –</p> <p>(a) On application by a judgment creditor of a member or transferee, a court may enter a charging order against the transferable interest of the judgment debtor for the unsatisfied amount of the judgment. A charging order constitutes a lien on a judgment debtor’s transferable interest and requires the limited liability company to pay over to the person to which the charging order was issued any distribution that would otherwise be paid to the judgment debtor.</p> <p>(b) To the extent necessary to effectuate the collection of distributions pursuant to a charging order in effect under subsection (a), the court may:</p>	<p>§ 607 –</p> <p>(a) On application to a court of competent jurisdiction by any judgment creditor of a member, the court may charge the membership interest of the member with payment of the unsatisfied amount of the judgment with interest. To the extent so charged, the judgment creditor has only the rights of an assignee of the membership interest. This chapter does not deprive any member of the benefit of any exemption laws applicable to his or her membership interest.</p> <p>(b) No creditor of a member shall have any right to obtain possession of, or</p>	<p>Both RULLCA and NYLLCL allow a court to issue a charging order, which constitutes a lien on the transferable interest of the judgment debtor.</p> <p>Whereas NYLLCL is silent as to foreclosure on a membership interest, RULLCA grants the court the power to order a sale of the transferable interest (i.e., right to distributions).</p>

Feature	RULLCA	NYLLCL	Comments
	<p>(1) appoint a receiver of the distributions subject to the charging order, with the power to make all inquiries the judgment debtor might have made; and</p> <p>(2) make all other orders necessary to give effect to the charging order.</p> <p>(c) Upon a showing that distributions under a charging order will not pay the judgment debt within a reasonable time, the court may foreclose the lien and order the sale of the transferable interest. The purchaser at the foreclosure sale only obtains the transferable interest, does not thereby become a member, and is subject to Section 502.</p> <p>(d) At any time before foreclosure under subsection (c), the member or transferee whose transferable interest is subject to a charging order under subsection (a) may extinguish the charging order by satisfying the judgment and filing a certified copy of the satisfaction with the court that issued the charging order.</p> <p>(e) At any time before disclosure under subsection (c), a limited liability company or one or more members whose transferable interests are not subject to the charging order may pay to the judgment creditor the full amount due under the judgment and thereby succeed to the rights of the judgment creditor, including the charging order.</p> <p>(f) This [act] does not deprive any member or transferee of the benefit of any exemption laws applicable to the member's or transferee's transferable interest.</p> <p>(g) This section provides the exclusive remedy by which a person seeking to enforce a judgment against a member or transferee may, in the capacity of judgment creditor, satisfy the judgment from the judgment debtor's transferable interest.</p>	<p>otherwise exercise legal or equitable remedies with respect to, the property of the limited liability company.</p>	
Transition Provisions	<p>§ 1104(a) Before [all-inclusive date], this [act] governs only:</p> <p>(1) a limited liability company formed on or after [the effective date of this act]; and</p> <p>(2) except as otherwise provided in subsection (c), a limited liability company formed before [the effective date of this act] which elects, in the manner provided in its operating agreement or by law for amending the operating agreement, to be subject to this [act].</p> <p>(b) Except as otherwise provided in subsection (c), on and after [all-inclusive date] this [act] governs all limited liability companies.</p> <p>(c) For the purposes applying this [act] to a limited liability company formed before [the effective date of this act]:</p> <p>(1) the company's articles of organization are deemed to be the company's certificate</p>	<p>Silent</p>	<p>LLCs formed under a predecessor to RULLCA would continue to be governed by the predecessor, until a specific transition date. After the transition date, all companies would be governed by RULLCA.</p> <p>LLCs formed under a predecessor may elect to be governed by RULLCA prior to the transition date.</p>

Feature	RULLCA	NYLLCL	Comments
	of organization; and (2) for the purposes of applying Section 102(10) and subject to Section 112(d), language in the company's articles of organization designating the company's management structure operates as if that language were in the operating agreement.		



NEW YORK  
CITY BAR

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**COMMITTEE ON CORPORATION LAW**

**REPORT RECOMMENDING ADOPTION BY NEW YORK STATE OF  
THE REVISED UNIFORM LIMITED LIABILITY COMPANY ACT**

The Corporation Law Committee of the Association of the Bar of the City of New York (the “**Committee**”) has reviewed the Revised Uniform Limited Liability Company Act (“**RULLCA**”), which was approved by the National Conference of Commissioners on Uniform State Laws (the “**NCCUSL**”) in July 2006 after a three-year drafting and deliberation process.<sup>1</sup> The Committee has also considered the changes that RULLCA would make to New York’s Limited Liability Company Law (“**NYLLCL**”).

As a result of this review process, the Committee recommends that New York enact RULLCA, in the form attached as Annex A.<sup>2</sup> The form of RULLCA that we are proposing is almost entirely the version approved by the NCCUSL; the limited changes that we have made are discussed in this Report below:

**Background**

RULLCA updates the original Uniform Limited Liability Company Act (“**ULLCA**”) in many respects. New York’s legislature chose not to enact ULLCA and instead enacted NYLLCL in 1994. New York’s statute may have been preferable to ULLCA at the time of its adoption, and NYLLCL has been supplemented by amendments since then. However, lawyers practicing in New York recognize that the NYLLCL has shortcomings, and, accordingly, many New York practitioners elect to form limited liability companies in Delaware, which has a more comprehensive and flexible statute, instead of New York.

RULLCA is the product of exhaustive studies by knowledgeable experts and has been designed to improve upon earlier generations of limited liability company statutes, such as the NYLLCL. The Committee considers RULLCA to be a significant advancement in the development of the law of limited liability companies, and believes that RULLCA would address many of the shortcomings found in the NYLLCL. Moreover, if New York adopts RULLCA, the Committee expects that members and managers of limited liability companies governed by RULLCA would benefit from the body of case law that develops not only in New York but also

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<sup>1</sup> Daniel S. Kleinberger and Carter G. Bishop, *The Next Generation: The Revised Uniform Limited Liability Company Act*, 62 Bus. Law. 515 at 518 (2006). The American Bar Association approved RULLCA in August 2007, many states are actively considering the enactment of RULLCA and two states (Utah and Idaho) have already adopted RULLCA.

<sup>2</sup> For convenience, we have included the NCCUSL’s comments in Annex A.

in the other states that have enacted RULLCA as courts interpret the statute. The development of this case law should enhance the participants' understanding of their relationship, rights and obligations, and thus make organizing a limited liability company in New York and other RULLCA states more attractive.

This Report identifies and discusses what the Committee believes are the most significant changes that enactment of RULLCA would make to New York law, in support of our recommendation that New York's legislature enact RULLCA, subject to certain limited changes as described in this Report. This Report also includes, in Exhibit A, a chart providing a section-by-section comparison of the key provisions of the version of RULLCA approved by the NCCUSL and the NYLLCL.

### **Discussion of RULLCA's Fundamental Changes**

Formation of a Limited Liability Company. Section 201 of RULLCA provides that a certificate of organization for a limited liability company may be filed with the Secretary of State, even if the limited liability company has no member at the time of filing. In the version of RULLCA approved by the NCCUSL, this section also requires, in Section 201(b)(3), that the certificate of organization must state if the limited liability company has no members at the time of filing, and if this is the case, Section 201(e) causes the certificate of formation to lapse and become void unless a notice stating that the limited liability company has at least one member (and identifying the date on which the initial member was admitted as a member) is filed with the Secretary of State within 90 days after the filing of the certificate of formation. The limited liability company is then deemed "formed" as of the date of initial membership stated in this notice.

By comparison, the NYLLCL recognizes that a limited liability company is formed when the initial articles of organization are filed with New York's Department of State (or up to 60 days later if so specified in the articles of organization). In one respect, RULLCA is an advancement relative to the NYLLCL, because RULLCA permits the filing of the certificate of organization of a limited liability company without members whereas Section 203(c) of the NYLLCL requires that a limited liability company must have at least one member at the time its articles are filed.

Allowing the flexibility to file the certificate of organization of a limited liability company without members (a so-called "shelf LLC") was controversial and intensely debated during the RULLCA drafting process, and the subsequent filing required by Section 201(e) of the version of RULLCA approved by the NCCUSL represents a compromise between participants in the drafting process who recognized the practical need for flexibility to form entities on short notice, versus those who insisted that a limited liability company can "exist" only as a partnership of its members and thus cannot "exist" without members.<sup>3</sup>

The Committee supports Section 201(a) of RULLCA in that it grants flexibility to initiate the process for forming a limited liability company without members, but it is opposed to the additional notice requirement established by Section 201(e) of the version of RULLCA approved by the NCCUSL. The Committee recognizes that "shelf" provisions allow for the efficient

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<sup>3</sup> See Kleinberger and Bishop, *supra* note 1, at 528; Comment to RULLCA §2.01.

creation of limited liability companies for legitimate purposes. In particular, participants in sophisticated legal transactions desire at times to form entities prior to a final determination of the particular entity's owners.

New York law currently permits the formation of a corporation upon the filing of the certificate of incorporation with the Department of State, without any requirement that the entity actually have shareholders at the time of such filing<sup>4</sup> and the Committee sees no compelling reason to treat limited liability companies in a different manner. Moreover, the Committee believes that the 90-day filing period required by Section 201(e) of the version of RULLCA approved by the NCCUSL could create a "trap for the unwary" without achieving any practical benefit, and could complicate opinion practice if the certificate of organization of a limited liability company without members upon filing lapses due to a failure to file a notice of a member within the requisite time period.

Accordingly, the Committee believes that the inclusion of Sections 201(b)(3) and 201(e) of the version of RULLCA approved by the NCCUSL would represent a step backward and not forward, and thus recommends their omission from the statute. In connection with this recommendation to delete Section 201(e), the Committee recommends the addition to RULLCA of provisions requiring that (i) until a limited liability company has at least one member, it would lack capacity to carry on any activity except delivering certain certificates and statements to the Secretary of State for filing, admitting a member and dissolving and (ii) a limited liability company that has at least one member may ratify acts or activities occurring prior to the time when the limited liability company had at least one member. These recommended additions are consistent with provisions in an earlier draft considered by the NCCUSL and have been incorporated into the attached version of RULLCA as Sections 201(d)(4) and (5).

Purpose of a Limited Liability Committee / Not-for-Profit Enterprises. Section 104(b) of RULLCA provides that a limited liability company may have any lawful purpose, for profit or not. In comparison, Section 201 of the NYLLCL provides that a limited liability company may be formed for any "lawful business purpose." The Committee supports the RULLCA formulation in clarifying that a New York limited liability company may be properly formed regardless of whether it will be a for-profit or not-for-profit enterprise.

Oral Operating Agreements. Section 102(13) of RULLCA broadly defines an "operating agreement" to encompass not only oral agreements, but, as reflected in the NCCUSL's comments to RULLCA (the "**Comments**"), also "any activity involving unanimous consent of the members" and "a number of separate documents (or records), however denominated."<sup>5</sup> Thus, although RULLCA requires that a limited liability company must have an operating agreement, the agreement may be implied. Under RULLCA, the only mechanical requirement for qualification as an operating agreement is the assent of all members.<sup>6</sup>

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<sup>4</sup> N.Y. Bus. Corp. Law §403.

<sup>5</sup> Comment to Paragraph 13 of RULLCA §102.

<sup>6</sup> *Id.*

In eschewing a requirement that the operating agreement must be in writing, RULLCA mirrors the limited liability company statutes in most states and is consistent with the view that a limited liability company is more like a partnership (which does not generally require a written agreement) than a corporation. In contrast, Section 417 of the NYLLCL requires that a limited liability company formed in New York must have a written operating agreement that must be entered into before, at the time of or within 90 days after the filing of the articles of organization. The NYLLCL does not, however, specify any penalties for the limited liability company, its members or managers if they fail to enter into a written operating agreement, and the courts have recognized the existence of such limited liability companies.<sup>7</sup>

A principal advantage of permitting operating agreements to be oral is that single member limited liability companies will be relieved of the obligation to prepare an operating agreement, as currently required by the NYLLCL. As soon as a limited liability company has a member, it is deemed to have an operating agreement.<sup>8</sup>

The Committee recognizes that the breadth of RULLCA's definition of an "operating agreement" has the potential to create uncertainty and increase the likelihood of disputes among members *inter se* and with third parties as to the terms of an operating agreement. For example, Section 111(b) of RULLCA provides that "[a] person that becomes a member of a limited liability company is deemed to assent to the operating agreement." Because oral and implied-in-fact terms, as well as unanimous member consent to a particular act, can be part of the operating agreement, a person joining a limited liability company may not be easily able, if at all, to determine all that he or she is agreeing to. RULLCA leaves the resolution of such matters to general principles of contract interpretation.

Although RULLCA does not require a record reflecting the existence of the operating agreement, the Committee expects that a limited liability company of any complexity would maintain such a record. In light of the Comment to Section 102 of RULLCA that "[o]ral and implied agreements invite memory problems and 'swearing matches'" and the foundational importance of the operating agreement, the Committee anticipates that "best practices" would suggest that the operating agreement should be in writing and address all material terms especially for larger limited liability companies. A written agreement which sets forth the rights, obligations, and liabilities of the members and managers will provide much greater security and stability.

The NYLLCL requirement that members of a limited liability company must adopt a written operating agreement does not eliminate disputes among members when a failure to adopt a written operating agreement occurs, because, as noted above, the courts have recognized the existence of limited liability companies without written operating agreements. Moreover, the flexibility afforded by RULLCA for limited liability companies with one or a few members should encourage the formation of limited liability companies under New York law if RULLCA is enacted in this State.

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<sup>7</sup> See e.g., *Villi v. O'Caing-Villi*, 809 N.Y.S. 2d 484 (N.Y. Sup. Ct. 2005); *Matter of Spires v. Casterline*, 778 N.Y.S. 2d 259 (N.Y. Sup. Ct. 2004); *Merrell-Benco Agency LLC v. HSBC Bank USA*, 799 N.Y.S.2d 590, (N.Y. 3d Dep't 2005), *lv. dismissed, lv. denied* 6 N.Y.3d 742 (2005).

<sup>8</sup> Comment to Paragraph 13 of RULLCA §102.

Standards of Conduct for Members and Managers – Fiduciary Duties. Section 409 of RULLCA establishes standards of conduct for members and managers. It provides that each member (in the case of a member-managed limited liability company) and manager (in the case of a manager-managed LLC) owes to the company and the other members the fiduciary duties of loyalty and care.

The duty of loyalty under Section 409 includes the following duties:

- (1) to account to the company and to hold as trustee for it any property, profit, or benefit derived by the member [or manager]:
  - A. in the conduct or winding up of the company’s activities;
  - B. from a use by the member [or manager] of the company’s property; or
  - C. from the appropriation of a limited liability company opportunity;
- (2) to refrain from dealing with the company in the conduct or winding up of the company’s activities as or on behalf of a person having an interest adverse to the company; and
- (3) to refrain from competing with the company in the conduct of the company’s activities before the dissolution of the company.

The concept of a duty of loyalty that *includes* a set of enumerated duties is in contrast to the approach in ULLCA, RULLCA’s predecessor, which provided an exclusive list of those duties. As indicated in the Comments, the approach in RULLCA is to codify the existence of fiduciary duties but not to limit the duties to those specified.

RULLCA differs from the NYLLCL in that RULLCA expressly articulates a duty of loyalty and identifies certain specified areas of conduct that fall within the duty, but does not limit the duty of loyalty to those specified. The duty of loyalty is not specified in the NYLLCL beyond the requirement to act in good faith, but it is guided by common law, which provides for duties similar to those described in RULLCA.

Except for limited and appropriate exceptions, the default standards of conduct specified in Section 409 of RULLCA may be modified and, in many respects, eliminated by the operating agreement, as indicated in the discussion below under the heading “The Power of the Operating Agreement.” In addition, the liability of members and managers for monetary damages may be limited under the operating agreement, with relatively limited and appropriate exceptions. The NYLLCL also provides broad authorization to eliminate damages for breach of duty, with limited exceptions, but does not expressly provide for contractual elimination or modification of the standard of care articulated in the statute.

Sections 409(c) and 409(g) of RULLCA provide that *subject to the business judgment rule*, the duty of care of a member (in the case of a member-managed limited liability company) or manager (in the case of a manager-managed limited liability company) “is to act with the care that a person in a like position would reasonably exercise under similar circumstances in a manner the member [or manager] reasonably believes to be in the best interests of the company.”



This formulation of the duty of care is similar to the formulation found in Section 409 of the NYLLCL, although the NYLLCL does not expressly state that the duty of care is subject to the business judgment rule.

The Power of the Operating Agreement. Section 110 of RULLCA delineates the scope and limits of the operating agreement, including the extent to which the operating agreement can define, alter or eliminate aspects of fiduciary duty.<sup>9</sup> In particular, subsections 110(d)(1)(A)-(C) of RULLCA provide that, if not “manifestly unreasonable,” the operating agreement may restrict or eliminate each of the specific applications of the duty of loyalty identified in Section 409(b) of RULLCA (*i.e.*, the duty to account for the use of the company’s property, the duty to refrain from dealing with the limited liability company on behalf of a party with an adverse interest and the duty to refrain from competing with the limited liability company before dissolution). Additionally, Section 110(d)(2) of RULLCA permits the operating agreement, if not “manifestly unreasonable,” to identify specific types or categories of activities that do not violate the duty of loyalty. Moreover, subsections (3) through (5) of Section 110(d) of RULLCA provide that the operating agreement may, if not “manifestly unreasonable,” (i) alter the duty of care (except to authorize intentional misconduct or knowing violation of law), (ii) alter any other fiduciary duty and (iii) prescribe standards by which to measure the performance of the contractual obligation of good faith and fair dealing.

In comparison, Section 409 of the NYLLCL provides for a good faith and ordinarily prudent person standard of care as the statutory minimum that may not be waived. However, under Section 417(a) of the NYLLCL, managers and members who exercise management powers and responsibilities may be exculpated for breaches of fiduciary duties other than as a result of bad faith, intentional misconduct, knowing violation of law, unjust enrichment and, in the case of distributions under Section 508 of the NYLLCL (*i.e.*, distributions that result in the liabilities of the limited liability company to third parties exceeding its assets), conduct inconsistent with the negligence standards of Section 409 of the NYLLCL.

Section 110(h) of RULLCA provides guidance for courts asked to determine if a term of an operating agreement is “manifestly unreasonable” and empowers the courts to invalidate such term, if “in light of the purposes and activities of the limited liability company, it is readily apparent that: (A) the objective of the term is unreasonable; or (B) the term is an unreasonable means to achieve the provision’s objective.”

The Committee notes an anomaly in RULLCA in that, in the case of the duty of loyalty, subject to the “manifestly unreasonable” standard, RULLCA permits the operating agreement to “restrict or eliminate” various components from the duty of loyalty and to “identify specific types or categories of activities that do not violate” that duty; however, RULLCA’s Section 110(d)(3) and (4) provide that it is only possible to “alter” the duty of care or “any other fiduciary duty.” Neither RULLCA nor the Comments explain (i) why certain duties may only be altered but not eliminated, (ii) the extent to which a duty may be “altered” before it is, in fact, “eliminated” or (iii) what “other fiduciary duties” are contemplated beyond the duty of loyalty and the duty of care. The Committee would prefer clearer treatment of these issues in the statute and recognizes that the guidance provided to the courts by Section 110(h) of RULLCA as to the meaning of “manifestly unreasonably” is imprecise. However, the Committee believes that any

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<sup>9</sup> See Kleinberger and Bishop, *supra* note 1, at 521.

ambiguities in RULLCA regarding the power of the operating agreement to modify duties are likely to be clarified by a well-drafted operating agreement and, if necessary, by looking to the courts to interpret this language; this seems, on balance, preferable to permitting total elimination of the various fiduciary duties involved regardless of how unreasonable such elimination may be.

The Committee further notes that the meaning of Section 110(d)(5) of RULLCA, which permits an operating agreement to “prescribe the standards by which to measure the performance of the contractual obligation of good faith and fair dealing,” is unclear. The contractual obligation of good faith and fair dealing is an implied covenant under New York common law. The contractual obligation of good faith and fair dealing does not constitute a separate duty or create obligations that are inconsistent with the express terms of the contractual relationship;<sup>10</sup> it simply permits a court to interpret a contract in light of the parties’ reasonable expectations.<sup>11</sup> Section 110(d)(5) of RULLCA, on the other hand, could lead a court to create a separate and more expansive duty of good faith and fair dealing. Therefore, if RULLCA is adopted in New York, the legislative history should make it clear that this provision of RULLCA incorporates and does not expand upon the current New York view of this duty. In any event, Section 110(d)(5) of RULLCA would permit the operating agreement to define the obligations of the managers and members in a manner consistent with the current narrow judicial reading of the contractual obligation of good faith and fair dealing.

Section 110(f) of RULLCA accepts that all members of a member-managed limited liability company need not share the same duties and responsibilities by providing that an operating agreement may (i) expressly relieve a member of a responsibility that the member would otherwise have under the statute and impose such responsibility on one or more other members; and (ii) eliminate or limit any fiduciary duty that would have pertained to the responsibility for the relieved member. The comparable provisions under New York law, Sections 401, 417 and 418 of the NYLLCL, provide for substantively similar rights to modify operating agreements as permitted by Section 110(f) of RULLCA.

Section 110(g) of RULLCA expressly authorizes the operating agreement to relieve members and managers from liability for money damages (except for a breach of the duty of loyalty, the receipt of financial benefits to which the member or manager is not entitled, receipt of improper distributions, the intentional infliction of harm on the limited liability company or a member, or an intentional violation of criminal law).<sup>12</sup> Section 417(a) of the NYLLCL contains a similar provision allowing the operating agreement to eliminate liability for damages subject to certain limits.

Management and Agency Power. Section 412(a) of the NYLLCL provides that “[u]nless the articles of organization of a limited liability company provide that management of the limited liability company shall be vested in a manager or managers, every member is an agent of the limited liability company for the purpose of its business.” In this case, the act of every member

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<sup>10</sup> See, e.g., *Murphy v American Home Prods. Corp.*, 58 N.Y.2d 293, 304 (1983).

<sup>11</sup> See, e.g., *Dalton v Education Testing Services* 87 N.Y.2d 384, 389, 639 N.Y.S.2d 977 (1995); *Rowe v Great Atl. & Pac. Tea Co.* 46 N.Y.2d 62, 69 (1975).

<sup>12</sup> Kleinberger & Bishop, *supra* note 1, at 522.

would bind the limited liability company “unless (i) the member so acting has in fact no authority to act for the limited liability company in the particular matter and (ii) the person with whom the member is dealing has knowledge of the fact that the member has no such authority.” Section 412(b) of the NYLLCL further provides that if the articles of organization vest management of a limited liability company in one or more managers, no member, solely by reason of being a member, is an agent of the limited liability company.

In contrast, RULLCA provides, in Section 301(a), that a member is not an agent of the limited liability company solely by reason of being a member. RULLCA recognizes that limited liability companies may have a flexible management structure, which structure is not apparent to third parties.<sup>13</sup> A limited liability company is thus unlike a limited or general partnership, where a third party can know by the formal name of the entity and by a person’s status as a limited or general partner whether the person has the power to bind the entity. Accordingly, RULLCA reflects the view, with which the Committee agrees, that the principle of “statutory apparent authority” should not apply to limited liability companies. Section 301(b) of RULLCA contemplates that the operating agreement and otherwise applicable agency law will define agency relationships. Thus, while the mere fact that a person is a member of a member-managed limited liability company cannot, by itself, establish apparent authority, a course of dealing may change the analysis.

The Committee recognizes that Section 301 of RULLCA may increase the unpredictability inherent in dealing with limited liability companies insofar as third parties will be unable (absent access to the operating agreement) to determine any applicable limits on a member’s authority in respect of a particular situation. However, the Committee believes that agency law principles are well-suited to addressing the challenges resulting from “decodification” of apparent authority by position – especially in light of the Third Restatement of Agency issued in 2006, which deals extensively with the ability of an enterprise’s participants to bind the enterprise.<sup>14</sup>

Moreover, the Committee believes that, as a practical matter, in the absence of statutory apparent authority, limited liability companies may find it expedient to make public, or furnish to parties with whom they have commercial dealings, their management structure in order to facilitate transactions with third parties. In this regard, Section 302(a)(2) of RULLCA provides for the public filing of a “statement of authority” that will provide confirmation of the authority of a person holding a particular position with a limited liability company to “(A) execute an instrument transferring real property held in the name of the company; or (B) enter into other transactions on behalf of, or otherwise act for or bind, the company.” With respect to transfers of real property, a statement of authority can constitute constructive notice if properly filed in the recording office of each property owned. In other matters, Section 302(e) of RULLCA provides that a statement of authority is conclusive in favor of a third party (non-member) who gives value in reliance of the grant of authority, unless, among other things, the third party had knowledge to the contrary.

Transfers. Membership in a limited liability company typically carries with it both economic rights (especially the right to distributions) and non-economic rights (such as the right

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<sup>13</sup> See Comment to RULLCA Section 301(a).

<sup>14</sup> See Comment to RULLCA §301(b).

to vote and, in certain cases, participate in management or receive information). Under NYLLCL and most other state limited liability company statutes, the transfer of an interest in a limited liability company merely transfers the member's right to receive distributions (the economic interest) and does not afford the assignee the automatic right to become a member or to participate in other non-economic rights.

Similarly, under Section 112(b) of RULLCA, the only interest that may be transferred, absent anything to the contrary in the operating agreement, is the "transferable interest" (*i.e.*, any right to distributions that a member has under the operating agreement). Unless otherwise provided by the operating agreement, a transferee is, in effect, the assignee of only the transferor's economic rights.

RULLCA's treatment of transferees (*e.g.*, subjecting the transferee to changes in the operating agreement that occur after the transfer) stems from the overarching "pick your partner" principle and is consistent with the current provisions of Article VI of the NYLLCL. The Comments to RULLCA Section 112 note that "the law of unincorporated business organizations is only beginning to grapple in a modern way with the tension between the rights of an organization's owners to carry on their activities as they see fit (or have agreed) and the rights of transferees of the organization's economic interests." These Comments also state that "whether, in extreme and sufficiently harsh circumstances, transferees might be able to claim some type of duty or obligation to protect against expropriation, is a question for other law." The Committee believes that RULLCA strikes an appropriate balance between protecting against transferee vulnerability to expropriation, on the one hand, and, on the other, not affording transferees the power to "freeze the deal" and interfere in limited liability company governance via threat of litigation.

Charging Orders. Both Section 607 of the NYLLCL and Section 503 of RULLCA provide for a charging order against a judgment debtor's transferable interest in a limited liability company. Section 503(a) of RULLCA provides that once properly served on the limited liability company, a charging order "requires the limited liability company to pay over to the person to which the charging order was issued any distribution that would otherwise be paid to the judgment debtor." Under both the NYLLCL and RULLCA, a charging order is a lien on the transferable interest and is not a transfer or assignment of the charged interest.

The Committee believes that Section 503(b) of RULLCA represents an advancement over Section 607 of the NYLLCL insofar as the provision in RULLCA grants a court the power to deal with efforts to evade the lien by appointing a receiver of the distributions subject to the charging order, who has the power to make all inquiries the judgment debtor might have made. Section 503(b) also empowers the court to make all other orders necessary to give effect to the charging order; however, the court's power is limited to evasive conduct and does not extend to interfering in the legitimate activities of the limited liability company. A receiver appointed under Section 503(b) of RULLCA is not a receiver for the limited liability company; the receiver's powers are limited solely to seeking information to which the judgment debtor is entitled. RULLCA requires a finding by a court that payment of the judgment debt will not be made within a reasonable time before ordering foreclosure.

Events Causing Dissolution. Section 701 of RULLCA provides for dissolution of a limited liability company upon the occurrence of certain events. The section is generally

comparable to Section 701 of the NYLLCL with two differences: the NYLLCL permits an application for dissolution by a majority in interest of the members (or such greater or lesser percentage as is specified in the operating agreement) while RULLCA requires unanimity of members unless otherwise provided in the operating agreement. While the Committee would prefer a majority in interest default rule so as to prevent members with majority ownership rights being oppressed by the minority, it recognizes the benefit of a uniform statute and believes that practitioners will typically vary the unanimity default rule as appropriate in the operating agreement. Also, RULLCA permits a member to seek dissolution in the event of unlawful activities by the limited liability company or fraudulent or oppressive conduct by the controlling managers or members. There is no comparable provision in the NYLLCL.

Claims Against Dissolved Limited Liability Company. Section 703 of RULLCA contains a procedure for dealing with known claims. While this procedure is comparable to that provided under New York law for corporations, it has no counterpart in the NYLLCL.

Section 704 of RULLCA provides a limited liability company with the option of publishing notice of its dissolution and requesting persons having claims against the limited liability company to present them. This provision mimics similar provisions of the Business Corporation Law of the State of New York (the “BCL”) and the Delaware General Corporation Law but the period within which RULLCA provides that claims may be filed is five years from the date notice of dissolution is published as compared with six months under the BCL. Section 704 of RULLCA also provides that a recipient of assets distributed by a dissolved limited liability company is responsible for its “proportionate share” of any unbarred claim against the limited liability company up to the total amount of assets it received in respect of the dissolution of the limited liability company. The statute is not clear how such proportionate share is to be calculated.

Distribution of Assets in Winding Up Limited Liability Company’s Activities. Section 708 of RULLCA includes a default rule providing that the surplus of the limited liability company’s assets after discharging all obligations to creditors (including members that are creditors) is to be distributed in the following order (subject to any charging order under Section 503 of RULLCA): (i) to return capital contributions attributable to transferable interests and not previously returned and (ii) in equal shares to the members and dissociated members, subject to any transfers made pursuant to Section 502 of RULLCA. If the limited liability company has insufficient surplus to return each owner’s capital contributions, the surplus must be distributed among the owners in proportion to the value of their respective unreturned contributions. Under the NYLLCL, such sharing would be in proportion to how the members would otherwise share in distributions. While the Committee members are divided on whether the provisions of the NYLLCL are preferable to the RULLCA approach, they recognize the benefits of a uniform statute and note that this provision can be modified by the operating agreement; accordingly, they do not object to it as a default rule.

Foreign Limited Liability Companies. Article 8 of RULLCA is analogous to Article VIII of the NYLLCL. However, there are certain differences that are worth noting.

Section 803(a) of RULLCA provides for numerous activities that may be conducted by a foreign limited liability company that will not constitute transacting business in the state. The list is similar to, but more extensive than, Section 803 of the NYLLCL and is consistent with

current corporation law statutes. The Committee notes that transacting business in interstate commerce is included in the list and therefore does not constitute doing business within the state, however Section 803(b) provides that owning certain income-producing real property or tangible personal property in the state constitutes transacting business in the state even if the entity has no office in the state.

Section 809 of RULLCA provides that the Attorney General may maintain an action to enjoin a foreign limited liability company from transacting business within the state if the limited liability company has failed to obtain a certificate of authority or is otherwise in violation of Article 8 of RULLCA. This structure may not be possible under New York state law governing the actions that the Attorney General may take.

Actions by Members. There are no comparable provisions in the NYLLCL to Article 9 of RULLCA, which deals with legal actions brought by a member against the limited liability company, its manager or other members as well as derivative actions.

The New York Court of Appeals recently held in *Tzolis v Wolff*<sup>15</sup> that members of a limited liability company may bring derivative suits on the limited liability company's behalf, although there are no provisions governing such suits in the NYLLCL. The Committee supports the enactment of Article 9 of RULLCA in that it would clearly establish the procedures that members must follow to pursue derivative actions on behalf of a limited liability company.

Section 903 of RULLCA provides that a derivative action to enforce a right of a limited liability company may be maintained only by a person that is a member of the limited liability company at the time the action is commenced and remains a member while the action continues, a requirement that is not contained in the Section 626 of the BCL, which provides for derivative actions to enforce rights of corporations. This provision of RULLCA could prevent estates from bringing derivative actions on behalf of deceased persons.

Pursuant to Section 905 of RULLCA, Special Litigation Committees ("SLCs") may be formed to investigate claims asserted by parties in a derivative proceeding in which a limited liability company is named. RULLCA grants the SLCs various powers, including the power to recommend that the court dismiss the action. The court is bound by the recommendation only if it finds that the SLC was composed of disinterested independent individuals who made the recommendation in good faith and acted with reasonable care.

RULLCA requires a member who brings a direct action to "plead and prove an actual or threatened injury that is not solely the result of an injury suffered or threatened to be suffered by the limited liability company."

Merger, Conversion and Domestication. Article 10 of RULLCA is comparable to Article X of the NYLLCL although the provisions of RULLCA are more comprehensive in that they permit conversion of a corporation to a limited liability company and domestication of foreign limited liability companies, both of which transactions are not provided for currently in the NYLLCL. However, Article 10 of RULLCA imposes a default rule requiring unanimous consent of the members for mergers, conversions and domestications, whereas NYLLCL

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<sup>15</sup> 2008 NY slip op. 01260 (N.Y. 2008).

requires only a majority in interest of the members unless the operating agreement requires a greater or lesser percentage. RULLCA generally allows the members to modify its default rules, other than the limited matters described in Section 110(c). The Committee concluded that it was important to ensure that a merger, conversion and domestication of a limited liability company would be permitted with less than unanimous consent if so provided in the operating agreement. Accordingly, the Committee has proposed adding to Section 110(a) of RULLCA a new subsection (5) to make clear that the operating agreement governs the requirements for approval of a merger, conversion or domestication. The Committee has also proposed a technical amendment to Section 1015 of RULLCA, to ensure that RULLCA does not preclude an entity from being merged, converted or domesticated in compliance with the applicable law of another state or another applicable domestic law.

No Publication Requirement. RULLCA, like its predecessor, contains no publication requirement. Under Section 206 of the NYLLCL, a New York limited liability company is required to publish, within 120 days after the effectiveness of its initial articles of organization, a notice containing a copy of the articles of organization or the substance thereof once each week for six successive weeks in two newspapers of the county in which the office of the limited liability company is located, including one newspaper designated by the county clerk. Proof of publication must be filed with the Department of State of the State of New York. If a limited liability company fails to file a Certificate of Publication within 120 days after its formation, its authority to carry on, conduct or transact any business in New York is suspended. The suspension will be annulled upon subsequent filing of a Certificate of Publication. The NYLLCL contains similar provisions applicable to foreign limited liability companies doing business in New York.

The publication requirements in the NYLLCL have been the subject of almost universal criticism. They are generally viewed as having no legitimate purpose. The cost of publication can be significant and, in certain instances, prohibitive to small businesses. It is estimated that these costs range from \$1,300 to \$2,500 for businesses whose offices are located in New York County. This is a cost that is not imposed by any other state and serves as a deterrent to new businesses that might otherwise organize or do business in New York. The publication requirement works a particular hardship on persons with limited financial means who conduct businesses in low income neighborhoods.

June 2009

THE CORPORATION LAW COMMITTEE<sup>16</sup>  
OF  
THE ASSOCIATION OF THE BAR OF THE CITY OF NEW YORK

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<sup>16</sup> This report was substantially completed under the guidance of the Committee's former Chairperson, Arnold J. Levine, and Secretary, Orrin R. Levine. The following were also members of the Committee at that time: Justin P. Caulfield, Michael Chernick, Susan G. Curtis, Tracey L. Daniels, Aviva F. Diamant, Martha M. Dwyer, Melvin Epstein, James E. Kaye, Asi Kirmayer, David B. Manno, Jeffrey D. Marell, Daniel P. Raglan, Stacey Sabo, Marilyn Sobel and Claudius O. Sokenu.



**REVISED UNIFORM LIMITED LIABILITY COMPANY  
ACT**

as originally drafted by the

**NATIONAL CONFERENCE OF COMMISSIONERS  
ON UNIFORM STATE LAWS**

and as modified and proposed for adoption in

**THE STATE OF NEW YORK**

by

**THE CORPORATION LAW COMMITTEE  
OF THE ASSOCIATION OF THE BAR OF THE CITY OF NEW YORK**

*WITH COMMENTS BY  
THE NATIONAL CONFERENCE OF COMMISSIONERS  
ON UNIFORM STATE LAWS*

# REVISED UNIFORM LIMITED LIABILITY COMPANY ACT

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## REVISED UNIFORM LIMITED LIABILITY COMPANY ACT

- (1) [ARTICLE] 1
- (2) GENERAL PROVISIONS

SECTION 101. SHORT TITLE. This [act] may be cited as the Revised Uniform Limited Liability Company Act.

### Comment

This Act is drafted to replace a state's current LLC statute, whether or not that statute is based on the original Uniform Limited Liability Company Act. Section 1104 contains transition provisions.

SECTION 102. DEFINITIONS. In this [act]:

(1) "Certificate of organization" means the certificate required by Section 201. The term includes the certificate as amended or restated.

(2) "Contribution" means any benefit provided by a person to a limited liability company:

(A) in order to become a member upon formation of the company and in accordance with an agreement between or among the persons that have agreed to become the initial members of the company;

(B) in order to become a member after formation of the company and in accordance with an agreement between the person and the company; or

(C) in the person's capacity as a member and in accordance with the operating agreement or an agreement between the member and the company.

(3) "Debtor in bankruptcy" means a person that is the subject of:

(A) an order for relief under Title 11 of the United States Code or a successor statute of general application; or

(B) a comparable order under federal, state, or foreign law governing insolvency.

(4) "Designated office" means:

(A) the office that a limited liability company is required to designate and maintain under Section 113; or

(B) the principal office of a foreign limited liability company.

(5) "Distribution", except as otherwise provided in Section 405(g), means a transfer of

money or other property from a limited liability company to another person on account of a transferable interest.

(6) “Effective”, with respect to a record required or permitted to be delivered to the Department of State for filing under this [act], means effective under Section 205(c).

(7) “Foreign limited liability company” means an unincorporated entity formed under the law of a jurisdiction other than this state and denominated by that law as a limited liability company.

(8) “Limited liability company”, except in the phrase “foreign limited liability company”, means an entity formed under this [act].

(9) “Manager” means a person that under the operating agreement of a manager-managed limited liability company is responsible, alone or in concert with others, for performing the management functions stated in Section 407(c).

(10) “Manager-managed limited liability company” means a limited liability company that qualifies under Section 407(a).

(11) “Member” means a person that has become a member of a limited liability company under Section 401 and has not dissociated under Section 602.

(12) “Member-managed limited liability company” means a limited liability company that is not a manager-managed limited liability company.

(13) “Operating agreement” means the agreement, whether or not referred to as an operating agreement and whether oral, in a record, implied, or in any combination thereof, of all the members of a limited liability company, including a sole member, concerning the matters described in Section 110(a). The term includes the agreement as amended or restated.

(14) “Organizer” means a person that acts under Section 201 to form a limited liability company.

(15) “Person” means an individual, corporation, business trust, estate, trust, partnership, limited liability company, association, joint venture, public corporation, government or governmental subdivision, agency, or instrumentality, or any other legal or commercial entity.

(16) “Principal office” means the principal executive office of a limited liability company or foreign limited liability company, whether or not the office is located in this state.

(17) “Record” means information that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in perceivable form.

(18) “Sign” means, with the present intent to authenticate or adopt a record:

(A) to execute or adopt a tangible symbol; or

(B) to attach to or logically associate with the record an electronic symbol, sound, or process.

(19) “State” means a state of the United States, the District of Columbia, Puerto Rico, the United States Virgin Islands, or any territory or insular possession subject to the jurisdiction of the United States.

(20) “Transfer” includes an assignment, conveyance, deed, bill of sale, lease, mortgage, security interest, encumbrance, gift, and transfer by operation of law.

(21) “Transferable interest” means the right, as originally associated with a person’s capacity as a member, to receive distributions from a limited liability company in accordance with the operating agreement, whether or not the person remains a member or continues to own any part of the right.

(22) “Transferee” means a person to which all or part of a transferable interest has been transferred, whether or not the transferor is a member.

### **Comment**

This Section contains definitions for terms used throughout the Act, while Section 1001 contains definitions specific to Article 10’s provisions on mergers, conversions and domestications. Section 405(g) contains an exception to the definition of “distribution,” which is specific to Section 405.

**Paragraph (1) [Certificate of organization]** – The original ULLCA and most other LLC statutes use “articles of organization” rather than “certificate of organization.” This Act purposely uses the latter term to signal that: (i) the certificate merely reflects the existence of an LLC (rather than being the locus for important governance rules); and (ii) this document is significantly different from articles of *incorporation*, which have a substantially greater power to affect *inter se* rules for the corporate entity and its owners. For the relationship between the certificate of organization and the operating agreement, see Section 112(d).

**Paragraph (2) [Contribution]** – This definition serves to distinguish capital contributions from other circumstances under which a member or would-be member might provide benefits to a limited liability company (e.g., providing services to the LLC as an employee or independent contractor, leasing property to the LLC). The definition contemplates three typical situations in which contributions are made, and for each situation establishes two “markers” to identify capital contributions – the purpose for which the contributor makes the contribution and the agreement that contemplates the contribution:



<b>circumstance</b>	<b>purpose/cause of providing benefits</b>	<b>the relevant agreement</b>
pre-formation deal among would-be initial members [Paragraph 2(A)]	in order to become initial member(s)	agreement among would-be initial members
deal between an existing LLC and would-be member [Paragraph 2(B)]	in order to become a member	agreement between the LLC and the would-be member
member contribution [Paragraph 2(C)]	in member's capacity as a member	operating agreement or an agreement between the member and the LLC

This definition does not encompass capital raised from transferees, which is sometimes provided for in operating agreements. In such circumstances, the default rules for liquidating distributions should be altered accordingly. *See* Section 708(b)(1) (“referring to contributions made by a member and not previously returned”).

**Paragraph (7) [Foreign limited liability company]** – Some statutes have elaborate definitions addressing the question of whether a non-U.S. entity is a “foreign limited liability company.” The NY statute, for example, defines a “foreign limited liability company” as:

an unincorporated organization formed under the laws of any jurisdiction, including any foreign country, other than the laws of this state (i) that is not authorized to do business in this state under any other law of this state and (ii) of which some or all of the persons who are entitled (A) to receive a distribution of the assets thereof upon the dissolution of the organization or otherwise or (B) to exercise voting rights with respect to an interest in the organization have, or are entitled or authorized to have, under the laws of such other jurisdiction, limited liability for the contractual obligations or other liabilities of the organization.

N.Y. LIMIT LIAB CO. LAW § 102(k) (McKinney 2006). ULLCA § 101(8) takes a similar but less complex approach (“an unincorporated entity organized under laws other than the laws of this State which afford limited liability to its owners comparable to the liability under Section 303 and is not required to obtain a certificate of authority to transact business under any law of this State other than this [Act]”). This Act follows Delaware’s still simpler approach. DEL. CODE ANN. tit. 6, § 18-101(4) (2006) (“denominated as such”).

**Paragraph (8) [Limited liability company]** – This definition makes no reference to a limited liability company having members upon formation, but Section 201 does. For a detailed discussion of the “shelf LLC” issue, see the Comment to Section 201.

**Paragraph (9) [Manager]** – The Act uses the word “manager” as a term of art, whose applicability is confined to manager-managed LLCs. The phrase “manager-managed” is itself a term of art, referring only to an LLC whose operating agreement refers to the LLC as such. Paragraph 10 (defining “manager-managed limited liability company”). Thus, for purposes of this Act, if the members of a *member*-managed LLC delegate plenipotentiary management authority to one person (whether or not a member), this Act’s references to “manager” do not apply to that person.

This approach does have the potential for confusion, but confusion around the term “manager” is common to almost all LLC statutes. The confusion stems from the choice to define “manager” as a term of art in a way that can be at odds with other, common usages of the word. For example, a member-managed LLC might well have an “office manager” or a “property manager.” Moreover, in a manager-managed LLC, the “property manager” is not likely to be a manager as the term is used in many LLC statutes. *See, e.g., Brown v. MR Group, LLC*, 278 Wis.2d 760, 768-9, 693 N.W.2d 138, 143 (Wis.App. 2005) (rejecting a party’s urging to use the dictionary definition of “manager” in determining coverage of a policy applicable to a limited liability company and its “managers” and relying instead on the meaning of the term under the Wisconsin LLC act).

Under this Act, the category of “person” is not limited to individuals. Therefore, a “manager” need not be a natural person. After a person ceases to be a manager, the term “manager” continues to apply to the person’s conduct while a manager. *See* Section 407(c)(7).

**Paragraph (10) [Manager-managed]** – This Act departs from most LLC statutes (including the original ULLCA) by authorizing a private agreement (the operating agreement) rather than a public document (certificate or articles of organization) to establish an LLC’s status as a manager-managed limited liability company. Using the operating agreement makes sense, because under this Act managerial structure creates no statutory power to bind the entity. *See* Section 301 (eliminating statutory apparent authority). The only direct consequences of manager-managed status are *inter se* – principally the triggering of a set of rules concerning management structure, fiduciary duty, and information rights. Sections 407 – 410. The management structure rules are entirely default provisions – subject to change in whole or in part by the operating agreement. The operating agreement can also significantly affect the duty and rights provisions. Section 110.

For pre-existing limited liability companies that eventually become subject to this Act, Section 1104(c) provides that “language in the limited liability company’s articles of organization designating the company’s management structure will operate as if that language were in the operating agreement.” For limited liability companies formed under this Act, the typical method to select manager-managed status will be an explicit provision of the operating agreement. However, a reference in the certificate of organization to manager-management might be evidence of the contents of the operating agreement. *See* Comment to Section 112(b).

An LLC that is “manager-managed” under this definition does not cease to be so simply because the members fail to designate anyone to act as a manager. In that situation, absent additional facts, the LLC is manager-managed and the manager position is vacant. Non-manager

members who exercise managerial functions during the vacancy (or at any other time) will have duties as determined by other law, most particularly the law of agency.

**Paragraph 10(A) and (B)** – In these paragraphs, the phrases “manager-managed” and “managed by managers” are “magic words” – i.e., for either subparagraph to apply, the operating agreement must include precisely the required language. However, the word “expressly” does not mean “in writing” or “in a record.” This Act permits operating agreements to be oral (in whole or in part), and an oral provision of an operating agreement could contain the magic words. This Act also recognizes that provisions of an operating agreement may be reflected in patterns of conduct.

Oral and implied agreements invite memory problems and “swearing matches.” Section 110(a)(4) empowers the operating agreement to determine “the means and conditions for the amending the operating agreement.”

**Paragraph 10(C)** – In contrast to Paragraphs 10(A) and (B), this provision does not contain “magic words” and considers instead all terms of the operating agreement that expressly refer to management by managers.

**Paragraph 11 [Member]** – After a person has been dissociated as a member, Section 602, the term “member” continues to apply to the person’s conduct while a member. *See* Section 603(b).

**Paragraph 12 [Member-managed limited liability company]** – A limited liability company that does not effectively designate itself a manager-member limited liability company will operate, subject to any contrary provisions in the operating agreement, under statutory rules providing for management by the members. Section 407(a). For a discussion of potential confusion relating to the term “manager”, see the Comment to Paragraph 9 (Manager).

**Paragraph (13) [Operating Agreement]** – This definition must be read in conjunction with Sections 110 through 112, which further describe the operating agreement. An operating agreement is a contract, and therefore all statutory language pertaining to the operating agreement must be understood in the context of the law of contracts.

The definition in Paragraph 13 is very broad and recognizes a wide scope of authority for the operating agreement: “the matters described in Section 110(a).” Those matters include not only all relations *inter se* the members and the limited liability company but also all “activities of the company and the conduct of those activities.” Section 110(a)(3). Moreover, the definition puts no limits on the form of the operating agreement. To the contrary, the definition contains the phrase “whether oral, in a record, implied, or in any combination thereof”.

This Act states no rule as to whether the statute of frauds applies to an oral operating agreement. Case law suggests that an oral agreement to form a partnership or joint venture with a term exceeding one year is within the statute. *E.g. Abbott v. Hurst*, 643 So.2d 589, 592 (Ala. 1994) (“Partnership agreements, like other contracts, are subject to the Statute of Frauds. A contract of partnership for a term exceeding one year is within the Statute of Frauds and is void

unless it is in writing; however, a contract establishing a partnership terminable at the will of any partner is generally held to be capable of performance by its terms within one year of its making and, therefore, to be outside the Statute of Frauds.”) (citations omitted); *Pemberton v. Ladue Realty & Const. Co.*, 362 Mo. 768, 770-71, 244 S.W.2d 62, 64 (Mo. 1951) (rejecting plaintiff’s contention that mere part performance sufficed to take the oral agreement outside the statute and holding that partnership was therefore at will); *Ebker v. Tan Jay Int’l, Ltd.*, 739 F.2d 812, 827-28 (2d Cir.1984) (same analysis with regard to a joint venture). However, it is not possible to form an LLC without someone signing and delivering to the filing officer a certificate of organization in record form, Section 201(a), and the Act itself then establishes the LLC’s duration. Subject to the operating agreement, that duration is perpetual. Section 104(c). An oral provision of an operating agreement calling for performance that extends beyond a year might be within the one-year provision – e.g., an oral agreement that a particular member will serve (and be permitted to serve) as manager for three years.

An oral provision of an operating agreement which involves the transfer of land, whether by or to the LLC, might come within the land provision of the statute of frauds. *Froiseth v. Nowlin*, 156 Wash. 314, 316, 287 P. 55, 56 (Wash. 1930) (“[The land provision] applies to an oral contract to transfer or convey partnership real property, and the interest of the other partners therein, to one partner as an individual, as well as to a parol contract by one of the parties to convey certain land owned by him individually to the partnership, or to another partner, or to put it into the partnership stock.”) (quoting 27 CORPUS JURIS 220).”).

In contrast, the fact that a limited liability company owns or deals in real property does not bring within the land provision agreements pertaining to the LLC’s membership interests. Interests in a limited liability company are personal property and reflect no direct interest in the entity’s assets. Re-ULLCA §§ 501 & 102(21). Thus, the real property issues pertaining to the LLC’s ownership of land do not “flow through” to the members and membership interests. See, e.g., *Wooten v. Marshall*, 153 F. Supp. 759, 763-764 (S.D. N.Y. 1957) (involving an “oral agreement for a joint venture concerning the purchase, exploitation and eventual disposition of this 160 acre tract” and stating “[t]he real property acquired and dealt with by the venturers takes on the character of personal property as between the partners in the enterprise, and hence is not covered by [the Statute of Frauds].”

The operating agreement may comprise a number of separate documents (or records), however denominated, unless the operating agreement itself provides otherwise. Section 110(a)(4). Absent a contrary provision in the operating agreement, a threshold qualification for status as part of the “operating agreement” is the assent of all the persons then members. An agreement among less than all of the members might well be enforceable among those members as parties, but would not be part of the operating agreement.

An agreement to form an LLC is not itself an operating agreement. The term “operating agreement” presupposes the existence of members, and a person cannot have “member” status until the LLC exists. However, the Act’s very broad definition of “operating agreement” means that, as soon as a limited liability company has any members, the limited liability company has an operating agreement. For example, suppose: (i) two persons orally and informally agree to join their activities in some way through the mechanism of an LLC, (ii) they form the LLC or

cause it to be formed, and (iii) without further ado or agreement, they become the LLC's initial members. The LLC has an operating agreement. "[A]ll the members" have agreed on who the members are, and that agreement – no matter how informal or rudimentary – is an agreement "concerning the matters described in Section 110(a)." (To the extent the agreement does not provide the *inter se* "rules of the game," this Act "fills in the gaps." Section 110(b).)

The same result follows when a person becomes the sole initial member of an LLC. It is not plausible that the person would lack any understanding or intention with regard to the LLC. That understanding or intention constitutes an "agreement of all the members of the limited liability company, including a sole member."

It may seem oxymoronic to refer an "agreement of . . . a sole member," but this approach is common in LLC statutes. *See, e.g.*, ARIZ. REV. STAT. ANN. § 29-601 (14)(b) (2006) (defining operating agreement to mean "in the case of a limited liability company that has a single member, any written or oral statement of the member made in good faith"); COLO. REV. STAT. ANN. § 7-80-102 (11)(b)(I) (West 2006) (defining operating agreement to include, in the case of a single member LLC "[a]ny writing, without regard to whether such writing otherwise constitutes an agreement . . . signed by the sole member"; N.H. REV. STAT. ANN. § 304-c:1 (VI) (2006) (defining limited liability company agreement to include "a document adopted by the sole member"); OR. REV. STAT. ANN. § 63.431(2) (2005) (vesting the "power to adopt, alter, amend or repeal an operating agreement of . . . a single member limited liability company, in the sole member of the limited liability company"); R.I. GEN. LAWS § 7-16-2 (19) (2005) (stating that the term operating agreement "includes a document adopted by the sole member of a limited liability company that has only one member"); and WASH. REV. CODE ANN. § 25.15.005 (5) (West 2006): (defining limited liability company agreement to include "any written statement of the sole member").

This re-definition of "agreement" is a function of "path dependence." By the time single-member LLCs became widely accepted, almost all LLC statutes were premised on the LLC's key organic document being the operating agreement. Because a key function of the operating agreement is to override statutory default rules, it was necessary to make clear that a sole member could make an operating agreement. Such an agreement may also be of interest to third parties, because the operating agreement binds the LLC. Section 111(a).

In light of Paragraph 13's broad definition, it is possible to argue that any activity involving unanimous consent of the members becomes part of the operating agreement. For example, if pursuant to an operating agreement all the members consent to the redemption of one-half of the managing-member's transferable interest, does that action constitute an addition to the agreement?

Typically, such questions will turn on the practical issue of whether the unanimous consent pertained solely to a single event (now past) or also to future circumstances (now in controversy) rather than on the semantic question of whether the operating agreement has been amended. Occasionally, however, the amendment *vel non* question could have practical import. For example, if the operating agreement entitles a non-member to approve (or veto) amendments, see Section 112(a), the members and the non-member might see the matter quite

differently.

Careful drafting of veto provisions can help avoid controversy – e.g., by defining with specificity the type of decisions subject to the veto. On the question of how far a written (or “in a record”) operating agreement can go to prevent oral or implied-in-fact terms, see Section 110(a)(4).

If it is necessary for a court to decide whether the contents of a matter approved by unanimous consent have become part of the operating agreement, the court should rely on principles of contract interpretation and look:

- first, at the manifestations of the members, including:
  - the manifestations made to give the unanimous consent; and
  - any terms of the operating agreement (e.g., terms specifying how matters become part of the operating agreement); and
- second, at whether, viewed from the perspective of a reasonable person in the position of the members giving consent, the consent was intended to incorporate the matter into the ongoing “rules of the game” or merely take some particular action as already permitted by those rules.

Of course, if all the members have the same understanding, the reasonableness *vel non* of that understanding is irrelevant and the shared meaning governs. *See* RESTATEMENT (SECOND) OF CONTRACTS, § 201(1) (1981).

**Paragraph (14) [Organizer]** – If an LLC is to have one or more members when the filing officer files the certificate of organization, the organizer: (i) acts on behalf of the person or persons who will become the LLC’s initial members, Section 401(a) and (b); and (ii) has no function other than to compose, sign, and deliver to the filing officer for filing the certificate of organization. Section 201(a). If an LLC is to have its first member sometime *after* the filing officer files the certificate of organization, the organizer has the power to admit the initial member or members, Section 401(c). Whether in this latter category of circumstances the organizer acts on behalf of the initial member or members is determined under ordinary principles of agency law and depends on the facts of each situation.

**Paragraph (20) [Transfer]** –The reference to “transfer by operation of law” is significant in connection with Section 502 (Transfer of Transferable Interest). That section severely restricts a transferee’s rights (absent the consent of the members), and this definition makes those restrictions applicable, for example, to transfers ordered by a family court as part of a divorce proceeding and transfers resulting from the death of a member. The restrictions also apply to transfers in the context of a member’s bankruptcy, except to the extent that bankruptcy law supersedes this Act.

**Paragraph (21) [Transferee]** – “Transferee” has displaced “assignee” as the Conference’s term of art.

SECTION 103. KNOWLEDGE; NOTICE.

(a) A person knows a fact when the person:

- (1) has actual knowledge of it; or
- (2) is deemed to know it under subsection (d)(1) or law other than this [act].

(b) A person has notice of a fact when the person:

(1) has reason to know the fact from all of the facts known to the person at the time in question; or

- (2) is deemed to have notice of the fact under subsection (d)(2);

(c) A person notifies another of a fact by taking steps reasonably required to inform the other person in ordinary course, whether or not the other person knows the fact.

(d) A person that is not a member is deemed:

(1) to know of a limitation on authority to transfer real property as provided in Section 302(g); and

- (2) to have notice of a limited liability company's:

(A) dissolution, 90 days after a statement of dissolution under Section 702(b)(2)(A) becomes effective;

(B) termination, 90 days after a statement of termination Section 702(b)(2)(F) becomes effective; and

(C) merger, conversion, or domestication, 90 days after articles of merger, conversion, or domestication under [Article] 10 become effective.

**Comment**

This section is substantially slimmer than the corresponding provisions of previous uniform acts pertaining to business organizations (RUPA, ULLCA, and ULPA (2001)). Each of those acts borrowed heavily from the comparable UCC provisions. For the most part, this Act relies instead on generally applicable principles of agency law, and therefore this section is mostly confined to rules specifically tailored to this Act.

Several facets of this section warrant particular note. First, and most fundamentally, because this Act does not provide for “statutory apparent authority,” see Section 301, this section contains no special rules for attributing to an LLC information possessed, communicated to, or communicated by a member or manager.

Second, the section contains no generally applicable provisions determining when an organization is charged with knowledge or notice, because those imputation rules: (i) comprise core topics within the law of agency; (ii) are very complicated; (iii) should not have any different content under this Act than in other circumstances; and (iv) are the subject of considerable

attention in the new Restatement (Third) of Agency.

Third, this Act does not define “notice” to include “knowledge.” Although conceptualizing the latter as giving the former makes logical sense and has a long pedigree, that conceptualization is counter-intuitive for the non-*aficionado*. In ordinary usage, notice has a meaning separate from knowledge. This Act follows ordinary usage and therefore contains some references to “knowledge or notice.”

**Subsection (a)(2)** – In this context, the most important source of “law other than this [act]” is the common law of agency.

**Subsection (b)(1)** – The “facts known to the person at the time in question” include facts the person is deemed to know under subsection (a)(2).

**Subsection (d)(2)** – Under this Act, the power to bind a limited liability company to a third party is primarily a matter of agency law. Section 301, Comment. The constructive notice provided under this paragraph will be relevant if a third party makes a claim under agency law that someone who purported to act on behalf of a limited liability company had the apparent authority to do so.

#### SECTION 104. NATURE, PURPOSE, AND DURATION OF LIMITED LIABILITY COMPANY.

(a) A limited liability company is an entity distinct from its members.

(b) A limited liability company may have any lawful purpose, regardless of whether for profit.

(c) A limited liability company has perpetual duration.

**Legislative Note:** *This state should consider whether to amend statutes protecting the public interest in organizations formed for charitable or similar purposes.*

#### Comment

**Subsection (a)** – The “separate entity” characteristic is fundamental to a limited liability company and is inextricably connected to both the liability shield, Section 304, and the charging order provision, Section 503.

**Subsection (b)** – The phrase “any lawful purpose, regardless of whether for profit” means that: (i) a limited liability company need not have any business purpose; and (ii) the issue of profit *vel non* is irrelevant to the question of whether a limited liability company has been validly formed. Although some LLC statutes continue to require a business purpose, this Act follows the current trend and takes a more expansive approach.

The expansive approach comports both with the original ULLCA and with ULPA (2001). See ULLCA §§ 112(a) (captioned with reference to “Nature of Business” and permitting “any



lawful purpose, subject to any law of this State governing or regulating business”) and 101(3) (defining “Business” as including “every trade, occupation, profession, and other lawful purpose, whether or not carried on for profit”); ULPA (2001) § 104(b) (permitting a limited partnership to be organized for any “lawful” purpose). *Compare* UPA § 6 (defining a general partnership as organized for profit), RUPA § 101(6) (same), and RULPA (1976/85) § 106 (delineating the “Nature of [a limited partnership’s] Business” by linking back to “any business that a partnership without limited partners may carry on”).

The subsection does not bar a limited liability company from being organized to carry on charitable activities, and this act does not include any protective provisions pertaining to charitable purposes. Those protections must be (and typically are) found in other law, although sometimes that “other law” appears within a state’s non-profit corporation statute. *See, e.g.*, MINN. STAT. § 317A.811 (2006) (providing restrictions on charitable organizations that seek to “dissolve, merge, or consolidate, or to transfer all or substantially all of their assets” but imposing those restrictions only on “corporations,” which are elsewhere defined as corporations incorporated under the non-profit corporation act).

**Subsection (c)** – In this context, the word “perpetual” is a misnomer, albeit one commonplace in LLC statutes. Like all current LLC statutes, this Act provides several consent-based avenues to override perpetuity: a term specified in the operating agreement; an event specified in the operating agreement; member consent. Section 701 (events causing dissolution). In this context, “perpetuity” actually means that the Act does not require a definite term and creates no nexus between the dissociation of a member and the dissolution of the entity. (The dissociation of an LLC’s last remaining member does threaten dissolution. Section 701(a)(3) (stating, as a default rule, that a limited liability company dissolves “upon . . . the passage of 90 consecutive days during which the limited liability company has no members”).

An operating agreement is not a publicly-filed document, which means that the public record pertaining to a limited liability company will not necessarily reveal whether a limited liability company actually has a perpetual duration. *Accord* ULPA (2001) § 104, comment to subsection (c) (“The partnership agreement has the power to vary this subsection [which provides for perpetual duration], either by stating a definite term or by specifying an event or events which cause dissolution. . . . [The limited partnership act] also recognizes several other occurrences that cause dissolution. Thus, the public record pertaining to a limited partnership will not necessarily reveal whether the limited partnership actually has a perpetual duration.”)

**SECTION 105. POWERS.** A limited liability company has the capacity to sue and be sued in its own name and the power to do all things necessary or convenient to carry on its activities.

### **Comment**

Following ULPA (2001), § 105, this Act omits as unnecessary any detailed list of specific powers. *Compare* ULLCA § 112 (containing a detailed list).

The capacity to sue and be sued is mentioned specifically so that Section 110(c)(1) can

prohibit the operating agreement from varying that capacity. An LLC's standing to enforce the operating agreement is a separate matter, which is covered by Section 111(a) (stating, as a default rule, that the limited liability company "may enforce the operating agreement").

SECTION 106. GOVERNING LAW. The law of this state governs:

- (1) the internal affairs of a limited liability company; and
- (2) the liability of a member as member and a manager as manager for the debts, obligations, or other liabilities of a limited liability company.

### Comment

**Paragraph (1)** – Like any other legal concept, "internal affairs" may be indeterminate at its edges. However, the concept certainly includes interpretation and enforcement of the operating agreement, relations among the members as members; relations between the limited liability company and a member as a member, relations between a manager-managed limited liability company and a manager, and relations between a manager of a manager-managed limited liability company and the members as members. *Compare* RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 302, cmt. a (defining "internal affairs" with reference to a corporation as "the relations inter se of the corporation, its shareholders, directors, officers or agents").

The operating agreement cannot alter this provision. Section 110(c)(2). However, an operating agreement may lawfully incorporate by reference the provisions of another state's LLC statute. If done correctly, this incorporation makes the foreign statutory language part of the operating agreement, and the incorporated terms (together with the rest of the operating agreement) then govern the members (and those claiming through the members) to the extent not prohibited by this Act. *See* Section 110. This approach does not switch the limited liability company's governing law to that of another state, but instead takes the provisions of another state's law and incorporates them by reference into the contract among the members.

**Paragraph (2)** – This paragraph certainly encompasses Section 304 (the liability shield) but does not necessarily encompass a claim that a member or manager is liable to a third party for (i) having purported to bind a limited liability company to the third party; or (ii) having committed a tort against the third party while acting on the limited liability company's behalf or in the course of the company's business. That liability is not by status (i.e., not "as member . . . [or] as manager") but rather results from function or conduct. Contrast Section 301(b) (stating that, although this Act does not make a member as member the agent of a limited liability company, other law may make an LLC liable for the conduct of a member).

This paragraph is stated separately from Paragraph (1), because it can be argued that the liability of members and managers to third parties is not an internal affair. *See, e.g.,* RESTATEMENT (SECOND) OF CONFLICT OF LAWS, § 307 (treating shareholders' liability separately from the internal affairs doctrine). A few cases subsume owner/manager liability into internal affairs, but many do not. *See, e.g., Kalb, Voorhis & Co. v. American Fin. Corp.*, 8 F.3d 130, 132 (2nd Cir. 1993). In any event, the rule stated in this paragraph is correct. All sensible authorities agree that, except in extraordinary circumstances, "shield-related" issues should be determined

according to the law of the state of organization.

SECTION 107. SUPPLEMENTAL PRINCIPLES OF LAW. Unless displaced by particular provisions of this [act], the principles of law and equity supplement this [act].

SECTION 108. NAME.

(a) The name of a limited liability company must contain the words “limited liability company” or “limited company” or the abbreviation “L.L.C.”, “LLC”, “L.C.”, or “LC”. “Limited” may be abbreviated as “Ltd.”, and “company” may be abbreviated as “Co.”.

(b) Unless authorized by subsection (c), the name of a limited liability company must be distinguishable in the records of the Department of State from:

(1) the name of each person that is not an individual and that is incorporated, organized, or authorized to transact business in this state;

(2) the limited liability company name stated in each certificate of organization that has been delivered to the Department of State pursuant to Section 201(a); and

(3) each name reserved under Section 109 and [cite other state laws allowing the reservation or registration of business names, including fictitious or assumed name statutes].

(c) A limited liability company may apply to the Department of State for authorization to use a name that does not comply with subsection (b). The Department of State shall authorize use of the name applied for if, as to each noncomplying name:

(1) the present user, registrant, or owner of the noncomplying name consents in a signed record to the use and submits an undertaking in a form satisfactory to the Department of State to change the noncomplying name to a name that complies with subsection (b) and is distinguishable in the records of the Department of State from the name applied for; or

(2) the applicant delivers to the Department of State a certified copy of the final judgment of a court establishing the applicant’s right to use in this state the name applied for.

(d) Subject to Section 805, this section applies to a foreign limited liability company transacting business in this state which has a certificate of authority to transact business in this state or which has applied for a certificate of authority.

**Comment**

Subsection (a) is taken verbatim from ULLCA § 105(a). Except for subsection (b)(2), the rest of the section is taken from ULPA (2001) § 108.

**Subsection (b)(2)** – This language is necessary to protect a name contained in a filed certificate of organization that has not become effective because there are no members. Section 201(d)(1).

#### SECTION 109. RESERVATION OF NAME.

(a) A person may reserve the exclusive use of the name of a limited liability company, including a fictitious or assumed name for a foreign limited liability company whose name is not available, by delivering an application to the Department of State for filing. The application must state the name and address of the applicant and the name proposed to be reserved. If the Department of State finds that the name applied for is available, it must be reserved for the applicant's exclusive use for a 120-day period.

(b) The owner of a name reserved for a limited liability company may transfer the reservation to another person by delivering to the Department of State for filing a signed notice of the transfer which states the name and address of the transferee.

#### **Comment**

**Source:** ULLCA, § 106.

**Subsection (a)** – Although 120-day reservation period is non-renewable, this subsection does not prevent a person from seeking successive 120-day periods of reservation.

#### SECTION 110. OPERATING AGREEMENT; SCOPE, FUNCTION, AND LIMITATIONS.

(a) Except as otherwise provided in subsections (b) and (c), the operating agreement governs:

- (1) relations among the members as members and between the members and the limited liability company;
- (2) the rights and duties under this [act] of a person in the capacity of manager;
- (3) the activities of the company and the conduct of those activities;
- (4) the means and conditions for amending the operating agreement; and
- (5) the requirements for approval of a merger, conversion or domestication.

(b) To the extent the operating agreement does not otherwise provide for a matter described in subsection (a), this [act] governs the matter.

(c) An operating agreement may not:

- (1) vary a limited liability company's capacity under Section 105 to sue and be sued in its own name;
- (2) vary the law applicable under Section 106;
- (3) vary the power of the court under Section 204;
- (4) subject to subsections (d) through (g), eliminate the duty of loyalty, the duty of care, or any other fiduciary duty;
- (5) subject to subsections (d) through (g), eliminate the contractual obligation of good faith and fair dealing under Section 409(d);
- (6) unreasonably restrict the duties and rights stated in Section 410;
- (7) vary the power of a court to decree dissolution in the circumstances specified in Section 701(a)(4) and (5);
- (8) vary the requirement to wind up a limited liability company's business as specified in Section 702(a) and (b)(1);
- (9) unreasonably restrict the right of a member to maintain an action under [Article] 9;
- (10) restrict the right to approve a merger, conversion, or domestication under Section 1014 to a member that will have personal liability with respect to a surviving, converted, or domesticated organization; or
- (11) except as otherwise provided in Section 112(b), restrict the rights under this [act] of a person other than a member or manager.

(d) If not manifestly unreasonable, the operating agreement may:

- (1) restrict or eliminate the duty:
  - (A) as required in Section 409(b)(1) and (g), to account to the limited liability company and to hold as trustee for it any property, profit, or benefit derived by the member in the conduct or winding up of the company's business, from a use by the member of the company's property, or from the appropriation of a limited liability company opportunity;
  - (B) as required in Section 409(b)(2) and (g), to refrain from dealing with the company in the conduct or winding up of the company's business as or on behalf of a party having an interest adverse to the company; and
  - (C) as required by Section 409(b)(3) and (g), to refrain from competing with the company in the conduct of the company's business before the dissolution of the

company;

(2) identify specific types or categories of activities that do not violate the duty of

loyalty;

(3) alter the duty of care, except to authorize intentional misconduct or knowing violation of law;

(4) alter any other fiduciary duty, including eliminating particular aspects of that duty; and

(5) prescribe the standards by which to measure the performance of the contractual obligation of good faith and fair dealing under Section 409(d).

(e) The operating agreement may specify the method by which a specific act or transaction that would otherwise violate the duty of loyalty may be authorized or ratified by one or more disinterested and independent persons after full disclosure of all material facts.

(f) To the extent the operating agreement of a member-managed limited liability company expressly relieves a member of a responsibility that the member would otherwise have under this [act] and imposes the responsibility on one or more other members, the operating agreement may, to the benefit of the member that the operating agreement relieves of the responsibility, also eliminate or limit any fiduciary duty that would have pertained to the responsibility.

(g) The operating agreement may alter or eliminate the indemnification for a member or manager provided by Section 408(a) and may eliminate or limit a member or manager's liability to the limited liability company and members for money damages, except for:

(1) breach of the duty of loyalty;

(2) a financial benefit received by the member or manager to which the member or manager is not entitled;

(3) a breach of a duty under Section 406;

(4) intentional infliction of harm on the company or a member; or

(5) an intentional violation of criminal law.

(h) The court shall decide any claim under subsection (d) that a term of an operating agreement is manifestly unreasonable. The court:

(1) shall make its determination as of the time the challenged term became part of the operating agreement and by considering only circumstances existing at that time; and

(2) may invalidate the term only if, in light of the purposes and activities of the limited liability company, it is readily apparent that:

(A) the objective of the term is unreasonable; or

(B) the term is an unreasonable means to achieve the provision’s objective.

**Comment**

The operating agreement is pivotal to a limited liability company, and Sections 110 through 112 are pivotal to this Act. They must be read together, along with Section 102(13) (defining the operating agreement).

One of the most complex questions in the law of unincorporated business organizations is the extent to which an agreement among the organization’s owners can affect the law of fiduciary duty. This section gives special attention to that question and is organized as follows:

Subsection (a)	grants broad, <i>general</i> authority to the operating agreement
Subsection (b)	establishes this Act as comprising the “default rules” (“gap fillers”) for matters within the purview of the operating agreement but not addressed by the operating agreement
Subsection (c)	states restrictions on the power of the operating agreement, especially but not exclusively with regard to fiduciary duties and the contractual obligation of good faith
Subsection (d)	contains <i>specific</i> grants of authority for the operating agreement with regard to fiduciary duty and the contractual obligation of good faith; expressed so as to state restrictions on those specific grants – including the “if not manifestly unreasonable” standard
Subsection (e)	specifically grants the operating agreement the power to provide mechanisms for approving or ratifying conduct that would otherwise violate the duty of loyalty; expressed so as to state restrictions on those mechanism – full disclosure and disinterested and independent

	decision makers
Subsection (f)	specifically authorizes the operating agreement to divest a member of fiduciary duty with regard to a matter if the operating agreement is also divesting the person of responsibility for the matter (and imposing that responsibility on one or more other members)
Subsection (g)	contains <i>specific</i> grants of authority for the operating agreement with regard to indemnification and exculpatory provisions; expressed so as to state restrictions on those specific grants
Subsection (h)	provides rules for applying the “not manifestly unreasonable” standard established by subsection (d)

A limited liability company is as much a creature of contract as of statute, and Section 102(13) delineates a very broad scope for “operating agreement.” As a result, once an LLC comes into existence and has a member, the LLC necessarily has an operating agreement. *See* Comment to Section 102(13). Accordingly, this Act refers to “the operating agreement” rather than “an operating agreement.”

This phrasing should not, however, be read to require a limited liability company or its members to take any formal action to adopt an operating agreement. *Compare* CAL. CORP. CODE § 17050(a) (West 2006) (“In order to form a limited liability company, one or more persons shall execute and file articles of organization with, and on a form prescribed by, the Secretary of State and, either before or after the filing of articles of organization, the members shall have entered into an operating agreement.”)

The operating agreement is the exclusive consensual process for modifying this Act’s various default rules pertaining to relationships *inter se* the members and between the members and the limited liability company. Section 110(b). The operating agreement also has power over “the rights and duties under this [act] of a person in the capacity of manager,” subsection (a)(2), and “the obligations of a limited liability company and its members to a person in the person’s capacity as a transferee or dissociated member.” Section 112(b).

**Subsection (a)** – This section describes the very broad scope of a limited liability company’s operating agreement, which includes all matters constituting “internal affairs.” Compare Section 106(1) (using the phrase “internal affairs” in stating a choice of law rule). This broad grant of authority is subject to the restrictions stated in subsection (c), including the broad restriction stated in paragraph (c)(11) (concerning the rights under this Act of third parties).



**Subsection (a)(1)** – Under this Act, a limited liability company is emphatically an entity, and the members lack the power to alter that characteristic.

**Subsection (a)(2)** – Under this paragraph, the operating agreement has the power to affect the rights and duties of managers (including non-member managers). Because the term “[o]perating agreement . . . includes the agreement as amended or restated,” Section 102(13), this paragraph gives the members the ongoing power to define the role of an LLC’s managers. Power is not the same as right, however, and exercising the power provided by this paragraph might constitute a breach of a separate contract between the LLC and the manager. A non-member manager might also have rights under Section 112(a).

**Subsection (a)(4)** – If the operating agreement does not address this matter, under subsection (b) this Act provides the rule. The rule appears in Section 407(b)(5) and 407(c)(4)(D) (unanimous consent).

**Subsection (a)(5)** – Under this paragraph, the operating agreement has the power to modify the requirement that all members of an LLC must consent to a plan of merger (Section 1003(a)), conversion (Section 1007(a)) or domestication (1011(a)).

This Act does not specially authorize the operating agreement to limit the sources in which terms of the operating agreement might be found or limit amendments to specified modes (e.g., prohibiting modifications except when consented to in writing). *Compare* UCC § 2-209(2) (authorizing such prohibitions in a “signed agreement” for the sale of goods). However, this Paragraph (a)(4) could be read to encompass such authorization. Also, under Section 107 the parol evidence rule will apply to a written operating agreement containing an appropriate merger provision.

**Subsection (c)** – If a person claims that a term of the operating agreement violates this subsection, as a matter of ordinary procedural law the burden is on the person making the claim.

**Subsection (c)(4)** – This limitation is less powerful than might first appear, because subsections (d) through (g) specifically authorize significant alterations to fiduciary duty. The reference to “or any other fiduciary duty” is necessary because the Act has “un-cabined” fiduciary duty. *See* Comment to Section 409.

**Subsection (c)(9)** – Arbitration and forum selection provisions are commonplace in business agreements, and this paragraph’s restrictions do not reflect any special hostility to or skepticism of such provisions.

**Subsection (c)(10)** – Under Section 1014:

- each member is protected from being merged, converted, or domesticated “into” the status of an unshielded general partner (or comparable position) without the member having *directly* consented to either:
  - the merger, conversion, or domestication; or

- an operating agreement provision that permits such transactions to occur with less than unanimous consent of the members; and
- merely consenting to an operating agreement provision that permits amendment of the operating agreement with less than unanimous consent of the members does not qualify as the requisite direct consent.

The sole function of subsection (c)(10) is to protect Section 1014 by denying the operating agreement the power to restrict or otherwise undercut the protections of Section 1014.

**Subsection (c)(11)** – This limitation pertains only to “the rights under this[act] of” third parties. The extent to which an operating agreement can affect other rights of third parties is a question for other law, particularly the law of contracts.

**Subsection (d)** – Delaware recently amended its LLC statute to permit an operating agreement to fully “eliminate” fiduciary duty within an LLC. This Act rejects the ultra-contractarian notion that fiduciary duty within a business organization is merely a set of default rule and seeks instead to balance the virtues of “freedom of contract” against the dangers that inescapably exist when some have power over the interests of others. As one source has explained:

The open-ended nature of fiduciary duty reflects the law’s long-standing recognition that devious people can smell a loophole a mile away. For centuries, the law has assumed that (1) power creates opportunities for abuse and (2) the devious creativity of those in power may outstrip the prescience of those trying, through ex ante contract drafting, to constrain that combination of power and creativity.

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Subsection (h) contains rules for applying the “not manifestly unreasonable” standard.

**Subsection (d)(1)** – Subject to the “not manifestly unreasonable” standard, this paragraph empowers the operating agreement to eliminate all aspects of the duty of loyalty listed in Section 409. The contractual obligation of good faith would remain, see subsections(c)(5) and (d)(5), as would any other, uncodified aspects of the duty of loyalty. *See* Comment to Section 409 (explaining the decision to “un-cabin” fiduciary duty). *See also* subsection (d)(4) (empowering the operating agreement to “alter any other fiduciary duty, including eliminating particular aspects of that duty”).

**Subsection (d)(3)** – The operating agreement’s power to affect this Act’s duty of care both parallels and differs from the agreement’s power to affect this Act’s duty of loyalty as well as any other fiduciary duties not codified in the statute. With regard to all fiduciary duties, the operating agreement is subject to the “manifestly unreasonable” standard. The differences concern: (i) the extent of the operating agreement’s power to restrict the duty; and (ii) the power of the operating agreement to provide indemnity or exculpation for persons subject to the duty.

duty	<p>extent of operating agreement's power to restrict the duty</p> <p>(subject to the "manifestly unreasonable" standard)</p> <p>Section 110(d)(1), (3) and (4)</p>	<p>power of the operating agreement to provide indemnity or exculpation w/r/t breach of the duty</p> <p>Section 110(g)</p>
<b>loyalty</b>	<b>restrict or completely eliminate</b>	<b>none</b>
<b>care</b>	<b>alter, but not eliminate; specifically may not authorize intentional misconduct or knowing violation of law</b>	<b>complete</b>
<b>other fiduciary duties, not codified in the statute</b>	<b>restrict or completely eliminate</b>  <b>Section 110(4)</b>	<b>complete</b>

**Subsection (e)** – Section 409(f) states the Act's default rule for authorization or ratification – unanimous consent. This subsection specifically empowers the operating agreement to provide alternate mechanisms but, in doing so, imposes significant restrictions – namely, any alternate mechanism must involve full disclosure to, and the disinterestedness and independence of, the decision makers. These restrictions are consonant with ordinary notions of authorization and ratification.

This Act provides four separate methods through which those with management power in a limited liability company can proceed with conduct that would otherwise violate the duty of loyalty:

Method	Statutory Authority
<b>The operating agreement might eliminate the duty or otherwise</b>	<b>Section 110(d)(1) and</b>

<b>permit the conduct, without need for further authorization or ratification.</b>	<b>(2)</b>
<b>The conduct might be authorized or ratified by all the members after full disclosure.</b>	<b>Section 409(f)</b>
<b>The operating agreement might establish a mechanism other than the informed consent for authorizing or ratifying the conduct.</b>	<b>Section 110(e)</b>
<b>In the case of self-dealing the conduct might be successfully defended as being or having been fair to the limited liability company.</b>	<b>Section 409(e)</b>

**Subsection (f)** – This subsection is intended to make clear that – regardless of the strictures stated elsewhere in this section – in the specified circumstances the operating agreement can entirely strip away the pertinent fiduciary duties.

**Subsection (g)** – This subsection specifically empowers the operating agreement to address matters of indemnification and exculpation but subjects that power to stated limitations. Those limitations are drawn from the raft of exculpatory provisions that sprung up in corporate statutes in response to *Smith v. Van Gorkum*, 488 A.2d 858 (Del. 1985). Delaware led the response with DEL. CODE ANN. tit. 8, § 102(b)(7) (2006), and a number of LLC statutes have similar provisions. *E.g.* GA. CODE ANN. § 14-11-305(4)(A) (West 2006); IDAHO CODE ANN. § 53-624(1) (2006). For an extreme example, see VA. CODE ANN. § 13.1-1025 (West 2006) (establishing limits of monetary liability as the default rule).

The restrictions stated in paragraphs (1) through (5) apply both to indemnification and exculpation. The power to “alter or eliminate the indemnification provided by Section 408(a)” includes the power to expand or reduce that indemnification.

**Subsection (g)(4)** – Due to this paragraph, an exculpatory provision cannot shield against a member’s claim of oppression. *See* Section 701(a)(5)(B) and (b).

**Subsection (h)** – The “not manifestly unreasonable standard” became part of uniform business entity statutes when RUPA imported the concept from the Uniform Commercial Code. This subsection provides rules for applying that standard, which are necessary because:

- Determining unreasonableness *inter se* owners of an organization is a different task than doing so in a commercial context, where concepts like “usages of trade” are available to inform the analysis. Each business organization must be understood in its own terms and context.
- If loosely applied, the standard would permit a court to rewrite the members’ agreement, which would destroy the balance this Act seeks to establish between freedom of contract and fiduciary duty.
- Case law research indicates that courts have tended to disregard the significance of the

word “manifestly.”

- Some decisions have considered reasonableness as of the time of the complaint, which means that a prospectively reasonable allocation of risk could be overturned because it functioned as agreed.

If a person claims that a term of the operating agreement is manifestly unreasonable under subsections (d) and (h), as a matter of ordinary procedural law the burden is on the person making the claim.

**Subsection (h)(1)** – The significance of the phrase “as of the time the term as challenged became part of the operating agreement” is best shown by example.

**EXAMPLE:** An LLC’s operating agreement as initially adopted includes a provision subjecting a matter to “the manager’s sole, reasonable discretion.” A year later, the agreement is amended to delete the word “reasonable.” Later, a member claims that, without the word “reasonable,” the provision is manifestly unreasonable. The relevant time under subsection (h)(1) is when the agreement was amended, not when the agreement was initially adopted.

**EXAMPLE:** When a particular manager-managed LLC comes into existence, its business plan is quite unusual and its success depends on the willingness of a particular individual to serve as the LLC’s sole manager. This individual has a rare combination of skills, experiences, and contacts, which are particularly appropriate for the LLC’s start-up. In order to induce the individual to accept the position of sole manager, the members are willing to have the operating agreement significantly limit the manager’s fiduciary duties. Several years later, when the LLC’s operations have turned prosaic and the manager’s talents and background are not nearly so crucial, a member challenges the fiduciary duty limitations as manifestly unreasonable. The relevant time under subsection (h)(1) is when the LLC began. Subsequent developments are not relevant, except as they might inferentially bear on the circumstances in existence at the relevant time.

## SECTION 111. OPERATING AGREEMENT; EFFECT ON LIMITED LIABILITY COMPANY AND PERSONS BECOMING MEMBERS; PREFORMATION AGREEMENT.

(a) A limited liability company is bound by and may enforce the operating agreement, whether or not the company has itself manifested assent to the operating agreement.

(b) A person that becomes a member of a limited liability company is deemed to assent to the operating agreement.

(c) Two or more persons intending to become the initial members of a limited liability company may make an agreement providing that upon the formation of the company the agreement will become the operating agreement. One person intending to become the initial

member of a limited liability company may assent to terms providing that upon the formation of the company the terms will become the operating agreement.

### **Comment**

**Subsection (a)** – This subsection does not consider whether a limited liability company is an indispensable party to a suit concerning the operating agreement. That is a question of procedural law, which can determine whether federal diversity jurisdiction exists.

**Subsection (b)** – Given the possibility of oral and implied-in-fact components to the operating agreement, see Comment to Section 110(a)(4), a person becoming a member of an existing limited liability company should take precautions to ascertain fully the contents of the operating agreement.

**Subsection (c)** – The second sentence refers to “assent to terms” rather than “make an agreement” because, under venerable principles of contract law, an agreement presupposes at least two parties. This Act specifically defines the operating agreement to include a sole member, Section 102(13), but a preformation arrangement is not an operating agreement. An operating agreement is among “members,” and, under this Act, the earliest a person can become a member is upon the formation of the limited liability company. Section 401.

## **SECTION 112. OPERATING AGREEMENT; EFFECT ON THIRD PARTIES AND RELATIONSHIP TO RECORDS EFFECTIVE ON BEHALF OF LIMITED LIABILITY COMPANY.**

(a) An operating agreement may specify that its amendment requires the approval of a person that is not a party to the operating agreement or the satisfaction of a condition. An amendment is ineffective if its adoption does not include the required approval or satisfy the specified condition.

(b) The obligations of a limited liability company and its members to a person in the person’s capacity as a transferee or dissociated member are governed by the operating agreement. Subject only to any court order issued under Section 503(b)(2) to effectuate a charging order, an amendment to the operating agreement made after a person becomes a transferee or dissociated member is effective with regard to any debt, obligation, or other liability of the limited liability company or its members to the person in the person’s capacity as a transferee or dissociated member.

(c) If a record that has been delivered by a limited liability company to the Department of State for filing and has become effective under this [act] contains a provision that would be ineffective under Section 110(c) if contained in the operating agreement, the provision is

likewise ineffective in the record.

(d) Subject to subsection (c), if a record that has been delivered by a limited liability company to the Department of State for filing and has become effective under this [act] conflicts with a provision of the operating agreement:

(1) the operating agreement prevails as to members, dissociated members, transferees, and managers; and

(2) the record prevails as to other persons to the extent they reasonably rely on the record.

### Comment

**Subsection (a)** – This subsection, derived from DEL. CODE ANN. tit. 6, § 18-302(e), permits a non-member to have veto rights over amendments to the operating agreement. Such veto rights are likely to be sought by lenders but may also be attractive to non-member managers.

EXAMPLE: A non-member manager enters into a management contract with the LLC, and that agreement provides in part that the LLC may remove the manager without cause only with the consent of members holding 2/3 of the profits interests. The operating agreement contains a parallel provision, but the non-member manager is not a party to the operating agreement. Later the LLC members amend the operating agreement to change the quantum to a simple majority and thereafter purport to remove the manager without cause. Although the LLC has undoubtedly breached its contract with the manager and subjected itself to a damage claim, the LLC has the power under Section 110(a)(2) to effect the removal – unless the operating agreement provided the non-member manager a veto right over changes in the quantum provision.

The subsection does not refer to member veto rights because, unless otherwise provided in the operating agreement, the consent of each member is necessary to effect an amendment. Section 407(b)(5) and (c)(4)(D).

**Subsection (b)** – The law of unincorporated business organizations is only beginning to grapple in a modern way with the tension between the rights of an organization’s owners to carry on their activities as they see fit (or have agreed) and the rights of transferees of the organization’s economic interests. (Such transferees can include the heirs of business founders as well as former owners who are “locked in” as transferees of their own interests. *See* Section 603(a)(3).).

If the law categorically favors the owners, there is a serious risk of expropriation and other abuse. On the other hand, if the law grants former owners and other transferees the right to seek judicial protection, that specter can “freeze the deal” as of the moment an owner leaves the enterprise or a third party obtains an economic interest.

*Bauer v. Blomfield Co./Holden Joint Venture*, 849 P2d 1365 (Alaska 1993) illustrates this

point nicely. The case arose after all the partners had approved a commission arrangement with a third party and the arrangement dried up all the partnership profits. When an assignee of a partnership interest objected, the court majority flatly rejected not only the claim but also the assignee's right to assert the claim. A mere assignee "was not entitled to complain about a decision made with the consent of all the partners." *Id.* at 1367. A footnote explained, "We are unwilling to hold that partners owe a duty of good faith and fair dealing to assignees of a partner's interest." *Id.* at 1367, n. 2.

The dissent, invoking the law of contracts, asserted that the majority had turned the statutory protection of the partners' management prerogatives into an instrument for abuse of assignees:

It is a well-settled principle of contract law that an assignee steps into the shoes of an assignor as to the rights assigned. Today, the court summarily dismisses this principle in a footnote and leaves the assignee barefoot....

As interpreted by the court, the [partnership] statute now allows partners to deprive an assignee of profits to which he is entitled by law for whatever outrageous motive or reason. The court's opinion essentially leaves the assignee of a partnership interest without remedy to enforce his right.

*Id.* at 1367-8 (Matthews, J., dissenting).

The *Bauer* majority is consistent with the limited but long-standing case law in this area (all of it pertaining to partnerships rather than LLCs). This subsection follows the *Bauer* majority and other cases by expressly subjecting transferees and dissociated members to operating agreement amendments made after the transfer or dissociation. *Compare* UPA § 32(2) (permitting an assignee to seek judicial dissolution of an at-will general partnership at any time and of a partnership for a term or undertaking if partnership continues in existence after the completion of the term or undertaking); RUPA § 801(6) (same except adding the requirement that the court determine that dissolution is equitable); ULLCA, § 801(5) (same as RUPA); ULLCA, § 801(4) (permitting a dissociated member to seek dissolution on the grounds *inter alia* of oppressive conduct). *See also* UCC §§ 9-405(a) and (b) and RESTATEMENT (SECOND) OF CONTRACTS § 338 (1981) (recognizing a duty of good faith applicable to the modification of a contract when an assignment of contract is in effect).

The issue of whether, in extreme and sufficiently harsh circumstances, transferees might be able to claim some type of duty or obligation to protect against expropriation, is a question for other law.

**Subsection (d)** – A limited liability company is a creature of contract as well as a creature of statute. It will be possible, albeit improvident, for the operating agreement to be inconsistent with the certificate of organization or other public filings pertaining to the limited liability company. For those circumstances, this subsection provides rules for determining which source of information prevails.

For members, managers and transferees, the operating agreement is paramount. For third



parties seeking to invoke the public record, actual knowledge of that record is necessary and notice, deemed notice, and deemed knowledge under Section 103 are irrelevant. A third party wishing to enforce the public record over the operating agreement must show reasonable reliance on the public record, and reliance presupposes knowledge.

The mere fact that a term is present in a publicly-filed record and not in the operating agreement, or *vice versa*, does not automatically establish a conflict. This subsection does not expressly cover a situation in which (i) one of the specified filed records contains information in addition to, but not inconsistent with, the operating agreement, and (ii) a person, other than a member or transferee, reasonably relies on the additional information. However, the policy reflected in this subsection seems equally applicable to that situation.

Section 110(a)(4) might also be relevant to the subject matter of this subsection. Absent a contrary provision in the operating agreement, language in an LLC's certificate of organization might be evidence of the members' agreement and might thereby constitute or at least imply a term of the operating agreement.

This subsection does not apply to records delivered to the Department of State for filing on behalf of persons other than a limited liability company.

#### SECTION 113. OFFICE AND AGENT FOR SERVICE OF PROCESS.

(a) A limited liability company shall designate and continuously maintain in this state:

- (1) an office, which need not be a place of its activity in this state; and
- (2) an agent for service of process.

(b) A foreign limited liability company that has a certificate of authority under Section 802 shall designate and continuously maintain in this state an agent for service of process.

(c) An agent for service of process of a limited liability company or foreign limited liability company must be an individual who is a resident of this state or other person with authority to transact business in this state.

#### **Comment**

Source: ULPA (2001), § 114.

#### SECTION 114. CHANGE OF DESIGNATED OFFICE OR AGENT FOR SERVICE OF PROCESS.

(a) A limited liability company or foreign limited liability company may change its designated office, its agent for service of process, or the address of its agent for service of process by delivering to the Department of State for filing a statement of change containing:

- (1) the name of the company;
- (2) the street and mailing addresses of its current designated office;
- (3) if the current designated office is to be changed, the street and mailing addresses of the new designated office;
- (4) the name and street and mailing addresses of its current agent for service of process; and
- (5) if the current agent for service of process or an address of the agent is to be changed, the new information.

(b) Subject to Section 205(c), a statement of change is effective when filed by the Department of State.

#### **Comment**

**Source** – ULPA (2001) § 115, which is based on ULLCA § 109.

**Subsection (a)** – This subsection uses “may” rather than “shall” because other avenues exist. A limited liability company may also change the information by amending its certificate of organization, Section 202, or through its annual report. Section 209(e). A foreign limited liability company may use its annual report. Section 209(e). However, neither a limited liability company nor a foreign limited liability company may wait for the annual report if the information described in the public record becomes inaccurate. *See* Sections 207 (imposing liability for false information in record) and 116(b) (providing for substitute service).

#### SECTION 115. RESIGNATION OF AGENT FOR SERVICE OF PROCESS.

(a) To resign as an agent for service of process of a limited liability company or foreign limited liability company, the agent must deliver to the Department of State for filing a statement of resignation containing the company name and stating that the agent is resigning.

(b) The Department of State shall file a statement of resignation delivered under subsection (a) and mail or otherwise provide or deliver a copy to the designated office of the limited liability company or foreign limited liability company and another copy to the principal office of the company if the mailing addresses of the principal office appears in the records of the Department of State and is different from the mailing address of the designated office.

(c) An agency for service of process terminates on the earlier of:

- (1) the 31st day after the Department of State files the statement of resignation;
- (2) when a record designating a new agent for service of process is delivered to the Department of State for filing on behalf of the limited liability company and becomes

effective.

### **Comment**

**Source** – ULPA (2001) § 116, which is based on ULLCA §110.

#### **SECTION 116. SERVICE OF PROCESS.**

(a) An agent for service of process appointed by a limited liability company or foreign limited liability company is an agent of the company for service of any process, notice, or demand required or permitted by law to be served on the company.

(b) If a limited liability company or foreign limited liability company does not appoint or maintain an agent for service of process in this state or the agent for service of process cannot with reasonable diligence be found at the agent's street address, the Department of State is an agent of the company upon whom process, notice, or demand may be served.

(c) Service of any process, notice, or demand on the Department of State as agent for a limited liability company or foreign limited liability company may be made by delivering to the Department of State duplicate copies of the process, notice, or demand. If a process, notice, or demand is served on the Department of State, the Department of State shall forward one of the copies by registered or certified mail, return receipt requested, to the company at its designated office.

(d) Service is effected under subsection (c) at the earliest of:

(1) the date the limited liability company or foreign limited liability company receives the process, notice, or demand;

(2) the date shown on the return receipt, if signed on behalf of the company; or

(3) five days after the process, notice, or demand is deposited with the United States Postal Service, if correctly addressed and with sufficient postage.

(e) The Department of State shall keep a record of each process, notice, and demand served pursuant to this section and record the time of, and the action taken regarding, the service.

(f) This section does not affect the right to serve process, notice, or demand in any other manner provided by law.

### **Comment**

**Source** – ULPA (2001) § 117, which is based on ULLCA §111.

(3) [ARTICLE] 2

(4) FORMATION; CERTIFICATE OF ORGANIZATION AND OTHER FILINGS

SECTION 201. FORMATION OF LIMITED LIABILITY COMPANY; CERTIFICATE OF ORGANIZATION.

(a) One or more persons may act as organizers to form a limited liability company by signing and delivering to the Department of State for filing a certificate of organization.

(b) A certificate of organization must state:

(1) the name of the limited liability company, which must comply with Section 108; and

(2) the street and mailing addresses of the initial designated office and the name and street and mailing addresses of the initial agent for service of process of the company.

(c) Subject to Section 112(c), a certificate of organization may also contain statements as to matters other than those required by subsection (b). However, a statement in a certificate of organization is not effective as a statement of authority.

(d) The following rules apply:

(1) A limited liability company is formed when the Department of State has filed the certificate of organization and the company has at least one member, unless the certificate states a delayed effective date pursuant to Section 205(c).

(2) If the certificate states a delayed effective date, a limited liability company is not formed if, before the certificate takes effect, a statement of cancellation is signed and delivered to the Department of State for filing and the Department of State files the certificate.

(3) Subject to any delayed effective date and except in a proceeding by this state to dissolve a limited liability company, the filing of the certificate of organization by the Department of State is conclusive proof that the organizer satisfied all conditions to the formation of a limited liability company.

(4) Until a limited liability company has or has had at least one member, the company lacks the capacity to do any act or carry on any activity except:

(A) delivering to the Department of State for filing a statement of change under Section 114, an amendment to the certificate of organization under Section 202, a statement of correction under Section 206, an annual report under section 209, and a statement of

termination under Section 702(b)(2)(F);

(B) admitting a member under section 401; and

(C) dissolving under Section 701.

(5) A limited liability company that has or has had at least one member may ratify any act or activity that occurred when the company lacked capacity under subsection (4).

### **Comment**

No topic received more attention or generated more debate in the drafting process for this Act than the question of the “shelf LLC” – i.e., an LLC formed without having at least one member upon formation. Reasonable minds differed (occasionally intensely) as to whether the “shelf” approach (i) is necessary to accommodate current business practices; and (ii) somehow does conceptual violence to the partnership antecedents of the limited liability company.

The 2006 Annual Meeting Draft provided for a “limited shelf” – a shelf that lacked capacity to conduct any substantive activities:

a) Except as otherwise provided in subsection (b), a limited liability company has the capacity to sue and be sued in its own name and the power to do all things necessary or convenient to carry on its activities.

(b) Until a limited liability company has or has had at least one member, the company lacks the capacity to do any act or carry on any activity except:

(1) delivering to the Department of State for filing a statement of change under Sections 114, an amendment to the certificate under Section 202, a statement of correction under Section 206, an annual report under section 209, and a statement of termination under Section 702(b)(2)(F);

(2) admitting a member under section 401; and

(3) dissolving under Section 701.

(c) A limited liability company that has or has had at least one member may ratify an act or activity that occurred when the company lacked capacity under subsection (b).

However, when the Conference considered the 2006 Annual Meeting Draft, the Drafting Committee itself proposed an amendment, and the Conference agreed. A product of intense discussion and compromise with several ABA Advisors, the amendment substituted a double filing and “embryonic certificate” approach. An organizer may deliver for filing a certificate of organization without the company having any members and the filing officer will file the certificate, but:

- the certificate as delivered to the filing officer must acknowledge that situation, Subsection (a)(3);
- the limited liability company is not formed until and unless the organizer timely delivers to the filing officer a notice that the company has at least one member, Subsection (e)(1);

and

- if the organizer does not timely deliver the required notice, the certificate lapses and is void. *Id.*

The Conference recommends a 90-day “window” for filing the notice, which must state “the date on which a person or persons became the company’s initial member or members.” When the filing officer files that notice, the company is deemed formed as of the date stated in the notice. Subsection (e)(2).

Thus under this Act, the delivery to the filing officer of a certificate of organization has different consequences, depending on whether the certificate contains the “no members” statement as provided by subsection (b)(3).

does the certificate contain the “no members” statement under subsection (b)(3)	by delivering the certificate for filing, what is the organizer affirming, per Section 207(c), about members	effect of the filing officer filing the certificate	logical relationship of the filed certificate to the formation of the LLC
<b>no</b>	<b>that the LLC will have at least one member upon formation</b>	<b>LLC is formed, subject to any delayed effective date</b>	<b>necessary and sufficient</b>
<b>yes</b>	<b>that the LLC will have no members when the filing officer files the certificate</b>	<b>the document is part of the public record, protects the name, and starts the 90-day clock ticking</b>	<b>necessary but not sufficient</b>

**Subsection (b)** – This Act does not require the certificate of organization to designate whether the limited liability company is manager-managed or member-managed. Under this Act, those characterizations pertain principally to *inter se* relations, and the Act therefore looks to the operating agreement to make the characterization. *See* Sections 102(10) and (12); 407(a).

**Subsection (d)** – This subsection states the “pathway” through which a limited liability company is formed if the certificate of organization does not contain a statement as provided in subsection (b)(3) – i.e., if the limited liability company will have at least one member when the filing officer files the certificate.

**Subsection (e)** – This subsection states the “pathway” through which a limited liability company is formed if the certificate of organization contains a statement as provided in subsection (b)(3) – i.e., if the limited liability company will not have at least one member when the filing officer files the certificate.

This pathway requires a second filing in order to form the limited liability company: “a notice stating (A) that the limited liability company has at least one member; and (B) the date on which a person or persons became the company’s initial member or members.” Subsection (e)(1).

In this pathway, a certificate of organization may not itself state a delayed effective date, Section 205(c), because:

- the reason to state a delayed effective date in a certificate of organization is to set the date on which the limited liability company is formed, Section 205(c); and
- when a certificate contains a statement as provided in subsection (b)(3), this Act mandates when (if at all) the limited liability company is deemed formed – i.e., “as of the date of initial membership stated in the notice delivered” to the filing officer as the second filing. Subsection (e)(2).

## SECTION 202. AMENDMENT OR RESTATEMENT OF CERTIFICATE OF ORGANIZATION.

(a) A certificate of organization may be amended or restated at any time.

(b) To amend its certificate of organization, a limited liability company must deliver to the Department of State for filing an amendment stating:

- (1) the name of the company;
- (2) the date of filing of its certificate of organization; and
- (3) the changes the amendment makes to the certificate as most recently amended

or restated.

(c) To restate its certificate of organization, a limited liability company must deliver to the Department of State for filing a restatement, designated as such in its heading, stating:

(1) in the heading or an introductory paragraph, the company’s present name and the date of the filing of the company’s initial certificate of organization;

(2) if the company’s name has been changed at any time since the company’s formation, each of the company’s former names; and

(3) the changes the restatement makes to the certificate as most recently amended or restated.

(d) Subject to Sections 112(c) and 205(c), an amendment to or restatement of a certificate of organization is effective when filed by the Department of State.

(e) If a member of a member-managed limited liability company, or a manager of a manager-managed limited liability company, knows that any information in a filed certificate of organization was inaccurate when the certificate was filed or has become inaccurate owing to changed circumstances, the member or manager shall promptly:

(1) cause the certificate to be amended; or

(2) if appropriate, deliver to the Department of State for filing a statement of change under Section 114 or a statement of correction under Section 206.

### **Comment**

**Subsection (e)** – This subsection is taken from ULPA (2001) § 202(c), which imposes the responsibility on general partners. The original ULLCA had no comparable provision.

This subsection imposes an obligation directly on the members and managers rather than on the limited liability company. A member or manager’s failure to meet the obligation exposes the member or manager to liability to third parties under Section 207(a)(2) and might constitute a breach of the member or manager’s duties under Section 409(c) and (g)(1). In addition, an aggrieved person may seek a remedy under Section 204 (Signing and Filing Pursuant to Judicial Order).

Like other provisions of the Act requiring records to be delivered to the filing officer for filing, this section is not subject to change by the operating agreement. *See* Section 110(c)(11) (precluding the operating agreement from “restrict[ing] the rights under this [act] of a person other than a member or manager”).

## **A SECTION 203. SIGNING OF RECORDS TO BE DELIVERED FOR FILING TO DEPARTMENT OF STATE.**

(a) A record delivered to the Department of State for filing pursuant to this [act] must be signed as follows:

(1) Except as otherwise provided in paragraphs (2) through (4), a record signed on behalf of a limited liability company must be signed by a person authorized by the company.

(2) A limited liability company’s initial certificate of organization must be signed by at least one person acting as an organizer.

(3) A record filed on behalf of a dissolved limited liability company that has no members must be signed by the person winding up the company’s activities under Section 702(c) or a person appointed under Section 702(d) to wind up those activities.

(4) A statement of cancellation under Section 201(d)(2) must be signed by each



organizer that signed the initial certificate of organization, but a personal representative of a deceased or incompetent organizer may sign in the place of the decedent or incompetent.

(5) A statement of denial by a person under Section 303 must be signed by that person.

(6) Any other record must be signed by the person on whose behalf the record is delivered to the Department of State.

(b) Any record filed under this [act] may be signed by an agent.

#### **Comment**

**Subsection (b)** – This subsection does not require that the agent’s authority be memorialized in a writing or other record. However, a person signing as an agent “thereby affirms under penalties of perjury that [the assertion of agent status is] . . . accurate.” Section 207(c).

#### **SECTION 204. SIGNING AND FILING PURSUANT TO JUDICIAL ORDER.**

(a) If a person required by this [act] to sign a record or deliver a record to the Department of State for filing under [this act] does not do so, any other person that is aggrieved may petition the [appropriate court] to order:

- (1) the person to sign the record;
- (2) the person to deliver the record to the Department of State for filing; or
- (3) the Department of State to file the record unsigned.

(b) If a petitioner under subsection (a) is not the limited liability company or foreign limited liability company to which the record pertains, the petitioner shall make the company a party to the action.

#### **Comment**

**Source** – ULPA (2001) § 205, which is based on RULPA § 205, which was the source of ULLCA § 210.

**Subsection (a)(3)** – A record filed under this paragraph is effective without being signed.

#### **SECTION 205. DELIVERY TO AND FILING OF RECORDS BY DEPARTMENT OF STATE; EFFECTIVE TIME AND DATE.**

(a) A record authorized or required to be delivered to the Department of State for filing under this [act] must be captioned to describe the record’s purpose, be in a medium permitted by the Department of State, and be delivered to the Department of State. If the filing fees have been

paid, unless the Department of State determines that a record does not comply with the filing requirements of this [act], the Department of State shall file the record and:

(1) for a statement of denial under Section 303, send a copy of the filed statement and a receipt for the fees to the person on whose behalf the statement was delivered for filing and to the limited liability company; and

(2) for all other records, send a copy of the filed record and a receipt for the fees to the person on whose behalf the record was filed.

(b) Upon request and payment of the requisite fee, the Department of State shall send to the requester a certified copy of a requested record.

(c) Except as otherwise provided in Sections 115 and 206, a record delivered to the Department of State for filing under this [act] may specify an effective time and a delayed effective date. Subject to Sections 115, 201(d)(1), and 206, a record filed by the Department of State is effective:

(1) if the record does not specify either an effective time or a delayed effective date, on the date and at the time the record is filed as evidenced by the Department of State's endorsement of the date and time on the record;

(2) if the record specifies an effective time but not a delayed effective date, on the date the record is filed at the time specified in the record;

(3) if the record specifies a delayed effective date but not an effective time, at 12:01 a.m. on the earlier of:

(A) the specified date; or

(B) the 90th day after the record is filed; or

(4) if the record specifies an effective time and a delayed effective date, at the specified time on the earlier of:

(A) the specified date; or

(B) the 90th day after the record is filed.

### **Comment**

**Source** – ULPA (2001) § 206, which was based on ULLCA §206.

This Act uses the concept of “filing” to refer to the official act of the Department of State, which is typically preceded by a person “delivering” some record “to the Department of State for filing.”

**Subsection (c)(3)(B) and 4(B)** – If a person delivers to the Secretary of State for filing a record that contains an over-long delay in the effective date, the Secretary of State: (i) will not reject the record; and (ii) is neither required nor authorized to inform the person that this Act will truncate the period of delay specified in the record.

#### SECTION 206. CORRECTING FILED RECORD.

(a) A limited liability company or foreign limited liability company may deliver to the Department of State for filing a statement of correction to correct a record previously delivered by the company to the Department of State and filed by the Department of State, if at the time of filing the record contained inaccurate information or was defectively signed.

(b) A statement of correction under subsection (a) may not state a delayed effective date and must:

(1) describe the record to be corrected, including its filing date, or attach a copy of the record as filed;

(2) specify the inaccurate information and the reason it is inaccurate or the manner in which the signing was defective; and

(3) correct the defective signature or inaccurate information.

(c) When filed by the Department of State, a statement of correction under subsection (a) is effective retroactively as of the effective date of the record the statement corrects, but the statement is effective when filed:

(1) for the purposes of Section 103(d); and

(2) as to persons that previously relied on the uncorrected record and would be adversely affected by the retroactive effect.

#### Comment

**Source** – ULPA (2001) § 207, which was based on ULLCA §207.

#### SECTION 207. LIABILITY FOR INACCURATE INFORMATION IN FILED RECORD.

(a) If a record delivered to the Department of State for filing under this [act] and filed by the Department of State contains inaccurate information, a person that suffers a loss by reliance on the information may recover damages for the loss from:

(1) a person that signed the record, or caused another to sign it on the person's

behalf, and knew the information to be inaccurate at the time the record was signed; and

(2) subject to subsection (b), a member of a member-managed limited liability company or the manager of a manager-managed limited liability company, if:

(A) the record was delivered for filing on behalf of the company; and

(B) the member or manager had notice of the inaccuracy for a reasonably sufficient time before the information was relied upon so that, before the reliance, the member or manager reasonably could have:

(i) effected an amendment under Section 202;

(ii) filed a petition under Section 204; or

(iii) delivered to the Department of State for filing a statement of change under Section 114 or a statement of correction under Section 206.

(b) To the extent that the operating agreement of a member-managed limited liability company expressly relieves a member of responsibility for maintaining the accuracy of information contained in records delivered on behalf of the company to the Department of State for filing under this [act] and imposes that responsibility on one or more other members, the liability stated in subsection (a)(2) applies to those other members and not to the member that the operating agreement relieves of the responsibility.

(c) An individual who signs a record authorized or required to be filed under this [act] affirms under penalty of perjury that the information stated in the record is accurate.

### **Comment**

Source: ULPA (2001) § 208, which expanded on ULLCA § 209.

**Section (a)(2)(B)** – This subparagraph implies that doing any of the acts listed in clauses (i) through (iii) will preclude liability arising from subsequent reliance. In this connection, Clause (a)(2)(B)(ii) warrants special attention, because that act (filing a petition in court) can occur without any immediate effect on the records relevant to a limited liability company maintained by the filing officer. The other clauses refer to acts that (assuming no filing backlog) affect that public record immediately.

### **SECTION 208. CERTIFICATE OF EXISTENCE OR AUTHORIZATION.**

(a) The Department of State, upon request and payment of the requisite fee, shall furnish to any person a certificate of existence for a limited liability company if the records filed with the Department of State show that the company has been formed under Section 201 and the Department of State has not filed a statement of termination pertaining to the company. A

certificate of existence must state:

- (1) the company's name;
  - (2) that the company was duly formed under the laws of this state and the date of formation;
  - (3) whether all fees, taxes, and penalties due under this [act] or other law to the Department of State have been paid;
  - (4) whether the company's most recent annual report required by Section 209 has been filed by the Department of State;
  - (5) whether the Department of State has administratively dissolved the company;
  - (6) whether the company has delivered to the Department of State for filing a statement of dissolution;
  - (7) that a statement of termination has not been filed by the Department of State;
- and
- (8) other facts of record in the office of the Department of State which are specified by the person requesting the certificate.

(b) The Department of State, upon request and payment of the requisite fee, shall furnish to any person a certificate of authorization for a foreign limited liability company if the records filed with the Department of State show that the Department of State has filed a certificate of authority, has not revoked the certificate of authority, and has not filed a notice of cancellation.

A certificate of authorization must state:

- (1) the company's name and any alternate name adopted under Section 805(a) for use in this state;
- (2) that the company is authorized to transact business in this state;
- (3) whether all fees, taxes, and penalties due under this [act] or other law to the Department of State have been paid;
- (4) whether the company's most recent annual report required by Section 209 has been filed by the Department of State;
- (5) that the Department of State has not revoked the company's certificate of authority and has not filed a notice of cancellation; and
- (6) other facts of record in the office of the Department of State which are specified by the person requesting the certificate.

(c) Subject to any qualification stated in the certificate, a certificate of existence or certificate of authorization issued by the Department of State is conclusive evidence that the limited liability company is in existence or the foreign limited liability company is authorized to transact business in this state.

### **Comment**

**Source** – ULPA (2001), § 209, which was based on ULLCA, § 208.

The information provided in a certificate of existence or authorization is, of course, current only as of the date of the certificate.

### **B SECTION 209. ANNUAL REPORT FOR DEPARTMENT OF STATE.**

(a) Each year, a limited liability company or a foreign limited liability company authorized to transact business in this state shall deliver to the Department of State for filing a report that states:

- (1) the name of the company;
- (2) the street and mailing addresses of the company's designated office and the name and street and mailing addresses of its agent for service of process in this state;
- (3) the street and mailing addresses of its principal office; and
- (4) in the case of a foreign limited liability company, the state or other jurisdiction under whose law the company is formed and any alternate name adopted under Section 805(a).

(b) Information in an annual report under this section must be current as of the date the report is delivered to the Department of State for filing.

(c) The first annual report under this section must be delivered to the Department of State between [January 1 and April 1] of the year following the calendar year in which a limited liability company was formed or a foreign limited liability company was authorized to transact business. A report must be delivered to the Department of State between [January 1 and April 1] of each subsequent calendar year.

(d) If an annual report under this section does not contain the information required in subsection (a), the Department of State shall promptly notify the reporting limited liability company or foreign limited liability company and return the report to it for correction. If the report is corrected to contain the information required in subsection (a) and delivered to the Department of State within 30 days after the effective date of the notice, it is timely delivered.

(e) If an annual report under this section contains an address of a designated office or the name or address of an agent for service of process which differs from the information shown in the records of the Department of State immediately before the annual report becomes effective, the differing information in the annual report is considered a statement of change under Section 114.

### **Comment**

**Source** – ULPA (2001) § 210, which was based on ULLCA § 211.

A limited liability company that fails to comply with this section is subject to administrative dissolution. Section 705(a)(2). A foreign limited liability company that fails to comply with this section is subject to having its certificate of authority revoked. Section 806(a)(2).

(5) [ARTICLE] 3

(6) RELATIONS OF MEMBERS AND MANAGERS

(7) TO PERSONS DEALING WITH LIMITED LIABILITY COMPANY

**SECTION 301. NO AGENCY POWER OF MEMBER AS MEMBER.**

(a) A member is not an agent of a limited liability company solely by reason of being a member.

(b) A person's status as a member does not prevent or restrict law other than this [act] from imposing liability on a limited liability company because of the person's conduct.

**Comment**

**Subsection (a)** – Most LLC statutes, including the original ULLCA, provide for what might be termed “statutory apparent authority” for members in a member-managed limited liability company and managers in a manager-managed limited liability company. This approach codifies the common law notion of apparent authority by position and dates back at least to the original, 1914 Uniform Partnership Act. UPA, § 9 provided that “the act of every partner ... for apparently carrying on in the usual way the business of the partnership ... binds the partnership,” and that formulation has been essentially followed by RUPA, § 301, ULLCA, § 301, ULPA (2001), § 402, and myriad state LLC statutes.

This Act rejects the statutory apparent authority approach, for reasons summarized in a “Progress Report on the Revised Uniform Limited Liability Company Act,” published in the March 2006 issue of the newsletter of the ABA Committee on Partnerships and Unincorporated Business Organizations:

The concept [of statutory apparent authority] still makes sense both for general and limited partnerships. A third party dealing with either type of partnership can know by the formal name of the entity and by a person's status as general or limited partner whether the person has the power to bind the entity.

Most LLC statutes have attempted to use the same approach but with a fundamentally important (and problematic) distinction. An LLC's status as member-managed or manager-managed determines whether members or managers have the statutory power to bind. But an LLC's status as member- or manager-managed is not apparent from the LLC's name. A third party must check the public record, which may reveal that the LLC is manager-managed, which in turn means a member as member has no power to bind the LLC. As a result, a provision that originated in 1914 as a protection for third parties can, in the LLC context, easily function as a trap for the unwary. The problem is exacerbated by the almost infinite variety of management structures permissible in and used by



LLCs.

The new Act cuts through this problem by simply eliminating statutory apparent authority.

PUBOGRAM, Vol. XXIII, no. 2 at 9-10.

Codifying power to bind according to position makes sense only for organizations that have well-defined, well-known, and almost paradigmatic management structures. Because:

- flexibility of management structure is a hallmark of the limited liability company; and
- an LLC's name gives no signal as to the organization's structure,

it makes no sense to:

- require each LLC to publicly select between two statutorily preordained structures (i.e., manager-managed/member-managed); and then
- link a "statutory power to bind" to each of those two structures.

Under this Act, other law – most especially the law of agency – will handle power-to-bind questions. See the Comment to subsection (b).

This subsection does not address the power to bind of a manager in a manager-managed LLC, although this Act does consider a manager's management responsibilities. See Section 407(c) (allocating management authority, subject to the operating agreement). For a discussion of how agency law will approach the actual and apparent authority of managers, see Section 407(c), cmt.

**Subsection (b)** – As the "flip side" to subsection (a), this subsection expressly preserves the power of other law to hold an LLC directly or vicariously liable on account of conduct by a person who happens to be a member. For example, given the proper set of circumstances: (i) a member might have actual or apparent authority to bind an LLC to a contract; (ii) the doctrine of *respondeat superior* might make an LLC liable for the tortious conduct of a member (i.e., in some circumstances a member acts as a "servant" of the LLC); and (iii) an LLC might be liable for negligently supervising a member who is acting on behalf of the LLC. A person's status as a member does not weigh against these or any other relevant theories of law.

Moreover, subsection (a) does not prevent member status from being relevant to one or more elements of an "other law" theory. The most categorical example concerns the authority of a non-manager member of a manager-managed LLC.

**EXAMPLE:** A vendor knows that an LLC is manager-managed but chooses to accept the signature of a person whom the vendor knows is merely a member of the LLC. Assuring the vendor that the LLC will stand by the member's commitment, the member states, "It's such a simple matter; no one will mind." The member genuinely believes the statement, and the vendor accepts the assurance.

The person's status as a mere member will undermine a claim of apparent authority. RESTATEMENT (THIRD) OF AGENCY § 2.03, cmt. d (2006) (explaining the "reasonable belief" element of a claim of apparent authority, and role played by context, custom, and the supposed agent's position in an organization). Likewise, the member will have no actual authority. Absent additional facts, section 407(c)(1) (vesting all management authority in the managers) renders the member's belief unreasonable. RESTATEMENT (THIRD) OF AGENCY § 2.01, cmt. c (2006) (explaining the "reasonable belief" element of a claim of actual authority).

In general, a member's actual authority to act for an LLC will depend fundamentally on the operating agreement.

EXAMPLE: Rachael and Sam, who have known each other for years, decide to go into business arranging musical tours. They fill out and electronically sign a one page form available on the website of the Secretary of State and become the organizers of MMT, LLC. They are the only members of the LLC, and their understanding of who will do what in managing the enterprise is based on several lengthy, late-night conversations that preceded the LLC's formation. Sam is to "get the acts," and Rachael is to manage the tour logistics. There is no written operating agreement.

In the terminology of this Act, MMT, LLC is member-managed, Section 407(a), and the understanding reached in the late night conversations has become part of the LLC's operating agreement. Section 111(c). In agency law terms, the operating agreement constitutes a manifestation by the LLC to Rachael and Sam concerning the scope of their respective authority to act on behalf of the LLC. RESTATEMENT (THIRD) OF AGENCY § 2.01, cmt. c (2006) (explaining that a person's actual authority depends first on some manifestation attributable to the principal and stating: "Actual authority is a consequence of a principal's expressive conduct toward an agent, through which the principal manifests assent to be affected by the agent's action, and the agent's reasonable understanding of the principal's manifestation.")

Circumstances outside the operating agreement can also be relevant to determining the scope of a member's actual authority.

EXAMPLE: Homeworks, LLC is a manager-managed LLC with three members. The LLC's written operating agreement:

- specifies in considerable detail the management responsibilities of Margaret, the LLC's manager-member, and also states that Margaret is responsible for "the day-to-day operations" of the company;
- puts Garrett, a non-manager member, in charge of the LLC's transportation department; and
- specifies no management role for Brooksley, the third member.

When the LLC's chief financial officer quits suddenly, Margaret asks Brooksley, a CPA, to "step in until we can hire a replacement."

Under the operating agreement, Margaret's request to Brooksley is within Margaret's actual authority and is a manifestation attributable to the LLC. If Brooksley manifests assent to Margaret's request, Brooksley will have the actual authority to act as the LLC's CFO.

In the unlikely event that two or more people form a member-managed LLC without any understanding of how to allocate management responsibility between or among them, agency law, operating in the context the Act's "gap fillers" on management responsibility, will produce the following result:

A single member of a multi-member, member-managed LLC:

- has no actual authority to commit the LLC to any matter "outside the ordinary course of the activities of the company," section 407(b)(3); and
- has the actual authority to commit the LLC to any matter "in the ordinary course of the activities of the company," section 407(b)(2), unless the member has reason to know that other members might disagree or the member has some other reason to know that consultation with fellow members is appropriate.

For an explanation of this result, see Section 407(c), cmt., which provides a detailed agency law analysis in the context of a multi-manager, manager-managed LLC whose operating agreement is silent on the analogous question.

The common law of agency will also determine the apparent authority of a member of a member-managed LLC, and in that analysis what the particular third party knows or has reason to know about the management structure and business practices of the particular LLC will always be relevant. RESTATEMENT (THIRD) OF AGENCY § 3.03, cmt. b (2006) ("A principal may also make a manifestation by placing an agent in a defined position in an organization .... Third parties who interact with the principal through the agent will naturally and reasonably assume that the agent has authority to do acts consistent with the agent's position ... unless they have notice of facts suggesting that this may not be so.")

Under section 301(a), however, the mere fact that a person is a member of a member-managed limited liability company cannot *by itself* establish apparent authority by position. A course of dealing, however, may easily change the analysis:

EXAMPLE: David is a one of two members of DS, LLC, a member-managed LLC. David orders paper clips on behalf of the LLC, signing the purchase agreement, "David, as a member of DS, LLC." The vendor accepts the order, sends an invoice to the LLC's address, and in due course receives a check drawn on the LLC's bank account. When David next places an order with the vendor, the LLC's payment of the first order is a manifestation that the vendor may use in establishing David's apparent authority to place the second order.

SECTION 302. STATEMENT OF AUTHORITY.

(a) A limited liability company may deliver to the Department of State for filing a statement of authority. The statement:

(1) must include the name of the company and the street and mailing addresses of its designated office;

(2) with respect to any position that exists in or with respect to the company, may state the authority, or limitations on the authority, of all persons holding the position to:

(A) execute an instrument transferring real property held in the name of the company; or

(B) enter into other transactions on behalf of, or otherwise act for or bind, the company; and

(3) may state the authority, or limitations on the authority, of a specific person to:

(A) execute an instrument transferring real property held in the name of the company; or

(B) enter into other transactions on behalf of, or otherwise act for or bind, the company.

(b) To amend or cancel a statement of authority filed by the Department of State under Section 205(a), a limited liability company must deliver to the Department of State for filing an amendment or cancellation stating:

(1) the name of the company;

(2) the street and mailing addresses of the company's designated office;

(3) the caption of the statement being amended or canceled and the date the statement being affected became effective; and

(4) the contents of the amendment or a declaration that the statement being affected is canceled.

(c) A statement of authority affects only the power of a person to bind a limited liability company to persons that are not members.

(d) Subject to subsection (c) and Section 103(d) and except as otherwise provided in subsections (f), (g), and (h), a limitation on the authority of a person or a position contained in an effective statement of authority is not by itself evidence of knowledge or notice of the limitation by any person.

(e) Subject to subsection (c), a grant of authority not pertaining to transfers of real property and contained in an effective statement of authority is conclusive in favor of a person that gives value in reliance on the grant, except to the extent that when the person gives value:

- (1) the person has knowledge to the contrary;
- (2) the statement has been canceled or restrictively amended under subsection (b);

or

(3) a limitation on the grant is contained in another statement of authority that became effective after the statement containing the grant became effective.

(f) Subject to subsection (c), an effective statement of authority that grants authority to transfer real property held in the name of the limited liability company and that is recorded by certified copy in the office for recording transfers of the real property is conclusive in favor of a person that gives value in reliance on the grant without knowledge to the contrary, except to the extent that when the person gives value:

(1) the statement has been canceled or restrictively amended under subsection (b) and a certified copy of the cancellation or restrictive amendment has been recorded in the office for recording transfers of the real property; or

(2) a limitation on the grant is contained in another statement of authority that became effective after the statement containing the grant became effective and a certified copy of the later-effective statement is recorded in the office for recording transfers of the real property.

(g) Subject to subsection (c), if a certified copy of an effective statement containing a limitation on the authority to transfer real property held in the name of a limited liability company is recorded in the office for recording transfers of that real property, all persons are deemed to know of the limitation.

(h) Subject to subsection (i), an effective statement of dissolution or termination is a cancellation of any filed statement of authority for the purposes of subsection (f) and is a limitation on authority for the purposes of subsection (g).

(i) After a statement of dissolution becomes effective, a limited liability company may deliver to the Department of State for filing and, if appropriate, may record a statement of authority that is designated as a post-dissolution statement of authority. The statement operates as provided in subsections (f) and (g).

(j) Unless earlier canceled, an effective statement of authority is canceled by operation of

law five years after the date on which the statement, or its most recent amendment, becomes effective. This cancellation operates without need for any recording under subsection (f) or (g).

(k) An effective statement of denial operates as a restrictive amendment under this section and may be recorded by certified copy for the purposes of subsection (f)(1).

### Comment

This section is derived from and builds on RUPA, § 303, and, like that provision is conceptually divided into two realms: statements pertaining to the power to transfer interests in the LLC's real property and statements pertaining to other matters. In the latter realm, statements are filed only in the records of the Department of State, operate only to the extent the statements are actually known. Section 302(d) and (e).

As to interests in real property, in contrast, this section: (i) requires double-filing – with the Department of State and in the appropriate land records; and (ii) provides for constructive knowledge of statements limiting authority. Thus, a properly filed and recorded statement can protect the limited liability company, Section 302(g), and, in order for a statement pertaining to real property to be a sword in the hands of a third party, the statement must have been both filed and properly recorded. Section 302(f).

**Subsection (a)(2)** – This paragraph permits a statement to designate authority by position (or office) rather than by specific person. This type of a statement will enable LLCs to provide evidence of ongoing authority to enter into transactions without having to disclose to third parties the entirety of the operating agreement.

Here and elsewhere in the section, the phrase “real property” includes interests in real property, such as mortgages, easements, etc.

**Subsection (b)** – For the requirement that the original statement, like any other record, be appropriately captioned, see Section 205(a).

**Subsection (c)** – This subsection contains a very important limitation – i.e., that this section's rules do not operate *viz a viz* members. The text of RUPA, § 303 makes this very important point only obliquely, but the Comment to that section is unequivocal:

It should be emphasized that Section 303 concerns the authority of partners to bind the partnership to third persons. As among the partners, the authority of a partner to take any action is governed by the partnership agreement, or by the provisions of RUPA governing the relations among partners, and is not affected by the filing or recording of a statement of partnership authority.

RUPA § 303, comment 4.

However, like any other record delivered for filing on behalf of an LLC, a statement of authority might be some evidence of the contents of the operating agreement. *See* Comment to

Section 112(d).

**Subsection (d)** - The phrase “by itself” is important, because the existence of a limitation could be evidence if, for example, the person in question reviewed the public record at a time when the limitation was of record.

**Subsection (e)(1)** – What happens if a statement of authority conflicts with the contents of an LLC’s certificate of organization? The contents of the certificate are not statements of authority, Section 201(c), so the information in the certificate does not directly figure into the operation of this section. However, if the person claiming to rely on a statement of authority had read the certificate’s conflicting information before giving value, that fact might be evidence that person gave value with “knowledge to the contrary” of the statement.

**SECTION 303. STATEMENT OF DENIAL.** A person named in a filed statement of authority granting that person authority may deliver to the Department of State for filing a statement of denial that:

- (1) provides the name of the limited liability company and the caption of the statement of authority to which the statement of denial pertains; and
- (2) denies the grant of authority.

#### **Comment**

For the effect of a statement of denial, see Section 302(k).

#### **SECTION 304. LIABILITY OF MEMBERS AND MANAGERS.**

(a) The debts, obligations, or other liabilities of a limited liability company, whether arising in contract, tort, or otherwise:

- (1) are solely the debts, obligations, or other liabilities of the company; and
- (2) do not become the debts, obligations, or other liabilities of a member or manager solely by reason of the member acting as a member or manager acting as a manager.

(b) The failure of a limited liability company to observe any particular formalities relating to the exercise of its powers or management of its activities is not a ground for imposing liability on the members or managers for the debts, obligations, or other liabilities of the company.

#### **Comment**

**Subsection (a)(2)** – This paragraph shields members and managers only against the debts, obligations and liabilities of the limited liability company and is irrelevant to claims seeking to hold a member or manager directly liable on account of the member’s or manager’s

own conduct.

EXAMPLE: A manager personally guarantees a debt of a limited liability company. Subsection (a)(2) is irrelevant to the manager's liability as guarantor.

EXAMPLE: A member purports to bind a limited liability company while lacking any agency law power to do so. The limited liability company is not bound, but the member is liable for having breached the "warranty of authority" (an agency law doctrine). Subsection (a)(2) does not apply. The liability is not *for* a "debt[], obligation[], [or] liability[]" of a limited liability company," but rather is the member's direct liability resulting because the limited liability company is *not* indebted, obligated or liable.

RESTATEMENT (THIRD) OF AGENCY § 6.10 (2006).

EXAMPLE: A manager of a limited liability company defames a third party in circumstances that render the limited liability company vicariously liable under agency law. Under subsection (a)(2), the third party cannot hold the manager accountable for the *company's* liability, but that protection is immaterial. The manager is the tortfeasor and in that role is directly liable to the third party.

Subsection (a)(2) pertains only to claims by third parties and is irrelevant to claims by a limited liability company against a member or manager and *vice versa*. See e.g. Sections 408 (pertaining to a limited liability company's obligation to indemnify a member or manager), 409 (pertaining to management duties) and 901 (pertaining to a member's rights to bring a direct claim against a limited liability company).

**Subsection (b)** – This subsection pertains to the equitable doctrine of "piercing the veil" – i.e., conflating an entity and its owners to hold one liable for the obligations of the other. The doctrine of "piercing the corporate veil" is well-established, and courts regularly (and sometimes almost reflexively) apply that doctrine to limited liability companies. In the corporate realm, "disregard of corporate formalities" is a key factor in the piercing analysis. In the realm of LLCs, that factor is inappropriate, because informality of organization and operation is both common and desired.

This subsection does not preclude consideration of another key piercing factor – disregard by an entity's owners of the entity's economic separateness from the owners.

EXAMPLE: The operating agreement of a three-member, member-managed limited liability company requires formal monthly meetings of the members. Each of the members works in the LLC's business, and they consult each other regularly. They have forgotten or ignore the requirement of monthly meetings. Under subsection (b), that fact is irrelevant to a piercing claim.

EXAMPLE: The sole owner of a limited liability company uses a car titled in the company's name for personal purposes and writes checks on the company's account to pay for personal expenses. These facts are relevant to a piercing claim; they pertain to economic separateness, not subsection (b) formalities.



This subsection has no relevance to a member's claim of oppression under Section 701(a)(5)(B). In some circumstances, disregard of agreed-upon formalities can be a "freeze out" mechanism. Likewise, this section has no relevance to a member's claim that the disregard of agreed-upon formalities is a breach of the operating agreement.

Provisions of regulatory law may impose liability by status on a member or manager. *See* CARTER G. BISHOP AND DANIEL S. KLEINBERGER, LIMITED LIABILITY COMPANIES: TAX AND BUSINESS LAW, ¶ 6.04(4) (Statutory Liability).

- (8) [ARTICLE] 4
- (9) RELATIONS OF MEMBERS TO EACH OTHER AND
- (10) TO LIMITED LIABILITY COMPANY

**SECTION 401. BECOMING MEMBER.**

(a) If a limited liability company is to have only one member upon formation, the person becomes a member as agreed by that person and the organizer of the company. That person and the organizer may be, but need not be, different persons. If different, the organizer acts on behalf of the initial member.

(b) If a limited liability company is to have more than one member upon formation, those persons become members as agreed by the persons before the formation of the company. The organizer acts on behalf of the persons in forming the company and may be, but need not be, one of the persons.

(c) If a limited liability company has no members when the certificate of organization is filed with the Department of State, a person becomes an initial member of the limited liability company with the consent of a majority of the organizers. The organizers may consent to more than one person simultaneously becoming the company's initial members.

(d) After formation of a limited liability company, a person becomes a member:

- (1) as provided in the operating agreement;
- (2) as the result of a transaction effective under [Article] 10;
- (3) with the consent of all the members; or
- (4) if, within 90 consecutive days after the company ceases to have any members:

(A) the last person to have been a member, or the legal representative of that person, designates a person to become a member; and

(B) the designated person consents to become a member.

(e) A person may become a member without acquiring a transferable interest and without making or being obligated to make a contribution to the limited liability company.

**Comment**

Most LLC statutes address in separate provisions: (i) how an LLC obtains its initial member or members; and (ii) how additional persons might later become members. This Act

follows that approach. Subsections (a) and (b) address the most common circumstances under which a limited liability company is formed – with one or more persons becoming members upon formation. Subsection (c) addresses how a person becomes the initial member of an LLC whose certificate of organization was filed without there being any members. Subsection (d) addresses how persons become members after an LLC has had at least one member.

For a discussion of the concept of a “shelf LLC” and this Act’s requirement that a limited liability company have at least one member upon formation, see the Comment to Section 201.

**Subsection (d)(4)** – The personal representative of the last member may designate her-, him-, or itself as the new member.

**Subsection (e)** – To accommodate business practices and also because a limited liability company need not have a business purpose, this subsection permits so-called “non-economic members.”

**SECTION 402. FORM OF CONTRIBUTION.** A contribution may consist of tangible or intangible property or other benefit to a limited liability company, including money, services performed, promissory notes, other agreements to contribute money or property, and contracts for services to be performed.

#### **Comment**

**Source** – ULPA (2001) § 501, which derived from ULLCA § 401.

#### **SECTION 403. LIABILITY FOR CONTRIBUTIONS.**

(a) A person’s obligation to make a contribution to a limited liability company is not excused by the person’s death, disability, or other inability to perform personally. If a person does not make a required contribution, the person or the person’s estate is obligated to contribute money equal to the value of the part of the contribution which has not been made, at the option of the company.

(b) A creditor of a limited liability company which extends credit or otherwise acts in reliance on an obligation described in subsection (a) may enforce the obligation.

#### **Comment**

**Source:** ULLCA § 402, which is taken from RULPA § 502(b), which also gave rise to ULPA (2001) § 502.

**Subsection (a)** – The reference to “perform personally” is not limited to individuals but rather may refer to any legal person (including an entity) that has a non-delegable duty.

SECTION 404. SHARING OF AND RIGHT TO DISTRIBUTIONS BEFORE DISSOLUTION.

(a) Any distributions made by a limited liability company before its dissolution and winding up must be in equal shares among members and dissociated members, except to the extent necessary to comply with any transfer effective under Section 502 and any charging order in effect under Section 503.

(b) A person has a right to a distribution before the dissolution and winding up of a limited liability company only if the company decides to make an interim distribution. A person's dissociation does not entitle the person to a distribution.

(c) A person does not have a right to demand or receive a distribution from a limited liability company in any form other than money. Except as otherwise provided in Section 708(c), a limited liability company may distribute an asset in kind if each part of the asset is fungible with each other part and each person receives a percentage of the asset equal in value to the person's share of distributions.

(d) If a member or transferee becomes entitled to receive a distribution, the member or transferee has the status of, and is entitled to all remedies available to, a creditor of the limited liability company with respect to the distribution.

**Comment**

This Act follows both the original ULLCA and ULPA (2001) in omitting any default rule for allocation of losses. The Comment to ULPA (2001), § 503 explains that omission as follows:

This Act has no provision allocating profits and losses among the partners. Instead, the Act directly apportions the right to receive distributions. Nearly all limited partnerships will choose to allocate profits and losses in order to comply with applicable tax, accounting and other regulatory requirements. Those requirements, rather than this Act, are the proper source of guidance for that profit and loss allocation.

**Subsection (b)** – The second sentence of this subsection accords with Section 603(a)(3) – upon dissociation a person is treated as a mere transferee of its own transferable interest. Like most *inter se* rules in this Act, this one is subject to the operating agreement. *See* Comment to Section 603(a)(3).

SECTION 405. LIMITATIONS ON DISTRIBUTION.

(a) A limited liability company may not make a distribution if after the distribution:

(1) the company would not be able to pay its debts as they become due in the ordinary course of the company's activities; or

(2) the company's total assets would be less than the sum of its total liabilities plus the amount that would be needed, if the company were to be dissolved, wound up, and terminated at the time of the distribution, to satisfy the preferential rights upon dissolution, winding up, and termination of members whose preferential rights are superior to those of persons receiving the distribution.

(b) A limited liability company may base a determination that a distribution is not prohibited under subsection (a) on financial statements prepared on the basis of accounting practices and principles that are reasonable in the circumstances or on a fair valuation or other method that is reasonable under the circumstances.

(c) Except as otherwise provided in subsection (f), the effect of a distribution under subsection (a) is measured:

(1) in the case of a distribution by purchase, redemption, or other acquisition of a transferable interest in the company, as of the date money or other property is transferred or debt incurred by the company; and

(2) in all other cases, as of the date:

(A) the distribution is authorized, if the payment occurs within 120 days after that date; or

(B) the payment is made, if the payment occurs more than 120 days after the distribution is authorized.

(d) A limited liability company's indebtedness to a member incurred by reason of a distribution made in accordance with this section is at parity with the company's indebtedness to its general, unsecured creditors.

(e) A limited liability company's indebtedness, including indebtedness issued in connection with or as part of a distribution, is not a liability for purposes of subsection (a) if the terms of the indebtedness provide that payment of principal and interest are made only to the extent that a distribution could be made to members under this section.

(f) If indebtedness is issued as a distribution, each payment of principal or interest on the indebtedness is treated as a distribution, the effect of which is measured on the date the payment

is made.

(g) In subsection (a), “distribution” does not include amounts constituting reasonable compensation for present or past services or reasonable payments made in the ordinary course of business under a bona fide retirement plan or other benefits program.

#### **Comment**

**Source** – ULPA (2001) § 508, which was derived from ULLCA § 406, which was in turn derived from MBCA § 6.40.

**Subsection (b)** – This subsection appears to involve a pure standard of ordinary care, in contrast with the more complicated approach stated in Section 409(c).

**Subsection (g)** – This exception applies only for the purposes of this section. *See* the Comment to Section 503(b)(2). The exception is derived from existing statutory provisions. *See, e.g.,* DEL. CODE ANN., tit. 6, § 18-607(a) (2006) and VA. CODE ANN. § 13.1-1035(E) (West 2006). *See also In re Tri-River Trading, LLC*, 329 B.R. 252, 266, (8th Cir. BAP 2005), *aff’d*, 452 F.3d 756 (8th Cir. 2006) (“We know of no principle of law which suggests that a manager of a company is required to give up agreed upon salary to pay creditors when business turns bad.”)

#### **SECTION 406. LIABILITY FOR IMPROPER DISTRIBUTIONS.**

(a) Except as otherwise provided in subsection (b), if a member of a member-managed limited liability company or manager of a manager-managed limited liability company consents to a distribution made in violation of Section 405 and in consenting to the distribution fails to comply with Section 409, the member or manager is personally liable to the company for the amount of the distribution that exceeds the amount that could have been distributed without the violation of Section 405.

(b) To the extent the operating agreement of a member-managed limited liability company expressly relieves a member of the authority and responsibility to consent to distributions and imposes that authority and responsibility on one or more other members, the liability stated in subsection (a) applies to the other members and not the member that the operating agreement relieves of authority and responsibility.

(c) A person that receives a distribution knowing that the distribution to that person was made in violation of Section 405 is personally liable to the limited liability company but only to the extent that the distribution received by the person exceeded the amount that could have been properly paid under Section 405.

(d) A person against which an action is commenced because the person is liable under

subsection (a) may:

(1) implead any other person that is subject to liability under subsection (a) and seek to compel contribution from the person; and

(2) implead any person that received a distribution in violation of subsection (c) and seek to compel contribution from the person in the amount the person received in violation of subsection (c).

(e) An action under this section is barred if not commenced within two years after the distribution.

### **Comment**

**Source** – Same derivation as Section 405.

Liability under this section is not affected by a person ceasing to be a member, manager or transferee after the time that the liability attaches.

**Subsection (b)** – The operating agreement could not accomplish the “switch” in liability provided by this subsection, because the “switch” implicates the rights of third parties under this Act. Section 110(c)(11).

**Subsections (c) and (d)(2)** – Liability could apply to a person who receives a distribution under a charging order, but only if the person meets the knowledge requirement. That situation is very unlikely unless the person with the charging order is also a member or manager.

### **SECTION 407. MANAGEMENT OF LIMITED LIABILITY COMPANY.**

(a) A limited liability company is a member-managed limited liability company unless the operating agreement:

(1) expressly provides that:

(A) the company is or will be “manager-managed”;

(B) the company is or will be “managed by managers”; or

(C) management of the company is or will be “vested in managers”; or

(2) includes words of similar import.

(b) In a member-managed limited liability company, the following rules apply:

(1) The management and conduct of the company are vested in the members.

(2) Each member has equal rights in the management and conduct of the company’s activities.

(3) A difference arising among members as to a matter in the ordinary course of

the activities of the company may be decided by a majority of the members.

(4) An act outside the ordinary course of the activities of the company may be undertaken only with the consent of all members.

(5) The operating agreement may be amended only with the consent of all members.

(c) In a manager-managed limited liability company, the following rules apply:

(1) Except as otherwise expressly provided in this [act], any matter relating to the activities of the company is decided exclusively by the managers.

(2) Each manager has equal rights in the management and conduct of the activities of the company.

(3) A difference arising among managers as to a matter in the ordinary course of the activities of the company may be decided by a majority of the managers.

(4) The consent of all members is required to:

(A) sell, lease, exchange, or otherwise dispose of all, or substantially all, of the company's property, with or without the good will, outside the ordinary course of the company's activities;

(B) approve a merger, conversion, or domestication under [Article] 10;

(C) undertake any other act outside the ordinary course of the company's activities; and

(D) amend the operating agreement.

(5) A manager may be chosen at any time by the consent of a majority of the members and remains a manager until a successor has been chosen, unless the manager at an earlier time resigns, is removed, or dies, or, in the case of a manager that is not an individual, terminates. A manager may be removed at any time by the consent of a majority of the members without notice or cause.

(6) A person need not be a member to be a manager, but the dissociation of a member that is also a manager removes the person as a manager. If a person that is both a manager and a member ceases to be a manager, that cessation does not by itself dissociate the person as a member.

(7) A person's ceasing to be a manager does not discharge any debt, obligation, or other liability to the limited liability company or members which the person incurred while a



manager.

(d) An action requiring the consent of members under this [act] may be taken without a meeting, and a member may appoint a proxy or other agent to consent or otherwise act for the member by signing an appointing record, personally or by the member's agent.

(e) The dissolution of a limited liability company does not affect the applicability of this section. However, a person that wrongfully causes dissolution of the company loses the right to participate in management as a member and a manager.

(f) This [act] does not entitle a member to remuneration for services performed for a member-managed limited liability company, except for reasonable compensation for services rendered in winding up the activities of the company.

### Comment

**Subsection (a)** – This subsection follows implicitly from the definitions of “manager-managed” and “member-managed” limited liability companies, Section 102(10) and (12), but is included here for the sake of clarity. Although this Act has eliminated the link between management structure and statutory apparent authority, Section 301, the Act retains the manager-managed and member-managed constructs as options for members to use to structure their *inter se* relationship.

**Subsection (b)** – The subsection states default rules that, under Section 110, are subject to the operating agreement.

**Subsection (c)** – Like subsection (b), this subsection states default rules that, under Section 110, are subject to the operating agreement. For example, a limited liability company's operating agreement might state “This company is manager-managed,” Section 102(10)(i), while providing that managers must submit specified ordinary matters for review by the members.

The actual authority of an LLC's manager or managers is a question of agency law and depends fundamentally on the contents of the operating agreement and any separate management contract between the LLC and its manager or managers. These agreements are the primary source of the manifestations of the LLC (as principal) from which a manager (as agent) will form the reasonable beliefs that delimit the scope of the manager's actual authority. RESTATEMENT (THIRD) OF AGENCY § 3.01 (2006). *See also* RESTATEMENT (SECOND) OF AGENCY §§ 15, 26.

Other information may be relevant as well, such as the course of dealing within the LLC, unless the operating agreement effectively precludes consideration of that information. See Section 110(a)(4) (stating that the operating agreement governs “the means and conditions for amending the operating agreement”) and the comment to that subparagraph, which states that:

[Although this] Act does not specially authorize the operating agreement to limit the sources in which terms of the operating agreement might be found or limit amendments to specified modes ... Paragraph (a)(4) could be read to encompass

such authorization. Also, under Section 107 the parol evidence rule will apply to a written operating agreement containing an appropriate merger provision.

If the operating agreement and a management contract conflict, the reasonable manager will know that the operating agreement controls the extent of the manager's rightful authority to act for the LLC— despite any contract claims the manager might have. *See* Section 111(a)(2) (stating that the operating agreement governs “the rights and duties under this [act] of a person in the capacity of manager”) and the comment to that paragraph, which states:

Because the term “[o]perating agreement . . . includes the agreement as amended or restated,” Section 102(13), this paragraph gives the members the ongoing power to define the role of an LLC's managers. Power is not the same as right, however, and exercising the power provided by this paragraph might constitute a breach of a separate contract between the LLC and the manager.

*See also* RESTATEMENT (THIRD) OF AGENCY § 8.13, cmt. b (2006) and RESTATEMENT (SECOND) OF AGENCY, § 432, cmt. b (stating that, when a principal's instructions to an agent contravene a contract between the principal and agent, the agent may have a breach of contract claim but has no right to act contrary to the principal's instructions).

If (i) an LLC's operating agreement merely states that the LLC is manager-managed and does not further specify the managerial responsibilities, and (ii) the LLC has only one manager, the actual authority analysis is simple. In that situation, this subsection:

- serves as “gap filler” to the operating agreement; and thereby
- constitutes the LLC's manifestation to the manager as to the scope of the manager's authority; and thereby
- delimits the manager's actual authority, subject to whatever subsequent manifestations the LLC may make to the manager (e.g., by a vote of the members, or an amendment of the operating agreement).

If the operating agreement states only that the LLC is manager-managed and the LLC has more than one manager, the question of actual authority has an additional aspect. It is necessary to determine what actual authority any one manager has to act alone.

Paragraphs (c)(2), (3), and (4) combine to provide the answer. A single manager of a multi-manager LLC:

- has no actual authority to commit the LLC to any matter “outside the ordinary course of the activities of the company,” paragraph (c)(4)(C), or any matter encompassed in paragraph (c)(4); and
- has the actual authority to commit the LLC to any matter “in the ordinary course of the activities of the company,” paragraph (c)(3), unless the manager has reason to know that other managers might disagree or the manager has some other reason to know that consultation with fellow managers is appropriate.

The first point follows self-evidently from the language of paragraphs (c)(3) and (c)(4). In light of that language, no manager could reasonably believe to the contrary (unless the operating agreement provided otherwise).

The second point follows because:

- Subsection (c) serves as the gap-filler manifestation from the LLC to its managers, and subsection (c) does not require managers of a multi-manager LLC to act only in concert or after consultation.
- To the contrary, subject to the operating agreement:
  - paragraph (c)(2) expressly provides that “each manager has equal rights in the management and conduct of the activities of the company,” and
  - paragraph (c)(3) suggests that several (as well as joint) activity is appropriate on ordinary matters, so long as the manager acting in the matter has no reason to believe that the matter will be controversial among the managers and therefore requires a decision under paragraph (c)(3).

While the individual members of a corporate board of directors lack actual authority to bind the corporation, 2 WILLIAM MEADE FLETCHER, FLETCHER CYCLOPEDIA OF THE LAW OF CORPORATIONS, § 392 (noting “the overwhelming weight of authority”), subsection (c) does not describe “board” management. Instead, subsection (c) provides management rules derived from those that govern the members of a general partnership and multiple general partners of a limited partnership. RUPA, § 401 and ULPA (2001), § 406.

The common law of agency will also determine the apparent authority of an LLC’s manager or managers, and in that analysis what the particular third party knows or has reason to know about the management structure and business practices of the particular LLC will always be relevant. RESTATEMENT (THIRD) OF AGENCY § 3.03 cmt. d (2006) (“The nature of an organization's business or activity is relevant to whether a third party could reasonably believe that a [manager] is authorized to commit the organization to a particular transaction.”).

As a general matter, however – i.e., as to the apparent authority of the position of LLC manager under this Act – courts may view the position as clothing its occupants with the apparent authority to take actions that reasonably appear within the ordinary course of the company’s business. The actual authority analysis stated above supports that proposition; absent a reason to believe to the contrary, a third party could reasonably believe a manager to possess the authority contemplated by the gap-fillers of the statute. *But see* Section 102(9), cmt. (stating that “confusion around the term ‘manager’ is common to almost all LLC statutes”).

**Subsection (c)(5)** – Under the default rule stated in this paragraph, dissolution of an entity that is a manager does not end the entity’s status as manager. Contrast Section 602(4)(D) (referring to the expulsion of a member that is a partnership or limited liability company and authorizing the other members to expel, by unanimous consent, the dissolved partnership or limited liability company).

An LLC does not cease to be “manager-managed” simply because no managers are in

place. In that situation, absent additional facts, the LLC is manager-managed and the manager position is vacant. Non-manager members who exercise managerial functions during the vacancy (or at any other time) will have duties as determined by other law, most particularly the law of agency.

**Subsection (c)(7)** – The obligation to safeguard trade secrets and other confidential or proprietary information is incurred when the person is a manager, and a subsequent cessation does not entitle the person to usurp the information or use it to the prejudice of the LLC after the cessation.

**Subsection (e)** – Under the default rules of this Act, it is not possible for a person to wrongfully cause dissolution (as distinguished from wrongfully dissociating). Compare Section 701 with Section 601(b). However, the operating agreement might contemplate wrongful dissolution, and this subsection would then apply – unless the operating provides otherwise. Under the second sentence of this subsection, a person might lose the rights to act as a manager without automatically and formally ceasing to be denominated as a manager.

**Subsection (f)** – This provision traces back to the 1914 Uniform Partnership Act, § 18(f) and is included for fear that its absence might be misinterpreted as implying a contrary rule.

This Act does not provide for remuneration to a manager of a manager-managed LLC. That issue is for the operating agreement, or a separate agreement between the LLC and the manager. A manager seeking compensation will have the burden of proving an agreement. For a case demonstrating how *not* to establish an agreement, see *Jandrain v. Lovald*, 351B.R. 679 (D. S.D. 2006).

#### SECTION 408. INDEMNIFICATION AND INSURANCE.

(a) A limited liability company shall reimburse for any payment made and indemnify for any debt, obligation, or other liability incurred by a member of a member-managed company or the manager of a manager-managed company in the course of the member's or manager's activities on behalf of the company, if, in making the payment or incurring the debt, obligation, or other liability, the member or manager complied with the duties stated in Sections 405 and 409.

(b) A limited liability company may purchase and maintain insurance on behalf of a member or manager of the company against liability asserted against or incurred by the member or manager in that capacity or arising from that status even if, under Section 110(g), the operating agreement could not eliminate or limit the person's liability to the company for the conduct giving rise to the liability.

#### Comment

**Subsection (a)** – This subsection states a default rule, which corresponds to the default

rules on management duties. In the default mode, the correspondence is appropriate, because otherwise the statutory rule on indemnification could undercut or even vitiate the statutory rules on duty. Both this subsection and the rules on duty are subject to the operating agreement.

This subsection does not expressly require a limited liability company to provide advances to cover expenses. However, in some jurisdictions the indemnity obligation might be interpreted to include an obligation to make advances.

This subsection concerns only managers of manager-managed limited liability companies and members of member-managed companies. The definite article in the phrases “the member’s” [paragraph (1)] and “the member” [paragraph (2)] refers back to the original phrase “A limited liability company shall reimburse . . . and indemnify . . . a member of a member-managed company . . .” A limited liability company’s obligation, if any, to reimburse or indemnify others (including non-managing members of a manager-managed LLC and LLC employees) is a question for other law, including the law of agency.

**Subsection (b)** – In contrast to subsection (a), this subsection encompasses all members, not just members in a member-managed LLC.

This subsection’s language is very broad and authorizes an LLC to purchase insurance to cover, e.g., a manager’s intentional misconduct. It is unlikely that such insurance would be available. For restrictions on the power of an operating agreement to provide for indemnification, see Section 110, particularly subsection (g).

#### SECTION 409. STANDARDS OF CONDUCT FOR MEMBERS AND MANAGERS.

(a) A member of a member-managed limited liability company owes to the company and, subject to Section 901(b), the other members the fiduciary duties of loyalty and care stated in subsections (b) and (c).

(b) The duty of loyalty of a member in a member-managed limited liability company includes the duties:

(1) to account to the company and to hold as trustee for it any property, profit, or benefit derived by the member:

(A) in the conduct or winding up of the company’s activities;

(B) from a use by the member of the company’s property; or

(C) from the appropriation of a limited liability company opportunity;

(2) to refrain from dealing with the company in the conduct or winding up of the company’s activities as or on behalf of a person having an interest adverse to the company; and

(3) to refrain from competing with the company in the conduct of the company’s activities before the dissolution of the company.

(c) Subject to the business judgment rule, the duty of care of a member of a member-managed limited liability company in the conduct and winding up of the company's activities is to act with the care that a person in a like position would reasonably exercise under similar circumstances and in a manner the member reasonably believes to be in the best interests of the company. In discharging this duty, a member may rely in good faith upon opinions, reports, statements, or other information provided by another person that the member reasonably believes is a competent and reliable source for the information.

(d) A member in a member-managed limited liability company or a manager-managed limited liability company shall discharge the duties under this [act] or under the operating agreement and exercise any rights consistently with the contractual obligation of good faith and fair dealing.

(e) It is a defense to a claim under subsection (b)(2) and any comparable claim in equity or at common law that the transaction was fair to the limited liability company.

(f) All of the members of a member-managed limited liability company or a manager-managed limited liability company may authorize or ratify, after full disclosure of all material facts, a specific act or transaction that otherwise would violate the duty of loyalty.

(g) In a manager-managed limited liability company, the following rules apply:

(1) Subsections (a), (b), (c), and (e) apply to the manager or managers and not the members.

(2) The duty stated under subsection (b)(3) continues until winding up is completed.

(3) Subsection (d) applies to the members and managers.

(4) Subsection (f) applies only to the members.

(5) A member does not have any fiduciary duty to the company or to any other member solely by reason of being a member.

### **Comment**

This section follows the structure of many LLC acts, first stating the duties of members in a member-managed limited liability company and then using that statement and a "switching" mechanism, subsection (g), to allocate duties in a manager-managed company. The duties stated in this section are subject to the operating agreement, but Section 110 contains important limitations on the power of the operating agreement to affect fiduciary duties and the obligation of good faith.

This section contains several noteworthy developments in the law of unincorporated business organizations:

- fiduciary duty is “uncabined” – see the Comment to subsections (a) and (b);
- the duty of care is not set at gross negligence – see the Comment to subsection (c); and
- the statutory endorsement of self-interest is omitted – see the Comment to section (e)

The standards, duties, and obligations of this Section are subject to delineation, restriction, and, to some extent, elimination by the operating agreement. See Section 110.

**Subsections (a) and (b)** – Until the promulgation of RUPA, it was almost axiomatic that: (i) fiduciary duties reflect judge-made law; and (ii) statutory formulations can express some of that law but do not exhaustively codify it. The original UPA was a prime example of this approach.

In an effort to respect freedom of contract, bolster predictability, and protect partnership agreements from second-guessing, the Conference decided that RUPA should fence or “cabin in” all fiduciary duties within a statutory formulation. That decision was followed without re-consideration in ULLCA and ULPA (2001).

This Act takes a different approach. After lengthy discussion in the drafting committee and on the floor of the 2006 Annual Meeting, the Conference decided that: (i) the “corral” created by RUPA does not fit in the very complex and variegated world of LLCs; and (ii) it is impracticable to cabin all LLC-related fiduciary duties within a statutory formulation.

As a result, this Act: (i) eschews “only” and “limited to” – the words RUPA used in an effort to exhaustively codify fiduciary duty; (ii) codifies the core of the fiduciary duty of loyalty; but (iii) does not purport to discern every possible category of overreaching. One important consequence is to allow courts to continue to use fiduciary duty concepts to police disclosure obligations in member-to-member and member-LLC transactions.

**Subsection (c)** – Although ULLCA, § 409(c) followed RUPA, § 404(c) and provided a gross negligence standard of care, at least a plurality of LLC statutes use an ordinary care standard. Sandra K. Miller, *The Role of the Court in Balancing Contractual Freedom With the Need For Mandatory Constraints on Opportunistic and Abusive Conduct in the LLC*, 152 U. PA. L. REV 1609, 1658 (May 2004) (containing two tables characterizing the standard of care under LLC statutes: 21 states with “good faith prudent person” language and 19 states using “gross negligence or willful misconduct” language); Elizabeth S. Miller and Thomas E. Rutledge, *The Duty of Finest Loyalty and Reasonable Decisions: The Business Judgment Rule in Unincorporated Business Organizations*, 30 DEL. J. CORP. L. 343, 366- 368 (2005) (stating that “[a]pproximately eighteen state LLC statutes parallel language formerly used in the MBCA and require managers and managing members to act in good faith and exercise the care of an ordinarily prudent person in a like position under similar circumstances”). See also William J. Callison, *“The Law Does Not Perfectly Comprehend . . .” : The Inadequacy of the Gross*

*Negligence Duty of Care Standard in Unincorporated Business Organizations*, 94 KY. L.J. 451, 452 (2005-2006) (“examin[ing] the gross negligence standard and find[ing] it wanting, particularly as it has intruded, largely unexamined and by drafting osmosis, into subsequent uniform acts governing limited partnerships and limited liability companies”).

In some circumstances, an unadorned standard of ordinary care is appropriate for those in charge of a business organization or similar, non-business enterprise. In others, the proper application of the duty of care must take into account the difficulties inherent in establishing an enterprise’s most fundamental policies, supervising the enterprise’s overall activities, or making complex business judgments. Corporate law subdivides circumstances somewhat according to the formal role exercised by the person whose conduct is later challenged (e.g., distinguishing the duties of directors from the duties of officers). LLC law cannot follow that approach, because a hallmark of the LLC entity is its structural flexibility.

This subsection, therefore, seeks “the best of both worlds” – stating a standard of ordinary care but subjecting that standard to the business judgment rule to the extent circumstances warrant. The content and force of the business judgment rule vary across jurisdictions, and therefore the meaning of this subsection may vary from jurisdiction to jurisdiction.

That result is intended. In any jurisdiction, the business judgment rule’s application will vary depending on the nature of the challenged conduct. There is, for example, very little (if any) judgment involved when a person with managerial power acts (or fails to act) on an essentially ministerial matter. Moreover, under the law of many jurisdictions, the business judgment rule applies similarly across the range of business organizations. That is, the doctrine is sufficiently broad and conceptual so that the formality of organizational choice is less important in shaping the application of the rule than are the nature of the challenged conduct and the responsibilities and authority of the person whose conduct is being challenged.

This Act seeks therefore to invoke rather than unsettle whatever may be each jurisdiction’s approach to the business judgment rule.

**Subsection (d)** – This subsection refers to the “*contractual* obligation of good faith and fair dealing” to emphasize that the obligation is not an invitation to re-write agreements among the members. As explained in the Comment to ULP A (2001), § 305(b):

The obligation of good faith and fair dealing is not a fiduciary duty, does not command altruism or self-abnegation, and does not prevent a partner from acting in the partner’s own self-interest. Courts should not use the obligation to change ex post facto the parties’ or this Act’s allocation of risk and power. To the contrary, in light of the nature of a limited partnership, the obligation should be used only to protect agreed-upon arrangements from conduct that is manifestly beyond what a reasonable person could have contemplated when the arrangements were made.... In sum, the purpose of the obligation of good faith and fair dealing is to protect the arrangement the partners have chosen for themselves, not to restructure that arrangement under the guise of safeguarding it.



At first glance, it may seem strange to apply a contractual obligation to statutory duties and rights – i.e., duties and rights “under this [act].” However, for the most part those duties and rights apply to relationships *inter se* the members and the LLC and function only to the extent not displaced by the operating agreement. In the contract-based organization that is an LLC, those statutory default rules are intended to function like a contract. Therefore, applying the contractual notion of good faith makes sense.

As to whether the obligation stated in this subsection applies to transferees, see the Comment to Section 112(b).

**Subsection (e)** – Section 409 omits a noteworthy provision, which, beginning with RUPA, has been standard in the uniform business entity acts. RUPA, ULLCA, ULPA (2001) each placed the following language in the subsection following the formulation of the obligation of good faith:

A member ... does not violate a duty or obligation under this [act] or under the operating agreement merely because the member’s conduct furthers the member’s own interest.

This language is inappropriate in the complex and variegated world of LLCs. As a proposition of contract law, the language is axiomatic and therefore unnecessary. In the context of fiduciary duty, the language is at best incomplete, at worst wrong, and in any event confusing.

This Act’s subsection (e) takes a very different approach, stating a well-established principle of judge-made law. Despite Section 107, the statement is not surplusage. Given this Act’s very detailed treatment of fiduciary duties and especially the Act’s very detailed treatment of the power of the operating agreement to modify fiduciary duties, the statement is important because its absence might be confusing. (An *ex post* fairness justification is not the same as an *ex ante* agreement to modify, but the topics are sufficiently close for a danger of the affirmative pregnant.)

This Act also omits, as anachronistic and potentially confusing, any provision resembling ULLCA, § 409(f) (“A member of a member-managed company may lend money to and transact other business with the company. As to each loan or transaction, the rights and obligations of the member are the same as those of a person who is not a member, subject to other applicable law.”) *See also* ULPA (2001), § 112 (“A partner may lend money to and transact other business with the limited partnership and has the same rights and obligations with respect to the loan or other transaction as a person that is not a partner.”)

Those provisions originated to combat the notion that debts to partners were categorically inferior to debts to non-partner creditors. That notion has never been part of LLC law, and so a modern uniform LLC act need not include language combating the notion. Moreover, to the uninitiated the language can be confusing, because the words might: (i) seem to undercut the duty of loyalty, which they do not; and (ii) deflect attention from bankruptcy law and the law of fraudulent transfer, which assuredly can look askance at transactions between an entity and an

“insider.”

**Subsection (f)** –The operating agreement can provide additional or different methods of authorization or ratification, subject to the strictures of Section 110(e). See the Comment to that subsection.

**Subsection (g)** – This is the “switching” mechanism, referred to in the introduction to this Comment.

**Subsection (g)(2)** – On the assumption that the members of a manager-managed LLC are dependent on the manager, this paragraph extends the duty longer than in a member-managed LLC.

**Subsection (g)(5)** – This paragraph merely negates a claim of fiduciary duty that is exclusively status-based and does not immunize misconduct.

EXAMPLE: Although a limited liability company is manager-managed, one member who is not a manager owns a controlling interest and effectively, albeit indirectly, controls the company’s activities. A member owning a minority interest brings an action for dissolution under Section 701(a)(5)(B) (oppression by “the managers or those members in control of the company”). The court wishes to understand a claim as one alleging a breach of fiduciary duty by the controlling member. Subsection (g)(5) does not preclude that approach.

#### SECTION 410. RIGHT OF MEMBERS, MANAGERS, AND DISSOCIATED MEMBERS TO INFORMATION.

(a) In a member-managed limited liability company, the following rules apply:

(1) On reasonable notice, a member may inspect and copy during regular business hours, at a reasonable location specified by the company, any record maintained by the company regarding the company’s activities, financial condition, and other circumstances, to the extent the information is material to the member’s rights and duties under the operating agreement or this [act].

(2) The company shall furnish to each member:

(A) without demand, any information concerning the company’s activities, financial condition, and other circumstances which the company knows and is material to the proper exercise of the member’s rights and duties under the operating agreement or this [act], except to the extent the company can establish that it reasonably believes the member already knows the information; and

(B) on demand, any other information concerning the company’s

activities, financial condition, and other circumstances, except to the extent the demand or information demanded is unreasonable or otherwise improper under the circumstances.

(3) The duty to furnish information under paragraph (2) also applies to each member to the extent the member knows any of the information described in paragraph (2).

(b) In a manager-managed limited liability company, the following rules apply:

(1) The informational rights stated in subsection (a) and the duty stated in subsection (a)(3) apply to the managers and not the members.

(2) During regular business hours and at a reasonable location specified by the company, a member may obtain from the company and inspect and copy full information regarding the activities, financial condition, and other circumstances of the company as is just and reasonable if:

(A) the member seeks the information for a purpose material to the member's interest as a member;

(B) the member makes a demand in a record received by the company, describing with reasonable particularity the information sought and the purpose for seeking the information; and

(C) the information sought is directly connected to the member's purpose.

(3) Within 10 days after receiving a demand pursuant to paragraph (2)(B), the company shall in a record inform the member that made the demand:

(A) of the information that the company will provide in response to the demand and when and where the company will provide the information; and

(B) if the company declines to provide any demanded information, the company's reasons for declining.

(4) Whenever this [act] or an operating agreement provides for a member to give or withhold consent to a matter, before the consent is given or withheld, the company shall, without demand, provide the member with all information that is known to the company and is material to the member's decision.

(c) On 10 days' demand made in a record received by a limited liability company, a dissociated member may have access to information to which the person was entitled while a member if the information pertains to the period during which the person was a member, the person seeks the information in good faith, and the person satisfies the requirements imposed on

a member by subsection (b)(2). The company shall respond to a demand made pursuant to this subsection in the manner provided in subsection (b)(3).

(d) A limited liability company may charge a person that makes a demand under this section the reasonable costs of copying, limited to the costs of labor and material.

(e) A member or dissociated member may exercise rights under this section through an agent or, in the case of an individual under legal disability, a legal representative. Any restriction or condition imposed by the operating agreement or under subsection (g) applies both to the agent or legal representative and the member or dissociated member.

(f) The rights under this section do not extend to a person as transferee.

(g) In addition to any restriction or condition stated in its operating agreement, a limited liability company, as a matter within the ordinary course of its activities, may impose reasonable restrictions and conditions on access to and use of information to be furnished under this section, including designating information confidential and imposing nondisclosure and safeguarding obligations on the recipient. In a dispute concerning the reasonableness of a restriction under this subsection, the company has the burden of proving reasonableness.

### Comment

This section is derived from ULPA (2001), §§ 304 (rights to information of limited partners and former limited partners) and 407 (same re: general partners and former general partners). The rules stated here are what might be termed “quasi-default rules” – subject to some change by the operating agreement. Section 110(c)(6) (prohibiting unreasonable restrictions on the information rights stated in this section).

Although the rights and duties stated in this section are extensive, they may not necessarily be exhaustive. In some situations, some courts have seen owners’ information rights as reflecting a fiduciary duty of those with management power. This Act’s statement of fiduciary duties is not exhaustive. *See* Comment to Section 409 (explaining that this Act does not seek to “cabin in” all fiduciary duties). In contrast, the operating agreement has considerable “cabining in” power of its own. Section 110(d)(4).

**Subsection (a)** – Paragraph 1 states the rule pertaining to information memorialized in “records maintained by the company”. Paragraph 2 applies to information not in such a record. Appropriately, paragraph (2) sets a more demanding standard for those seeking information.

**Subsection (a)(2) and (3)** – In appropriate circumstances, violation of either or both of these provisions might cause a court to enjoin or even rescind action taken by the LLC, especially when the violation has interfered with an approval or veto mechanism involving member consent. *E.g. Blue Chip Emerald LLC v. Allied Partners Inc.*, 299 A.D.2d 278, 279-280 (N.Y. App. Div. 2002) (invoking partnership law precedent as reflecting a duty of full disclosure

and holding that “[a]bsent such full disclosure, the transaction is voidable).

**Subsection (a)(2)** – Violation of this paragraph could give rise to a claim for damages against a member or manager [see subsection (b)(1)] who breaches the duties stated in Section 409 in causing or suffering the LLC to violate this paragraph.

**Subsection (a)(3)** – A member’s violation of this paragraph is actionable in damages without need to show a violation of a duty stated in Section 409.

**Subsection (b)(1)** – This is a switching provision. A manager’s violation of the duty stated in subsection (a)(3) is actionable in damages without need to show a violation of a duty stated in Section 409.

**Subsection (b)(2)** – This paragraph refers to “information” rather than “records maintained by the company” – compare subsection (a) – so in some circumstances the company might have an obligation to memorialize information. Such circumstances will likely be rare or at least unusual. Section 410 generally concerns providing existing information, not creating it. In any event, a member does not trigger the company’s obligation under this paragraph merely by satisfying subparagraphs (A) through (C). The member must also satisfy the “just and reasonable” requirement.

**Subsection (c)** – This section does not control the rights of the estate of a member who dissociates by dying. In that circumstance, Section 504 controls.

**Subsection (g)** – The phrase “as a matter within the ordinary course of its activities” means that a mere majority consent is needed to impose a restriction or condition. *See* Section 407(b)(3) and (c)(3). This approach is necessary, lest a requesting member (or manager-member) have the power to block imposition of a reasonable restriction or condition needed to prevent the requestor from abusing the LLC.

The burden of proof under this subsection contrasts with the burden of proof when someone claims that a term of an operating agreement violates Section 110(c)(6). Under that subsection, as a matter of ordinary procedural law, the burden is on the person making the claim.

(11) [ARTICLE] 5

(12) TRANSFERABLE INTERESTS AND RIGHTS OF TRANSFEREES AND CREDITORS

SECTION 501. NATURE OF TRANSFERABLE INTEREST. A transferable interest is personal property.

**Comment**

**Source** – This Article most directly follows ULPA (2001), Article 7, because ULPA (2001) reflects the Conference’s most recent thinking on the issues addressed here. However, ULPA (2001), Article 7 is quite similar in substance to ULLCA, Article 5, and both those Articles derive from Article 5 of RUPA.

Whether a transferable interest pledged as security is governed by Article 8 or 9 of the Uniform Commercial Code depends on the facts and the rules stated in those Articles.

This Act does not include ULLCA § 501(a), which provided: “A member is not a co-owner of, and has no transferable interest in, property of a limited liability company.” That language was a vestige of the “aggregate” notion of the law of general partnerships, and in a modern LLC statute would be at least surplusage and perhaps confusing as well.

SECTION 502. TRANSFER OF TRANSFERABLE INTEREST.

(a) A transfer, in whole or in part, of a transferable interest:

(1) is permissible;

(2) does not by itself cause a member’s dissociation or a dissolution and winding up of the limited liability company’s activities; and

(3) subject to Section 504, does not entitle the transferee to:

(A) participate in the management or conduct of the company’s activities;

or

(B) except as otherwise provided in subsection (c), have access to records or other information concerning the company’s activities.

(b) A transferee has the right to receive, in accordance with the transfer, distributions to which the transferor would otherwise be entitled.

(c) In a dissolution and winding up of a limited liability company, a transferee is entitled to an account of the company’s transactions only from the date of dissolution.

(d) A transferable interest may be evidenced by a certificate of the interest issued by the limited liability company in a record, and, subject to this section, the interest represented by the certificate may be transferred by a transfer of the certificate.

(e) A limited liability company need not give effect to a transferee's rights under this section until the company has notice of the transfer.

(f) A transfer of a transferable interest in violation of a restriction on transfer contained in the operating agreement is ineffective as to a person having notice of the restriction at the time of transfer.

(g) Except as otherwise provided in Section 602(4)(B), when a member transfers a transferable interest, the transferor retains the rights of a member other than the interest in distributions transferred and retains all duties and obligations of a member.

(h) When a member transfers a transferable interest to a person that becomes a member with respect to the transferred interest, the transferee is liable for the member's obligations under Sections 403 and 406(c) known to the transferee when the transferee becomes a member.

### **Comment**

One of the most fundamental characteristics of LLC law is its fidelity to the "pick your partner" principle. This section is the core of the Act's provisions reflecting and protecting that principle.

A member's rights in a limited liability company are bifurcated into economic rights (the transferable interest) and governance rights (including management rights, consent rights, rights to information, rights to seek judicial intervention). Unless the operating agreement otherwise provides, a member acting without the consent of all other members lacks both the power and the right to: (i) bestow membership on a non-member, Section 401(d); or (ii) transfer to a non-member anything other than some or all of the member's transferable interest. Section 502(a)(3). However, consistent with current law, a member may transfer governance rights to another member without obtaining consent from the other members. Thus, this Act does not itself protect members from control shifts that result from transfers among members (as distinguished from transfers to non-members who seek thereby to become members).

This section applies regardless of whether the transferor is a member, a transferee of a member, a transferee of a transferee, etc. *See* Section 102(21) (defining "transferable interest" in terms of a right "originally associated with a person's capacity as a member" regardless of "whether or not the person remains a member or continues to own any part of the right").

**Subsection (a)** – The definition of "transfer," Section 102(20), and this subsection's reference to "in whole or in part" combine to mean that this section encompasses not only unconditional, permanent, and complete transfers but also temporary, contingent, and partial ones as well. Thus, for example, a charging order under Section 504 effects a transfer of part of

the judgment debtor's transferable interest, as does the pledge of a transferable interest as collateral for a loan and the gift of a life-interest in a member's rights to distribution.

**Subsection (a)(2)** – Section 602(4)(B) creates a risk of dissociation via expulsion when a member transfers all of the member's transferable interest.

**Subsection (a)(3)** – Mere transferees have no right to intrude as the members carry on their activities as members. When a member dies, other law may effect a transfer of the member's interest to the member's estate or personal representative. Section 504 contains special rules applicable to that situation.

**Subsection (b)** – Amounts due under this subsection are of course subject to offset for any amount owed to the limited liability company by the member or dissociated member on whose account the distribution is made. As to whether an LLC may properly offset for claims against a transferor that was never a member is matter for other law, specifically the law of contracts dealing with assignments.

**Subsection (d)** – The use of certificates can raise issues relating to Articles 8 and 9 of the Uniform Commercial Code.

#### SECTION 503. CHARGING ORDER.

(a) On application by a judgment creditor of a member or transferee, a court may enter a charging order against the transferable interest of the judgment debtor for the unsatisfied amount of the judgment. A charging order constitutes a lien on a judgment debtor's transferable interest and requires the limited liability company to pay over to the person to which the charging order was issued any distribution that would otherwise be paid to the judgment debtor.

(b) To the extent necessary to effectuate the collection of distributions pursuant to a charging order in effect under subsection (a), the court may:

(1) appoint a receiver of the distributions subject to the charging order, with the power to make all inquiries the judgment debtor might have made; and

(2) make all other orders necessary to give effect to the charging order.

(c) Upon a showing that distributions under a charging order will not pay the judgment debt within a reasonable time, the court may foreclose the lien and order the sale of the transferable interest. The purchaser at the foreclosure sale only obtains the transferable interest, does not thereby become a member, and is subject to Section 502.

(d) At any time before foreclosure under subsection (c), the member or transferee whose transferable interest is subject to a charging order under subsection (a) may extinguish the



charging order by satisfying the judgment and filing a certified copy of the satisfaction with the court that issued the charging order.

(e) At any time before foreclosure under subsection (c), a limited liability company or one or more members whose transferable interests are not subject to the charging order may pay to the judgment creditor the full amount due under the judgment and thereby succeed to the rights of the judgment creditor, including the charging order.

(f) This [act] does not deprive any member or transferee of the benefit of any exemption laws applicable to the member's or transferee's transferable interest.

(g) This section provides the exclusive remedy by which a person seeking to enforce a judgment against a member or transferee may, in the capacity of judgment creditor, satisfy the judgment from the judgment debtor's transferable interest.

### **Comment**

Charging order provisions appear in various forms in UPA, ULPA, RULPA, RUPA, ULLCA, and ULPA (2001). This section builds on those acts, while: (i) modernizing the language; (ii) making explicit certain points that have been at best implicit; and (iii) seeking to delineate more precisely the types of extraordinary circumstances that would have to exist before a court enforcing a charging order would be justified in interfering with an LLC's management or activities.

This section balances the needs of a judgment creditor of a member or transferee with the needs of the limited liability company and the members. The section achieves that balance by allowing the judgment creditor to collect on the judgment through the transferable interest of the judgment debtor while prohibiting interference in the management and activities of the limited liability company.

Under this section, the judgment creditor of a member or transferee is entitled to a charging order against the relevant transferable interest. While in effect, that order entitles the judgment creditor to whatever distributions would otherwise be due to the member or transferee whose interest is subject to the order. However, the judgment creditor has no say in the timing or amount of those distributions. The charging order does not entitle the judgment creditor to accelerate any distributions or to otherwise interfere with the management and activities of the limited liability company.

The operating agreement has no power to alter the provisions of this section to the prejudice of third parties. Section 110(c)(11).

**Subsection (a)** – The phrase “judgment debtor” encompasses both members and transferees. As a matter of civil procedure and due process, an application for a charging order must be served both on the limited liability company and the member or transferee whose transferable interest is to be charged.

**Subsection (b)** – Paragraph (2) refers to “other orders” rather than “additional orders”. Therefore, given appropriate circumstances, a court may invoke either paragraph (1) or (2) or both.

**Subsection (b)(1)** – The receiver contemplated here is not a receiver for the limited liability company, but rather a receiver for the distributions. The principal advantage provided by this paragraph is an expanded right to information. However, that right goes no further than “the extent necessary to effectuate the collections of distributions pursuant to a charging order.”

**Subsection (b)(2)** – This paragraph must be understood in the context of the balance described in the introduction to this section’s Comment. In particular, the court’s power to make orders “that the circumstances may of the case may require” is limited to “giv[ing] effect to the charging order.”

**Example:** A judgment creditor with a charging order believes that the limited liability company should invest less of its surplus in operations, leaving more funds for distributions. The creditor moves the court for an order directing the limited liability company to restrict re-investment. Subsection (b)(2) does not authorize the court to grant the motion.

**Example:** A judgment creditor with a judgment for \$10,000 against a member obtains a charging order against the member’s transferable interest. Having been properly served with the order, the limited liability company nonetheless fails to comply and makes a \$3000 distribution to the member. The court has the power to order the limited liability company to pay \$3000 to the judgment creditor to “give effect to the charging order.”

Under subsection (b)(2), the court also has the power to decide whether a particular payment is a distribution, because that decision determines whether the payment is part of a transferable interest subject to a charging order. To the extent a payment is not a distribution, it is not part of the transferable interest and is not subject to subsection (g). The payment is therefore subject to whatever other creditor remedies may apply.

Section 405(g) states a special exception to the definition of “distribution,” but that exception applies only “[f]or purposes of subsection (a)” of Section 405. Therefore, whether a charging order applies to “amounts constituting reasonable compensation for present or past services or reasonable payments made in the ordinary course of business under a bona fide retirement plan or other benefits program,” Section 405(g), is a question determined under this section, without regard to Section 405(g). To date, case law is scant, but there is authority holding that compensation is a distribution. *PB Real Estate, Inc. v. Dem II Properties*, 719 A.2d 73, 75 (Conn. App. Ct. 1998) (rejecting the defendants’ claim that the payments at issue were merely compensation for their services to their law firm, which was organized as an LLC; noting that the defendants’ characterization was at odds with the firm’s business records and tax returns; holding that the payments received were distributions subject to the charging order).

This Act has no specific rules for determining the fate or effect of a charging order when the limited liability company undergoes a merger, conversion, or domestication under [Article]

10. In the proper circumstances, such an organic change might trigger an order under subsection (b)(2).

**Subsection (c)** –The phrase “that distributions under the charging order will not pay the judgment debt within a reasonable period of time” comes from case law. *See, e.g., Nigri v. Lotz*, 453 S.E.2d 780, 783 (Ga. Ct. App. 1995).

**Subsection (e)** – This Act jettisons the confusing concept of redemption and substitutes an approach that more closely parallels the modern, real-world possibility of the LLC or its members buying the underlying judgment (and thereby dispensing with any interference the judgment creditor might seek to inflict on the LLC). When possible, buying the judgment remains superior to the mechanism provided by this subsection, because: (i) this subsection requires full satisfaction of the underlying judgment, (ii) while the LLC or the other members might be able to buy the judgment for less than face value. On the other hand, this subsection operates without need for the judgment creditor’s consent, so it remains a valuable protection in the event a judgment creditor seeks to do mischief to the LLC.

Whether an LLC’s decision to invoke this subsection is “ordinary course” or “outside the ordinary course,” Section 407(b)(3) and (4) and (c)(3) and (4)(C), depends on the circumstances. However, the involvement of this subsection does not by itself make the decision “outside the ordinary course.”

**Subsection (g)** – This subsection does not override Article 9, which may provide different remedies for a secured creditor acting in that capacity. A secured creditor with a judgment might decide to proceed under Article 9 alone, under this section alone, or under both Article 9 and this section. In the last-mentioned circumstance, the constraints of this section would apply to the charging order but not to the Article 9 remedies.

This subsection is not intended to prevent a court from effecting a “reverse pierce” where appropriate. In a reverse pierce, the court conflates the entity and its owner to hold the entity liable for a debt of the owner. *Litchfield Asset Mgmt. Corp. v. Howell*, 799 A.2d 298, 312 (Conn. App. Ct. 2002) (approving a reverse pierce where a judgment debtor had established a limited liability company in a patent attempt frustrate the judgment creditor).

**SECTION 504. POWER OF PERSONAL REPRESENTATIVE OF DECEASED MEMBER.** If a member dies, the deceased member’s personal representative or other legal representative may exercise the rights of a transferee provided in Section 502(c) and, for the purposes of settling the estate, the rights of a current member under Section 410.

#### **Comment**

**Source:** ULPA (2001) § 704.

Section 410 pertains only to information rights.

(13) [ARTICLE] 6

(14) MEMBER'S DISSOCIATION

**SECTION 601. MEMBER'S POWER TO DISSOCIATE; WRONGFUL DISSOCIATION.**

(a) A person has the power to dissociate as a member at any time, rightfully or wrongfully, by withdrawing as a member by express will under Section 602(1).

(b) A person's dissociation from a limited liability company is wrongful only if the dissociation:

(1) is in breach of an express provision of the operating agreement; or

(2) occurs before the termination of the company and:

(A) the person withdraws as a member by express will;

(B) the person is expelled as a member by judicial order under Section 602(5);

(C) the person is dissociated under Section 602(7)(A) by becoming a debtor in bankruptcy; or

(D) in the case of a person that is not a trust other than a business trust, an estate, or an individual, the person is expelled or otherwise dissociated as a member because it willfully dissolved or terminated.

(c) A person that wrongfully dissociates as a member is liable to the limited liability company and, subject to Section 901, to the other members for damages caused by the dissociation. The liability is in addition to any other debt, obligation, or other liability of the member to the company or the other members.

**Comment**

**Source** – ULPA (2001) § 604, which is based on RUPA Section 602. ULLCA § 602 is functionally identical in some respects but is not a good overall source, because that section presupposes the term/at-will paradigm.

**SECTION 602. EVENTS CAUSING DISSOCIATION.** A person is dissociated as a member from a limited liability company when:

(1) the company has notice of the person's express will to withdraw as a member, but, if the person specified a withdrawal date later than the date the company had notice, on that later

date;

(2) an event stated in the operating agreement as causing the person's dissociation occurs;

(3) the person is expelled as a member pursuant to the operating agreement;

(4) the person is expelled as a member by the unanimous consent of the other members if:

(A) it is unlawful to carry on the company's activities with the person as a

member;

(B) there has been a transfer of all of the person's transferable interest in the

company, other than:

(i) a transfer for security purposes; or

(ii) a charging order in effect under Section 503 which has not been

foreclosed;

(C) the person is a corporation and, within 90 days after the company notifies the person that it will be expelled as a member because the person has filed a certificate of dissolution or the equivalent, its charter has been revoked, or its right to conduct business has been suspended by the jurisdiction of its incorporation, the certificate of dissolution has not been revoked or its charter or right to conduct business has not been reinstated; or

(D) the person is a limited liability company or partnership that has been dissolved and whose business is being wound up;

(5) on application by the company, the person is expelled as a member by judicial order because the person:

(A) has engaged, or is engaging, in wrongful conduct that has adversely and materially affected, or will adversely and materially affect, the company's activities;

(B) has willfully or persistently committed, or is willfully and persistently committing, a material breach of the operating agreement or the person's duties or obligations under Section 409; or

(C) has engaged in, or is engaging, in conduct relating to the company's activities which makes it not reasonably practicable to carry on the activities with the person as a member;

(6) in the case of a person who is an individual:

(A) the person dies; or

(B) in a member-managed limited liability company:

(i) a guardian or general conservator for the person is appointed; or

(ii) there is a judicial order that the person has otherwise become incapable of performing the person's duties as a member under [this act] or the operating agreement;

(7) in a member-managed limited liability company, the person:

(A) becomes a debtor in bankruptcy;

(B) executes an assignment for the benefit of creditors; or

(C) seeks, consents to, or acquiesces in the appointment of a trustee, receiver, or liquidator of the person or of all or substantially all of the person's property;

(8) in the case of a person that is a trust or is acting as a member by virtue of being a trustee of a trust, the trust's entire transferable interest in the company is distributed;

(9) in the case of a person that is an estate or is acting as a member by virtue of being a personal representative of an estate, the estate's entire transferable interest in the company is distributed;

(10) in the case of a member that is not an individual, partnership, limited liability company, corporation, trust, or estate, the termination of the member;

(11) the company participates in a merger under [Article] 10, if:

(A) the company is not the surviving entity; or,

(B) otherwise as a result of the merger, the person ceases to be a member;

(12) the company participates in a conversion under [Article] 10;

(13) the company participates in a domestication under [Article] 10, if, as a result of the domestication, the person ceases to be a member; or

(14) the company terminates.

#### **Comment**

**Source** – ULLCA § 601; RUPA Section 601; ULPA (2001) §§ 601 and 603.

**Paragraph (4)(B)** –Under this paragraph (unless the operating agreement provides otherwise), a member's transferee can protect itself from the vulnerability of "bare transferee" status by obligating the member/transferor to retain a 1% interest and then to exercise its governance rights (including the right to bring a derivative suit) to protect the transferee's interests.

#### **SECTION 603. EFFECT OF PERSON'S DISSOCIATION AS MEMBER.**

(a) When a person is dissociated as a member of a limited liability company:

(1) the person's right to participate as a member in the management and conduct

of the company's activities terminates;

(2) if the company is member-managed, the person's fiduciary duties as a member end with regard to matters arising and events occurring after the person's dissociation; and

(3) subject to Section 504 and [Article] 10, any transferable interest owned by the person immediately before dissociation in the person's capacity as a member is owned by the person solely as a transferee.

(b) A person's dissociation as a member of a limited liability company does not of itself discharge the person from any debt, obligation, or other liability to the company or the other members which the person incurred while a member.

### Comment

**Source** – ULPA (2001) § 605, which was drawn from RUPA Section 603(b).

**Subsection (a)** – This provision makes no reference to power-to-bind matters, because the Act provides that a member *qua* member has no power to bind the LLC. Section 301.

**Subsection (a)(2)** – This provision applies only when the limited liability company is member-managed, because in a manager-managed LLC these duties do not apply to a member *qua* member. Section 409(g)(5).

**Subsection (a)(3)** – This paragraph accords with Section 404(b) – dissociation does not entitle a person to any distribution. Like most *inter se* rules in this Act, this one is subject to the operating agreement. For example, the operating agreement has the power to provide for the buy out of a person's transferable interest in connection with the person's dissociation.

**Subsection (b)** – In a member-managed limited liability company, the obligation to safeguard trade secrets and other confidential or proprietary information is incurred when a person is a member. A subsequent dissociation does not entitle the person to usurp the information or use it to the prejudice of the LLC after the dissociation. (In a manager-managed LLC, any obligations of a non-manager member *viz a viz* proprietary information would be a matter for the operating agreement, the obligation of good faith, or other law.)

(15) [ARTICLE] 7

(16) DISSOLUTION AND WINDING UP

SECTION 701. EVENTS CAUSING DISSOLUTION.

(a) A limited liability company is dissolved, and its activities must be wound up, upon the occurrence of any of the following:

(1) an event or circumstance that the operating agreement states causes dissolution;

(2) the consent of all the members;

(3) the passage of 90 consecutive days during which the company has no members;

(4) on application by a member, the entry by [appropriate court] of an order dissolving the company on the grounds that:

(A) the conduct of all or substantially all of the company's activities is unlawful; or

(B) it is not reasonably practicable to carry on the company's activities in conformity with the certificate of organization and the operating agreement; or

(5) on application by a member, the entry by [appropriate court] of an order dissolving the company on the grounds that the managers or those members in control of the company:

(A) have acted, are acting, or will act in a manner that is illegal or fraudulent; or

(B) have acted or are acting in a manner that is oppressive and was, is, or will be directly harmful to the applicant.

(b) In a proceeding brought under subsection (a)(5), the court may order a remedy other than dissolution.

**Comment**

**Subsection(a)(4)** – The standard stated here is conventional, and this subsection (a)(4) is non-waivable. Section 110(c)(7).

**Subsection (a)(5)** – ULLCA § 801(4)(v) contains a comparable provision, although that provision also gives standing to dissociated members. Even in non-ULLCA states, courts have



begun to apply close corporation “oppression” doctrine to LLCs.

This provision’s reference to “those members in control of the company” implies that such members have a duty to avoid acting oppressively toward fellow members.

Subsection (a)(5) is non-waivable. *See* Section 110(c)(7).

**Subsection (b)** – In the close corporation context, many courts have reached this position without express statutory authority, most often with regard to court-ordered buyouts of oppressed shareholders. This subsection saves courts and litigants the trouble of re-inventing that wheel in the LLC context. However, unlike, subsection (a)(4) and (5), subsection (b) can be overridden by the operating agreement. Thus, the members may agree to a restrict or eliminate a court’s power to craft a lesser remedy, even to the extent of confining the court (and themselves) to the all-or-nothing remedy of dissolution.

#### SECTION 702. WINDING UP.

(a) A dissolved limited liability company shall wind up its activities, and the company continues after dissolution only for the purpose of winding up.

(b) In winding up its activities, a limited liability company:

(1) shall discharge the company’s debts, obligations, or other liabilities, settle and close the company’s activities, and marshal and distribute the assets of the company; and

(2) may:

(A) deliver to the Department of State for filing a statement of dissolution stating the name of the company and that the company is dissolved;

(B) preserve the company activities and property as a going concern for a reasonable time;

(C) prosecute and defend actions and proceedings, whether civil, criminal, or administrative;

(D) transfer the company’s property;

(E) settle disputes by mediation or arbitration;

(F) deliver to the Department of State for filing a statement of termination stating the name of the company and that the company is terminated; and

(G) perform other acts necessary or appropriate to the winding up.

(c) If a dissolved limited liability company has no members, the legal representative of the last person to have been a member may wind up the activities of the company. If the person does so, the person has the powers of a sole manager under Section 407(c) and is deemed to be a

manager for the purposes of Section 304(a)(2).

(d) If the legal representative under subsection (c) declines or fails to wind up the company's activities, a person may be appointed to do so by the consent of transferees owning a majority of the rights to receive distributions as transferees at the time the consent is to be effective. A person appointed under this subsection:

(1) has the powers of a sole manager under Section 407(c) and is deemed to be a manager for the purposes of Section 304(a)(2); and

(2) shall promptly deliver to the Department of State for filing an amendment to the company's certificate of organization to:

(A) state that the company has no members;

(B) state that the person has been appointed pursuant to this subsection to wind up the company; and

(C) provide the street and mailing addresses of the person.

(e) The [appropriate court] may order judicial supervision of the winding up of a dissolved limited liability company, including the appointment of a person to wind up the company's activities:

(1) on application of a member, if the applicant establishes good cause;

(2) on the application of a transferee, if:

(A) the company does not have any members;

(B) the legal representative of the last person to have been a member declines or fails to wind up the company's activities; and

(C) within a reasonable time following the dissolution a person has not been appointed pursuant to subsection (c); or

(3) in connection with a proceeding under Section 701(a)(4) or (5).

### **Comment**

**Source** – ULPA (2001) § 803, which was based on RUPA Sections 802 and 803.

Because under this Act the power to bind a limited liability company to a third party is primarily a matter of agency law, Section 301, Comment, this Act has no need of provisions delineating the effect of dissolution on a member or manager's power to bind.

**Subsection (b)(2)(A) and (F)** – For the constructive notice effect of a statement of dissolution or termination, see Section 103(d)(2)(A) and (B).

SECTION 703. KNOWN CLAIMS AGAINST DISSOLVED LIMITED LIABILITY COMPANY.

(a) Except as otherwise provided in subsection (d), a dissolved limited liability company may give notice of a known claim under subsection (b), which has the effect as provided in subsection (c).

(b) A dissolved limited liability company may in a record notify its known claimants of the dissolution. The notice must:

- (1) specify the information required to be included in a claim;
- (2) provide a mailing address to which the claim is to be sent;
- (3) state the deadline for receipt of the claim, which may not be less than 120 days after the date the notice is received by the claimant; and
- (4) state that the claim will be barred if not received by the deadline.

(c) A claim against a dissolved limited liability company is barred if the requirements of subsection (b) are met and:

- (1) the claim is not received by the specified deadline; or
- (2) if the claim is timely received but rejected by the company:
  - (A) the company causes the claimant to receive a notice in a record stating that the claim is rejected and will be barred unless the claimant commences an action against the company to enforce the claim within 90 days after the claimant receives the notice; and
  - (B) the claimant does not commence the required action within the 90 days.

(d) This section does not apply to a claim based on an event occurring after the effective date of dissolution or a liability that on that date is contingent.

**Comment**

**Source** – ULPA (2001) § 806, which was based on ULLCA § 807, which in turn was based on MBCA § 14.06.

SECTION 704. OTHER CLAIMS AGAINST DISSOLVED LIMITED LIABILITY COMPANY.

(a) A dissolved limited liability company may publish notice of its dissolution and request persons having claims against the company to present them in accordance with the

notice.

(b) The notice authorized by subsection (a) must:

(1) be published at least once in a newspaper of general circulation in the [county] in this state in which the dissolved limited liability company's principal office is located or, if it has none in this state, in the [county] in which the company's designated office is or was last located;

(2) describe the information required to be contained in a claim and provide a mailing address to which the claim is to be sent; and

(3) state that a claim against the company is barred unless an action to enforce the claim is commenced within five years after publication of the notice.

(c) If a dissolved limited liability company publishes a notice in accordance with subsection (b), unless the claimant commences an action to enforce the claim against the company within five years after the publication date of the notice, the claim of each of the following claimants is barred:

(1) a claimant that did not receive notice in a record under Section 703;

(2) a claimant whose claim was timely sent to the company but not acted on; and

(3) a claimant whose claim is contingent at, or based on an event occurring after, the effective date of dissolution.

(d) A claim not barred under this section may be enforced:

(1) against a dissolved limited liability company, to the extent of its undistributed assets; and

(2) if assets of the company have been distributed after dissolution, against a member or transferee to the extent of that person's proportionate share of the claim or of the assets distributed to the member or transferee after dissolution, whichever is less, but a person's total liability for all claims under this paragraph does not exceed the total amount of assets distributed to the person after dissolution.

### **Comment**

**Source** – ULPA (2001) § 807, which was based on ULLCA § 808, which in turn was based on MBCA § 14.07.

**Subsection (d)(2)** – Liability under this paragraph extends to those who have received distributions under a charging order. *See* Comment to 502(a) (explaining that the beneficiary of

a charging order is a transferee). Unlike Section 406(c) (recapture of improper interim distributions), this paragraph contains no “knowledge” element.

#### SECTION 705. ADMINISTRATIVE DISSOLUTION.

(a) The Department of State may dissolve a limited liability company administratively if the company does not:

(1) pay, within 60 days after the due date, any fee, tax, or penalty due to the Department of State under this [act] or law other than this [act]; or

(2) deliver, within 60 days after the due date, its annual report to the Department of State.

(b) If the Department of State determines that a ground exists for administratively dissolving a limited liability company, the Department of State shall file a record of the determination and serve the company with a copy of the filed record.

(c) If within 60 days after service of the copy pursuant to subsection (b) a limited liability company does not correct each ground for dissolution or demonstrate to the reasonable satisfaction of the Department of State that each ground determined by the Department of State does not exist, the Department of State shall dissolve the company administratively by preparing, signing, and filing a declaration of dissolution that states the grounds for dissolution. The Department of State shall serve the company with a copy of the filed declaration.

(d) A limited liability company that has been administratively dissolved continues in existence but, subject to Section 706, may carry on only activities necessary to wind up its activities and liquidate its assets under Sections 702 and 708 and to notify claimants under Sections 703 and 704.

(e) The administrative dissolution of a limited liability company does not terminate the authority of its agent for service of process.

#### **Comment**

**Source** – ULPA (2001) § 809, which was based on ULLCA §§ 809 and 810. *See also* RMBCA §§ 14.20 and 14.21.

#### SECTION 706. REINSTATEMENT FOLLOWING ADMINISTRATIVE DISSOLUTION.

(a) A limited liability company that has been administratively dissolved may apply to the

Department of State for reinstatement within two years after the effective date of dissolution. The application must be delivered to the Department of State for filing and state:

- (1) the name of the company and the effective date of its dissolution;
- (2) that the grounds for dissolution did not exist or have been eliminated; and
- (3) that the company's name satisfies the requirements of Section 108.

(b) If the Department of State determines that an application under subsection (a) contains the required information and that the information is correct, the Department of State shall prepare a declaration of reinstatement that states this determination, sign and file the original of the declaration of reinstatement, and serve the limited liability company with a copy.

(c) When a reinstatement becomes effective, it relates back to and takes effect as of the effective date of the administrative dissolution and the limited liability company may resume its activities as if the dissolution had not occurred.

#### **Comment**

**Source** – ULPA (2001) § 810, which was based on ULLCA § 811. *See also* RMBCA Section 14.22.

#### **SECTION 707. APPEAL FROM REJECTION OF REINSTATEMENT.**

(a) If the Department of State rejects a limited liability company's application for reinstatement following administrative dissolution, the Department of State shall prepare, sign, and file a notice that explains the reason for rejection and serve the company with a copy of the notice.

(b) Within 30 days after service of a notice of rejection of reinstatement under subsection (a), a limited liability company may appeal from the rejection by petitioning the [appropriate court] to set aside the dissolution. The petition must be served on the Department of State and contain a copy of the Department of State's declaration of dissolution, the company's application for reinstatement, and the Department of State's notice of rejection.

(c) The court may order the Department of State to reinstate a dissolved limited liability company or take other action the court considers appropriate.

#### **Comment**

**Source** – ULPA (2001) § 811, which was based on ULLCA § 812.

This section uses "rejection" rather than "denial" (the word used by both ULPA (2001)

and ULLCA). The change is to avoid confusion with a “statement of denial” under Section 302.

**SECTION 708. DISTRIBUTION OF ASSETS IN WINDING UP LIMITED LIABILITY COMPANY’S ACTIVITIES.**

(a) In winding up its activities, a limited liability company must apply its assets to discharge its obligations to creditors, including members that are creditors.

(b) After a limited liability company complies with subsection (a), any surplus must be distributed in the following order, subject to any charging order in effect under Section 503:

(1) to each person owning a transferable interest that reflects contributions made by a member and not previously returned, an amount equal to the value of the unreturned contributions; and

(2) in equal shares among members and dissociated members, except to the extent necessary to comply with any transfer effective under Section 502.

(c) If a limited liability company does not have sufficient surplus to comply with subsection (b)(1), any surplus must be distributed among the owners of transferable interests in proportion to the value of their respective unreturned contributions.

(d) All distributions made under subsections (b) and (c) must be paid in money.

**Comment**

**Source:** ULLCA § 806, restyled.

**Subsection (a)** – This section is mostly not a default rule. *See* Section 110(c)(11) (stating that “except as provided in Section 112(b), [the operating agreement may not] restrict the rights under this [act] of a person other than a member or manager”). However, if the creditors are willing, a dissolved limited liability company may certainly make agreements with them specifying the terms under which the LLC will “discharge its obligations to creditors.”

**Subsections (b), (c) and (d)** – These subsection provide default rules. Distributions under these subsections (or otherwise under the operating agreement) are subject to Section 503 (charging orders).

(17) [ARTICLE] 8

(18) FOREIGN LIMITED LIABILITY COMPANIES

**SECTION 801. GOVERNING LAW.**

(a) The law of the state or other jurisdiction under which a foreign limited liability company is formed governs:

(1) the internal affairs of the company; and

(2) the liability of a member as member and a manager as manager for the debts, obligations, or other liabilities of the company.

(b) A foreign limited liability company may not be denied a certificate of authority by reason of any difference between the law of the jurisdiction under which the company is formed and the law of this state.

(c) A certificate of authority does not authorize a foreign limited liability company to engage in any business or exercise any power that a limited liability company may not engage in or exercise in this state.

**Comment**

**Subsection (a)** – This Section parallels the formulation stated in Section 106 for a domestic limited liability company.

**Subsection (a)(2)** – This provision does not pertain to the “internal shields” of a foreign “series” LLC, because those shields do not concern the liability of members or managers for the obligations of the LLC. Instead, those shields seek to protect specified assets of the LLC (associated with one series) from being available to satisfy specified obligations of the LLC (associated with another series). See the Prefatory Note, *No Provision for “Series” LLCs*.

**SECTION 802. APPLICATION FOR CERTIFICATE OF AUTHORITY.**

(a) A foreign limited liability company may apply for a certificate of authority to transact business in this state by delivering an application to the Department of State for filing. The application must state:

(1) the name of the company and, if the name does not comply with Section 108, an alternate name adopted pursuant to Section 805(a);

(2) the name of the state or other jurisdiction under whose law the company is formed;



(3) the street and mailing addresses of the company's principal office and, if the law of the jurisdiction under which the company is formed require the company to maintain an office in that jurisdiction, the street and mailing addresses of the required office; and

(4) the name and street and mailing addresses of the company's initial agent for service of process in this state.

(b) A foreign limited liability company shall deliver with a completed application under subsection (a) a certificate of existence or a record of similar import signed by the Department of State or other official having custody of the company's publicly filed records in the state or other jurisdiction under whose law the company is formed.

### **Comment**

**Source** – ULPA (2001) § 902, which was based on ULLCA § 1002.

### **SECTION 803. ACTIVITIES NOT CONSTITUTING TRANSACTING BUSINESS.**

(a) Activities of a foreign limited liability company which do not constitute transacting business in this state within the meaning of this [article] include:

- (1) maintaining, defending, or settling an action or proceeding;
- (2) carrying on any activity concerning its internal affairs, including holding meetings of its members or managers;
- (3) maintaining accounts in financial institutions;
- (4) maintaining offices or agencies for the transfer, exchange, and registration of the company's own securities or maintaining trustees or depositories with respect to those securities;
- (5) selling through independent contractors;
- (6) soliciting or obtaining orders, whether by mail or electronic means or through employees or agents or otherwise, if the orders require acceptance outside this state before they become contracts;
- (7) creating or acquiring indebtedness, mortgages, or security interests in real or personal property;
- (8) securing or collecting debts or enforcing mortgages or other security interests in property securing the debts and holding, protecting, or maintaining property so acquired;
- (9) conducting an isolated transaction that is completed within 30 days and is not

in the course of similar transactions; and

(10) transacting business in interstate commerce.

(b) For purposes of this [article], the ownership in this state of income-producing real property or tangible personal property, other than property excluded under subsection (a), constitutes transacting business in this state.

(c) This section does not apply in determining the contacts or activities that may subject a foreign limited liability company to service of process, taxation, or regulation under law of this state other than this [act].

#### **Comment**

**Source** – ULPA (2001) § 903, which was based on ULLCA § 1003.

**SECTION 804. FILING OF CERTIFICATE OF AUTHORITY.** Unless the Department of State determines that an application for a certificate of authority does not comply with the filing requirements of this [act], the Department of State, upon payment of all filing fees, shall file the application of a foreign limited liability company, prepare, sign, and file a certificate of authority to transact business in this state, and send a copy of the filed certificate, together with a receipt for the fees, to the company or its representative.

#### **Comment**

**Source** – ULPA (2001) § 904, which was based on ULLCA § 1004 and RULPA § 903.

**SECTION 805. NONCOMPLYING NAME OF FOREIGN LIMITED LIABILITY COMPANY.**

(a) A foreign limited liability company whose name does not comply with Section 108 may not obtain a certificate of authority until it adopts, for the purpose of transacting business in this state, an alternate name that complies with Section 108. A foreign limited liability company that adopts an alternate name under this subsection and obtains a certificate of authority with the alternate name need not comply with [fictitious or assumed name statute]. After obtaining a certificate of authority with an alternate name, a foreign limited liability company shall transact business in this state under the alternate name unless the company is authorized under [fictitious or assumed name statute] to transact business in this state under another name.

(b) If a foreign limited liability company authorized to transact business in this state

changes its name to one that does not comply with Section 108, it may not thereafter transact business in this state until it complies with subsection (a) and obtains an amended certificate of authority.

#### **Comment**

**Source** – ULPA (2001) § 905, which was based on ULLCA § 1005.

#### **SECTION 806. REVOCATION OF CERTIFICATE OF AUTHORITY.**

(a) A certificate of authority of a foreign limited liability company to transact business in this state may be revoked by the Department of State in the manner provided in subsections (b) and (c) if the company does not:

- (1) pay, within 60 days after the due date, any fee, tax, or penalty due to the Department of State under this [act] or law other than this [act];
- (2) deliver, within 60 days after the due date, its annual report required under Section 209;
- (3) appoint and maintain an agent for service of process as required by Section 113(b); or
- (4) deliver for filing a statement of a change under Section 114 within 30 days after a change has occurred in the name or address of the agent.

(b) To revoke a certificate of authority of a foreign limited liability company, the Department of State must prepare, sign, and file a notice of revocation and send a copy to the company's agent for service of process in this state, or if the company does not appoint and maintain a proper agent in this state, to the company's designated office. The notice must state:

- (1) the revocation's effective date, which must be at least 60 days after the date the Department of State sends the copy; and
- (2) the grounds for revocation under subsection (a).

(c) The authority of a foreign limited liability company to transact business in this state ceases on the effective date of the notice of revocation unless before that date the company cures each ground for revocation stated in the notice filed under subsection (b). If the company cures each ground, the Department of State shall file a record so stating.

#### **Comment**

**Source** – ULPA (2001) § 906, which was based on ULLCA § 1006.

SECTION 807. CANCELLATION OF CERTIFICATE OF AUTHORITY. To cancel its certificate of authority to transact business in this state, a foreign limited liability company must deliver to the Department of State for filing a notice of cancellation stating the name of the company and that the company desires to cancel its certificate of authority. The certificate is canceled when the notice becomes effective.

SECTION 808. EFFECT OF FAILURE TO HAVE CERTIFICATE OF AUTHORITY.

(a) A foreign limited liability company transacting business in this state may not maintain an action or proceeding in this state unless it has a certificate of authority to transact business in this state.

(b) The failure of a foreign limited liability company to have a certificate of authority to transact business in this state does not impair the validity of a contract or act of the company or prevent the company from defending an action or proceeding in this state.

(c) A member or manager of a foreign limited liability company is not liable for the debts, obligations, or other liabilities of the company solely because the company transacted business in this state without a certificate of authority.

(d) If a foreign limited liability company transacts business in this state without a certificate of authority or cancels its certificate of authority, it appoints the Department of State as its agent for service of process for rights of action arising out of the transaction of business in this state.

**Comment**

**Source** – ULPA (2001) § 907, which was based on RULPA § 907(d) and ULLCA § 1008.

SECTION 809. ACTION BY [ATTORNEY GENERAL]. The [Attorney General] may maintain an action to enjoin a foreign limited liability company from transacting business in this state in violation of this [article].

**Comment**

**Source** – ULPA (2001) § 908, which was based on RULPA § 908 and ULLCA § 1009.

(19) [ARTICLE] 9

(20) ACTIONS BY MEMBERS

**SECTION 901. DIRECT ACTION BY MEMBER.**

(a) Subject to subsection (b), a member may maintain a direct action against another member, a manager, or the limited liability company to enforce the member's rights and otherwise protect the member's interests, including rights and interests under the operating agreement or this [act] or arising independently of the membership relationship.

(b) A member maintaining a direct action under this section must plead and prove an actual or threatened injury that is not solely the result of an injury suffered or threatened to be suffered by the limited liability company.

**Comment**

**Subsection (a)** – Source: ULPA (2001) § 1001(a), which was based on RUPA Section 405(b). The subsection has been somewhat re-styled from the ULPA version, and the phrase “for legal or equitable relief” has been deleted as unnecessary. ULPA’s reference to “with or without an accounting” has been deleted because the reference: (i) was to the partnership remedy of accounting, which reflected the aggregate nature of a partnership and is inapposite for an *entity* such as an LLC; and (ii) generated some confusion with the equitable claim for an accounting (in the nature of a constructive trust). The “entity-analog” to the partnership-as-aggregate notion of an accounting is the distinction between a direct and derivative claim.

The last phrase of this subsection (“or arising independently . . .”) comes from RUPA § 405(b)(3), does not create any new rights, obligations, or remedies, and is included merely to emphasize that a person’s membership in an LLC does not preclude the person from enforcing rights existing “independently or the membership relationship.”

**Subsection (b)** – Source: ULPA (2001) § 1001(b). The Comment to that subsection explains:

In ordinary contractual situations it is axiomatic that each party to a contract has standing to sue for breach of that contract. Within a limited partnership, however, different circumstances may exist. A partner does not have a direct claim against another partner merely because the other partner has breached the operating agreement. Likewise a partner’s violation of this Act does not automatically create a direct claim for every other partner. To have standing in his, her, or its own right, a partner plaintiff must be able to show a harm that occurs independently of the harm caused or threatened to be caused to the limited partnership.

SECTION 902. DERIVATIVE ACTION. A member may maintain a derivative action to enforce a right of a limited liability company if:

(1) the member first makes a demand on the other members in a member-managed limited liability company, or the managers of a manager-managed limited liability company, requesting that they cause the company to bring an action to enforce the right, and the managers or other members do not bring the action within a reasonable time; or

(2) a demand under paragraph (1) would be futile.

**Comment**

**Source** – ULPA (2001) § 1002, which was a re-styled version RULPA § 1001.

SECTION 903. PROPER PLAINTIFF.

(a) Except as otherwise provided in subsection (b), a derivative action under Section 902 may be maintained only by a person that is a member at the time the action is commenced and remains a member while the action continues.

(b) If the sole plaintiff in a derivative action dies while the action is pending, the court may permit another member of the limited liability company to be substituted as plaintiff.

**Comment**

This section abandons the traditional “contemporaneous ownership” rule, on the theory that the protections of that rule are unnecessary given the closely-held nature of most limited liability companies and the built-in, statutory restrictions on persons becoming members.

**Subsection (b)** – This subsection will be inapposite if the limited liability company has only two members, one of whom is the derivative plaintiff. In that limited circumstance, the plaintiff’s death would cause the derivative action to abate. The “pick your partner” principal enshrined in Section 502 would prevent the decedent’s heirs from succeeding to plaintiff status in the derivative action. This Act does not take a position on whether the death of member abates a direct claim against the LLC or a fellow member.

SECTION 904. PLEADING. In a derivative action under Section 902, the complaint must state with particularity:

(1) the date and content of plaintiff’s demand and the response to the demand by the managers or other members; or

(2) if a demand has not been made, the reasons a demand under Section 902(1) would be futile.

**Comment**

**Source** – ULPA (2001) § 1004, which was a re-styled version RULPA § 1003.

**SECTION 905. SPECIAL LITIGATION COMMITTEE.**

(a) If a limited liability company is named as or made a party in a derivative proceeding, the company may appoint a special litigation committee to investigate the claims asserted in the proceeding and determine whether pursuing the action is in the best interests of the company. If the company appoints a special litigation committee, on motion by the committee made in the name of the company, except for good cause shown, the court shall stay discovery for the time reasonably necessary to permit the committee to make its investigation. This subsection does not prevent the court from enforcing a person's right to information under Section 410 or, for good cause shown, granting extraordinary relief in the form of a temporary restraining order or preliminary injunction.

(b) A special litigation committee may be composed of one or more disinterested and independent individuals, who may be members.

(c) A special litigation committee may be appointed:

(1) in a member-managed limited liability company:

(A) by the consent of a majority of the members not named as defendants or plaintiffs in the proceeding; and

(B) if all members are named as defendants or plaintiffs in the proceeding, by a majority of the members named as defendants; or

(2) in a manager-managed limited liability company:

(A) by a majority of the managers not named as defendants or plaintiffs in the proceeding; and

(B) if all managers are named as defendants or plaintiffs in the proceeding, by a majority of the managers named as defendants.

(d) After appropriate investigation, a special litigation committee may determine that it is in the best interests of the limited liability company that the proceeding:

(1) continue under the control of the plaintiff;

(2) continue under the control of the committee;

(3) be settled on terms approved by the committee; or

(4) be dismissed.

(e) After making a determination under subsection (d), a special litigation committee shall file with the court a statement of its determination and its report supporting its determination, giving notice to the plaintiff. The court shall determine whether the members of the committee were disinterested and independent and whether the committee conducted its investigation and made its recommendation in good faith, independently, and with reasonable care, with the committee having the burden of proof. If the court finds that the members of the committee were disinterested and independent and that the committee acted in good faith, independently, and with reasonable care, the court shall enforce the determination of the committee. Otherwise, the court shall dissolve the stay of discovery entered under subsection (a) and allow the action to proceed under the direction of the plaintiff.

### Comment

Although special litigation committees are best known in the corporate field, they are no more inherently corporate than derivative litigation or the notion that an organization is a person distinct from its owners. An “SLC” can serve as an ADR mechanism, help protect an agreed upon arrangement from strike suits, protect the interests of members who are neither plaintiffs nor defendants (if any), and bring to any judicial decision the benefits of a specially tailored business judgment.

This section’s approach corresponds to established law in most jurisdictions, modified to fit the typical governance structures of a limited liability company.

**Subsection (a)** – On the availability of Section 410 remedies pending the SLC’s investigation, compare *Kaufman v. Computer Assoc. Int’l, Inc.*, No. Civ.A. 699-N, 2005 WL 3470589 at \*1 (Del.Ch. Dec. 21, 2005, as revised) (presenting “the question of whether to stay a books and records action under 8 Del. C. § 220 at the request of a special litigation committee when a derivative action encompassing substantially the same allegations of wrongdoing filed by different plaintiffs is pending in another jurisdiction;” concluding “[f]or reasons that have much to do with the light burden imposed by the plaintiff’s demand in this case . . . that the special litigation committee’s motion to stay the books and records action should be denied”)

**Subsection (d)** – The standard stated for judicial review of the SLC determination follows *Auerbach v. Bennett*, 47 N.Y.2d 619, 419 N.Y.S.2d 920 (N.Y. 1979) rather than *Zapata Corp. v. Maldonado*, 430 A.2d 779 (Del. 1981), because the latter’s reference to a court’s business judgment has generally not been followed in other states.

*Houle v. Low*, 407 Mass. 810, 822, 556 N.E.2d 51, 58 (Mass. 1990) contains an excellent explanation of the court’s role in reviewing an SLC decision:

The value of a special litigation committee is coextensive with the extent to which that committee truly exercises business judgment. In order to ensure that special litigation committees do act for the [entity]’s best interest, a good deal of judicial



oversight is necessary in each case. At the same time, however, courts must be careful not to usurp the committee's valuable role in exercising business judgment. . . . [A] special litigation committee must be independent, unbiased, and act in good faith. Moreover, such a committee must conduct a thorough and careful analysis regarding the plaintiff's derivative suit, ... The burden of proving that these procedural requirements have been met must rest, in all fairness, on the party capable of making that proof--the [entity].

For a discussion of how a court should approach the question of independence, *see Einhorn v. Culea*, 612 N.W.2d 78, 91 (Wis.2000).

#### SECTION 906. PROCEEDS AND EXPENSES.

(a) Except as otherwise provided in subsection (b):

(1) any proceeds or other benefits of a derivative action under Section 902, whether by judgment, compromise, or settlement, belong to the limited liability company and not to the plaintiff; and

(2) if the plaintiff receives any proceeds, the plaintiff shall remit them immediately to the company.

(b) If a derivative action under Section 902 is successful in whole or in part, the court may award the plaintiff reasonable expenses, including reasonable attorney's fees and costs, from the recovery of the limited liability company.

#### **Comment**

**Source** – ULPA (2001) § 1005, which was a re-styled version RULPA § 1004.

(21) [ARTICLE] 10

(22) MERGER, CONVERSION, AND DOMESTICATION

SECTION 1001. DEFINITIONS. In this [article]:

(1) “Constituent limited liability company” means a constituent organization that is a limited liability company.

(2) “Constituent organization” means an organization that is party to a merger.

(3) “Converted organization” means the organization into which a converting organization converts pursuant to Sections 1006 through 1009.

(4) “Converting limited liability company” means a converting organization that is a limited liability company.

(5) “Converting organization” means an organization that converts into another organization pursuant to Section 1006.

(6) “Domesticated company” means the company that exists after a domesticating foreign limited liability company or limited liability company effects a domestication pursuant to Sections 1010 through 1013.

(7) “Domesticating company” means the company that effects a domestication pursuant to Sections 1010 through 1013.

(8) “Governing statute” means the statute that governs an organization’s internal affairs.

(9) “Organization” means a general partnership, including a limited liability partnership, limited partnership, including a limited liability limited partnership, limited liability company, business trust, corporation, or any other person having a governing statute. The term includes a domestic or foreign organization regardless of whether organized for profit.

(10) “Organizational documents” means:

(A) for a domestic or foreign general partnership, its partnership agreement;

(B) for a limited partnership or foreign limited partnership, its certificate of limited partnership and partnership agreement;

(C) for a domestic or foreign limited liability company, its certificate or articles of organization and operating agreement, or comparable records as provided in its governing statute;

(D) for a business trust, its agreement of trust and declaration of trust;

(E) for a domestic or foreign corporation for profit, its articles of incorporation, bylaws, and other agreements among its shareholders which are authorized by its governing statute, or comparable records as provided in its governing statute; and

(F) for any other organization, the basic records that create the organization and determine its internal governance and the relations among the persons that own it, have an interest in it, or are members of it.

(11) “Personal liability” means liability for a debt, obligation, or other liability of an organization which is imposed on a person that co-owns, has an interest in, or is a member of the organization:

(A) by the governing statute solely by reason of the person co-owning, having an interest in, or being a member of the organization; or

(B) by the organization’s organizational documents under a provision of the governing statute authorizing those documents to make one or more specified persons liable for all or specified debts, obligations, or other liabilities of the organization solely by reason of the person or persons co-owning, having an interest in, or being a member of the organization.

(12) “Surviving organization” means an organization into which one or more other organizations are merged whether the organization preexisted the merger or was created by the merger.

### **Comment**

This article is based on Article 11 of ULPA (2001) and differs principally in treating domestications as a separate type of organic transaction rather than as a subset of conversions.

#### **SECTION 1002. MERGER.**

(a) A limited liability company may merge with one or more other constituent organizations pursuant to this section, Sections 1003 through 1005, and a plan of merger, if:

(1) the governing statute of each of the other organizations authorizes the merger;

(2) the merger is not prohibited by the law of a jurisdiction that enacted any of the governing statutes; and

(3) each of the other organizations complies with its governing statute in effecting the merger.

(b) A plan of merger must be in a record and must include:

- (1) the name and form of each constituent organization;
- (2) the name and form of the surviving organization and, if the surviving organization is to be created by the merger, a statement to that effect;
- (3) the terms and conditions of the merger, including the manner and basis for converting the interests in each constituent organization into any combination of money, interests in the surviving organization, and other consideration;
- (4) if the surviving organization is to be created by the merger, the surviving organization's organizational documents that are proposed to be in a record; and
- (5) if the surviving organization is not to be created by the merger, any amendments to be made by the merger to the surviving organization's organizational documents that are, or are proposed to be, in a record.

**SECTION 1003. ACTION ON PLAN OF MERGER BY CONSTITUENT LIMITED LIABILITY COMPANY.**

(a) Subject to Section 1014, a plan of merger must be consented to by all the members of a constituent limited liability company.

(b) Subject to Section 1014 and any contractual rights, after a merger is approved, and at any time before articles of merger are delivered to the Department of State for filing under Section 1004, a constituent limited liability company may amend the plan or abandon the merger:

- (1) as provided in the plan; or
- (2) except as otherwise prohibited in the plan, with the same consent as was required to approve the plan.

**SECTION 1004. FILINGS REQUIRED FOR MERGER; EFFECTIVE DATE.**

(a) After each constituent organization has approved a merger, articles of merger must be signed on behalf of:

- (1) each constituent limited liability company, as provided in Section 203(a); and
- (2) each other constituent organization, as provided in its governing statute.

(b) Articles of merger under this section must include:

- (1) the name and form of each constituent organization and the jurisdiction of its governing statute;
- (2) the name and form of the surviving organization, the jurisdiction of its

governing statute, and, if the surviving organization is created by the merger, a statement to that effect;

(3) the date the merger is effective under the governing statute of the surviving organization;

(4) if the surviving organization is to be created by the merger:

(A) if it will be a limited liability company, the company's certificate of organization; or

(B) if it will be an organization other than a limited liability company, the organizational document that creates the organization that is in a public record;

(5) if the surviving organization preexists the merger, any amendments provided for in the plan of merger for the organizational document that created the organization that are in a public record;

(6) a statement as to each constituent organization that the merger was approved as required by the organization's governing statute;

(7) if the surviving organization is a foreign organization not authorized to transact business in this state, the street and mailing addresses of an office that the Department of State may use for the purposes of Section 1005(b); and

(8) any additional information required by the governing statute of any constituent organization.

(c) Each constituent limited liability company shall deliver the articles of merger for filing with the Department of State.

(d) A merger becomes effective under this [article]:

(1) if the surviving organization is a limited liability company, upon the later of:

(A) compliance with subsection (c); or

(B) subject to Section 205(c), as specified in the articles of merger; or

(2) if the surviving organization is not a limited liability company, as provided by the governing statute of the surviving organization.

#### **SECTION 1005. EFFECT OF MERGER.**

(a) When a merger becomes effective:

(1) the surviving organization continues or comes into existence;

(2) each constituent organization that merges into the surviving organization

ceases to exist as a separate entity;

(3) all property owned by each constituent organization that ceases to exist vests in the surviving organization;

(4) all debts, obligations, or other liabilities of each constituent organization that ceases to exist continue as debts, obligations, or other liabilities of the surviving organization;

(5) an action or proceeding pending by or against any constituent organization that ceases to exist may be continued as if the merger had not occurred;

(6) except as prohibited by other law, all of the rights, privileges, immunities, powers, and purposes of each constituent organization that ceases to exist vest in the surviving organization;

(7) except as otherwise provided in the plan of merger, the terms and conditions of the plan of merger take effect; and

(8) except as otherwise agreed, if a constituent limited liability company ceases to exist, the merger does not dissolve the limited liability company for the purposes of [Article] 7;

(9) if the surviving organization is created by the merger:

(A) if it is a limited liability company, the certificate of organization becomes effective; or

(B) if it is an organization other than a limited liability company, the organizational document that creates the organization becomes effective; and

(10) if the surviving organization preexisted the merger, any amendments provided for in the articles of merger for the organizational document that created the organization become effective.

(b) A surviving organization that is a foreign organization consents to the jurisdiction of the courts of this state to enforce any debt, obligation, or other liability owed by a constituent organization, if before the merger the constituent organization was subject to suit in this state on the debt, obligation, or other liability. A surviving organization that is a foreign organization and not authorized to transact business in this state appoints the Department of State as its agent for service of process for the purposes of enforcing a debt, obligation, or other liability under this subsection. Service on the Department of State under this subsection must be made in the same manner and has the same consequences as in Section 116(c) and (d).

#### SECTION 1006. CONVERSION.

(a) An organization other than a limited liability company or a foreign limited liability company may convert to a limited liability company, and a limited liability company may convert to an organization other than a foreign limited liability company pursuant to this section, Sections 1007 through 1009, and a plan of conversion, if:

- (1) the other organization's governing statute authorizes the conversion;
- (2) the conversion is not prohibited by the law of the jurisdiction that enacted the other organization's governing statute; and
- (3) the other organization complies with its governing statute in effecting the conversion.

(b) A plan of conversion must be in a record and must include:

- (1) the name and form of the organization before conversion;
- (2) the name and form of the organization after conversion;
- (3) the terms and conditions of the conversion, including the manner and basis for converting interests in the converting organization into any combination of money, interests in the converted organization, and other consideration; and
- (4) the organizational documents of the converted organization that are, or are proposed to be, in a record.

#### **SECTION 1007. ACTION ON PLAN OF CONVERSION BY CONVERTING LIMITED LIABILITY COMPANY.**

(a) Subject to Section 1014, a plan of conversion must be consented to by all the members of a converting limited liability company.

(b) Subject to Section 1014 and any contractual rights, after a conversion is approved, and at any time before articles of conversion are delivered to the Department of State for filing under Section 1008, a converting limited liability company may amend the plan or abandon the conversion:

- (1) as provided in the plan; or
- (2) except as otherwise prohibited in the plan, by the same consent as was required to approve the plan.

#### **SECTION 1008. FILINGS REQUIRED FOR CONVERSION; EFFECTIVE DATE.**

(a) After a plan of conversion is approved:

- (1) a converting limited liability company shall deliver to the Department of State

for filing articles of conversion, which must be signed as provided in Section 203(a) and must include;

(A) a statement that the limited liability company has been converted into another organization;

(B) the name and form of the organization and the jurisdiction of its governing statute;

(C) the date the conversion is effective under the governing statute of the converted organization;

(D) a statement that the conversion was approved as required by this [act];

(E) a statement that the conversion was approved as required by the governing statute of the converted organization; and

(F) if the converted organization is a foreign organization not authorized to transact business in this state, the street and mailing addresses of an office which the Department of State may use for the purposes of Section 1009(c); and

(2) if the converting organization is not a converting limited liability company, the converting organization shall deliver to the Department of State for filing a certificate of organization, which must include, in addition to the information required by Section 201(b):

(A) a statement that the converted organization was converted from another organization;

(B) the name and form of that converting organization and the jurisdiction of its governing statute; and

(C) a statement that the conversion was approved in a manner that complied with the converting organization's governing statute.

(b) A conversion becomes effective:

(1) if the converted organization is a limited liability company, when the certificate of organization takes effect; and

(2) if the converted organization is not a limited liability company, as provided by the governing statute of the converted organization.

#### SECTION 1009. EFFECT OF CONVERSION.

(a) An organization that has been converted pursuant to this [article] is for all purposes the same entity that existed before the conversion.



(b) When a conversion takes effect:

(1) all property owned by the converting organization remains vested in the converted organization;

(2) all debts, obligations, or other liabilities of the converting organization continue as debts, obligations, or other liabilities of the converted organization;

(3) an action or proceeding pending by or against the converting organization may be continued as if the conversion had not occurred;

(4) except as prohibited by law other than this [act], all of the rights, privileges, immunities, powers, and purposes of the converting organization remain vested in the converted organization;

(5) except as otherwise provided in the plan of conversion, the terms and conditions of the plan of conversion take effect; and

(6) except as otherwise agreed, the conversion does not dissolve a converting limited liability company for the purposes of [Article] 7.

(c) A converted organization that is a foreign organization consents to the jurisdiction of the courts of this state to enforce any debt, obligation, or other liability for which the converting limited liability company is liable if, before the conversion, the converting limited liability company was subject to suit in this state on the debt, obligation, or other liability. A converted organization that is a foreign organization and not authorized to transact business in this state appoints the Department of State as its agent for service of process for purposes of enforcing a debt, obligation, or other liability under this subsection. Service on the Department of State under this subsection must be made in the same manner and has the same consequences as in Section 116(c) and (d).

#### SECTION 1010. DOMESTICATION.

(a) A foreign limited liability company may become a limited liability company pursuant to this section, Sections 1011 through 1013, and a plan of domestication, if:

(1) the foreign limited liability company's governing statute authorizes the domestication;

(2) the domestication is not prohibited by the law of the jurisdiction that enacted the governing statute; and

(3) the foreign limited liability company complies with its governing statute in

effecting the domestication.

(b) A limited liability company may become a foreign limited liability company pursuant to this section, Sections 1011 through 1013, and a plan of domestication, if:

(1) the foreign limited liability company's governing statute authorizes the domestication;

(2) the domestication is not prohibited by the law of the jurisdiction that enacted the governing statute; and

(3) the foreign limited liability company complies with its governing statute in effecting the domestication.

(c) A plan of domestication must be in a record and must include:

(1) the name of the domesticating company before domestication and the jurisdiction of its governing statute;

(2) the name of the domesticated company after domestication and the jurisdiction of its governing statute;

(3) the terms and conditions of the domestication, including the manner and basis for converting interests in the domesticating company into any combination of money, interests in the domesticated company, and other consideration; and

(4) the organizational documents of the domesticated company that are, or are proposed to be, in a record.

#### SECTION 1011. ACTION ON PLAN OF DOMESTICATION BY DOMESTICATING LIMITED LIABILITY COMPANY.

(a) A plan of domestication must be consented to:

(1) by all the members, subject to Section 1014, if the domesticating company is a limited liability company; and

(2) as provided in the domesticating company's governing statute, if the company is a foreign limited liability company.

(b) Subject to any contractual rights, after a domestication is approved, and at any time before articles of domestication are delivered to the Department of State for filing under Section 1012, a domesticating limited liability company may amend the plan or abandon the domestication:

(1) as provided in the plan; or

(2) except as otherwise prohibited in the plan, by the same consent as was required to approve the plan.

**SECTION 1012. FILINGS REQUIRED FOR DOMESTICATION; EFFECTIVE DATE.**

(a) After a plan of domestication is approved, a domesticating company shall deliver to the Department of State for filing articles of domestication, which must include:

(1) a statement, as the case may be, that the company has been domesticated from or into another jurisdiction;

(2) the name of the domesticating company and the jurisdiction of its governing statute;

(3) the name of the domesticated company and the jurisdiction of its governing statute;

(4) the date the domestication is effective under the governing statute of the domesticated company;

(5) if the domesticating company was a limited liability company, a statement that the domestication was approved as required by this [act];

(6) if the domesticating company was a foreign limited liability company, a statement that the domestication was approved as required by the governing statute of the other jurisdiction; and

(7) if the domesticated company was a foreign limited liability company not authorized to transact business in this state, the street and mailing addresses of an office that the Department of State may use for the purposes of Section 1013(b).

(b) A domestication becomes effective:

(1) when the certificate of organization takes effect, if the domesticated company is a limited liability company; and

(2) according to the governing statute of the domesticated company, if the domesticated organization is a foreign limited liability company.

**SECTION 1013. EFFECT OF DOMESTICATION.**

(a) When a domestication takes effect:

(1) the domesticated company is for all purposes the company that existed before the domestication;

(2) all property owned by the domesticating company remains vested in the

domesticated company;

(3) all debts, obligations, or other liabilities of the domesticating company continue as debts, obligations, or other liabilities of the domesticated company;

(4) an action or proceeding pending by or against a domesticating company may be continued as if the domestication had not occurred;

(5) except as prohibited by other law, all of the rights, privileges, immunities, powers, and purposes of the domesticating company remain vested in the domesticated company;

(6) except as otherwise provided in the plan of domestication, the terms and conditions of the plan of domestication take effect; and

(7) except as otherwise agreed, the domestication does not dissolve a domesticating limited liability company for the purposes of [Article] 7.

(b) A domesticated company that is a foreign limited liability company consents to the jurisdiction of the courts of this state to enforce any debt, obligation, or other liability owed by the domesticating company, if, before the domestication, the domesticating company was subject to suit in this state on the debt, obligation, or other liability. A domesticated company that is a foreign limited liability company and not authorized to transact business in this state appoints the Department of State as its agent for service of process for purposes of enforcing a debt, obligation, or other liability under this subsection. Service on the Department of State under this subsection must be made in the same manner and has the same consequences as in Section 116(c) and (d).

(c) If a limited liability company has adopted and approved a plan of domestication under Section 1010 providing for the company to be domesticated in a foreign jurisdiction, a statement surrendering the company's certificate of organization must be delivered to the Department of State for filing setting forth:

(1) the name of the company;

(2) a statement that the certificate of organization is being surrendered in connection with the domestication of the company in a foreign jurisdiction;

(3) a statement the domestication was approved as required by this [act]; and

(4) the jurisdiction of formation of the domesticated foreign limited liability company.

SECTION 1014. RESTRICTIONS ON APPROVAL OF MERGERS, CONVERSIONS, AND DOMESTICATIONS.

(a) If a member of a constituent, converting, or domesticating limited liability company will have personal liability with respect to a surviving, converted, or domesticated organization, approval or amendment of a plan of merger, conversion, or domestication are ineffective without the consent of the member, unless:

(1) the company's operating agreement provides for approval of a merger, conversion, or domestication with the consent of fewer than all the members; and

(2) the member has consented to the provision of the operating agreement.

(b) A member does not give the consent required by subsection (a) merely by consenting to a provision of the operating agreement that permits the operating agreement to be amended with the consent of fewer than all the members.

SECTION 1015. [ARTICLE] NOT EXCLUSIVE. This [article] does not preclude an entity from being merged, converted, or domesticated in compliance with the applicable law of another state or other applicable law of this State.

(23) [ARTICLE] 11

(24) MISCELLANEOUS PROVISIONS

SECTION 1101. UNIFORMITY OF APPLICATION AND CONSTRUCTION. In applying and construing this uniform act, consideration must be given to the need to promote uniformity of the law with respect to its subject matter among states that enact it.

SECTION 1102. RELATION TO ELECTRONIC SIGNATURES IN GLOBAL AND NATIONAL COMMERCE ACT. This [act] modifies, limits, and supersedes the federal Electronic Signatures in Global and National Commerce Act, 15 U.S.C. Section 7001 et seq., but does not modify, limit, or supersede Section 101(c) of that act, 15 U.S.C. Section 7001(c), or authorize electronic delivery of any of the notices described in Section 103(b) of that act, 15 U.S.C. Section 7003(b).

SECTION 1103. SAVINGS CLAUSE. This [act] does not affect an action commenced, proceeding brought, or right accrued before this [act] takes effect.

SECTION 1104. APPLICATION TO EXISTING RELATIONSHIPS.

(a) Before [all-inclusive date], this [act] governs only:

(1) a limited liability company formed on or after [the effective date of this act];

and

(2) except as otherwise provided in subsection (c), a limited liability company formed before [the effective date of this act] which elects, in the manner provided in its operating agreement or by law for amending the operating agreement, to be subject to this [act].

(b) Except as otherwise provided in subsection (c), on and after [all-inclusive date] this [act] governs all limited liability companies.

(c) For the purposes applying this [act] to a limited liability company formed before [the effective date of this act]:

(1) the company's articles of organization are deemed to be the company's certificate of organization; and

(2) for the purposes of applying Section 102(10) and subject to Section 112(d), language in the company's articles of organization designating the company's management structure operates as if that language were in the operating agreement.

**Legislative Note:** *It is recommended that the “all-inclusive” date should be at least one year after the date of enactment but no longer than two years.*

*Each enacting jurisdiction should consider whether: (i) this Act makes material changes to the “default” (or “gap filler”) rules of jurisdiction’s predecessor statute; and (ii) if so, whether subsection (c) should carry forward any of those rules for pre-existing limited liability companies. In this assessment, the focus is on pre-existing limited liability companies that have left default rules in place, whether advisedly or not. The central question is whether, for such limited liability companies, expanding subsection (c) is necessary to prevent material changes to the members’ “deal.”*

*For an example of this type of analysis in the context of another business entity act, see the Uniform Limited Partnership Act (2001), § 1206(c).*

*Section 301 (de-codifying statutory apparent authority) does not require any special transition provisions, because: (i) applying the law of agency, as explained in the Comments to Sections 301 and 407, will produce appropriate results; and (ii) the notion of “lingering apparent authority” will protect any third party that has previously relied on the statutory apparent authority of a member of a particular member-managed LLC or a manager of a particular manager-managed LLC. RESTATEMENT (THIRD) OF AGENCY § 3.11, cmt. c (2006).*

*It is unnecessary to expand subsection (c) of this Act if the state’s predecessor act is the original Uniform Limited Liability Company Act, revised to provide for perpetual duration.*

### **Comment**

**Subsection (c)** – When a pre-existing limited liability company becomes subject to this Act, the company ceases to be governed by the predecessor act, including whatever requirements that act might have imposed for the contents of the articles of organization.

SECTION 1105. REPEALS. Effective [all-inclusive date], the following acts and parts of acts are repealed: [the state limited liability company act, as amended, and in effect immediately before the effective date of this act].

SECTION 1106. EFFECTIVE DATE. This [act] takes effect on . . . .