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FROM THE CHAIR

Christina Houston
DLA Piper LLP
Wilmington, Delaware

Greetings from the Chair,

There are several people who are responsible for my being here today. Each of them who knows me knows how deeply appreciative I am for this opportunity and that I will not take one day of this position for granted.

Our Committee’s strengths are our foundation: the giants in this field are the backbone of this group, and our substance is unmatched. How do we build upon that in order to create the greatest value proposition for each of us in what we are doing each day?

First, we ground ourselves in our foundation. Our Committee’s greatest treasure is our wealth of knowledge and the legends who walk among us and the few who have gone before us. We need one centralized location to showcase their great works; provide a platform for our future writers to demonstrate their contributions; and establish the Committee as the comprehensive authority on LLCs, partnerships and unincorporated entities. We are creating a Committee library and resource center which Committee members easily can access at any time. Stay tuned for more information. If you are interested in being a part of this project, please contact me (christina.houston@dlapiper.com) or Johnny Lyle (johnny@ljlawllc.com).

Second, we help each other and, in doing so, we help ourselves. The Committee List Serve is an open conversation line among friends facing similar questions and challenges
that you confront each day. I challenge you to find a more helpful and friendly group of people than members of this Committee. There are no dumb questions. If you prefer, I am happy to post your questions and comments anonymously. We will archive List Serve conversations by topic on the Committee library and resource center for future reference. I encourage you to take advantage of this resource.

Third, we create opportunities where none exist. We are the lawyers who create unprecedented paths for clients. This Committee is an opportunity for you, and we only are limited by a lack of creativity as to your involvement in a way that is most meaningful to you.

Fourth, we welcome everyone everywhere in the Committee, without exception. I promise each and every person taking the time to read this message that you belong wherever you want to be in this Committee. I do not know a single person on this Committee who disagrees with that statement. THAT is one of the intangibles of this Committee. I have nothing to add to this strength, other than to make sure that new members in particular know that is who we are and what we do. We not only say the words. We live them.

Fifth, we save front-row seats for law students and “younger” lawyers. If you are fortunate enough to get the added benefit of just one person ahead of you on this path who gives you what even might seem like the smallest opportunity at that moment, seize it and turn it into the biggest thing possible for you. That is why those of us are here ahead of you on this path. We never have forgotten who blazed a path for us once. I would not be here personally or professionally without someone in this Section once giving me a shot, and without someone in this Committee once telling me that he supported my path without exception. Opportunities that are meaningful to you are available to you in this Committee.

We have many ideas and projects in the works. What else would be helpful to you? Please let me (christina.houston@dlapiper.com), Johnny Lyle (johnny@ljlawllc.com), or Tom Rutledge (thomas.rutledge@skofirm.com) know what would help you in your practice.

Thank you, Christina

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**2019 Amendments to the Kansas LLC Act**

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**Messler v. Cotz**

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**2019 Amendments to Delaware’s General Corporation Law and Alternative Entity Statutes**

By: Norman M. Powell, John J. Paschetto and Tammy L. Mercer

**Wisconsin District Court Finds LLC Minority Owners Owe No Common Law Duties to Majority Members**

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**Wisconsin Supreme Court Concludes Wisconsin’s LLC Act Does Not Preempt Common Law Claims**

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**What If There The Parties Cannot Agree On an Operating Agreement – Why Not Claim A General Partnership Was Formed Instead – Did Not Work This Time**

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Christina Houston - Chair
Thomas E. Rutledge – Editor
Peter D. Hutcheon - Editor Emeritus
2019 LLC Institute
November 7-8, 2019
Agenda

**Wednesday, November 6, 2019**

5:30 p.m. – 7:00 p.m.  **Welcome Reception at Holland & Knight, LLP**

100 N Tampa St #4100, Tampa, Florida 33602

The Welcome Reception is made possible by the generous support of Holland & Knight, LLP

*(Through the registration page, please indicate whether you will attend, number of guests, etc.)*

**Thursday, November 7, 2019**

7:20 a.m. - 8:00 a.m.  Breakfast (included in registration)

8:00 a.m. - 8:15 a.m.  Welcome; Housekeeping

8:15 a.m. - 10:15 a.m.  **Program (2 hrs.) Case Law Update (Non-Delaware)**

Prof. Elizabeth “Beth” Miller (Baylor Law School, Waco, Texas); Kelley Bender (Chapman & Cutler, Chicago, Illinois); Sean Ducharme (Hunton Andrews Kurth LLP, Richmond, Virginia); Dan Sheridan (Stark & Stark, Lawrenceville, New Jersey)

*This panel will discuss recent LLC and partnership cases other than from Delaware on various topics of significance, including cases dealing with fiduciary duties and veil piercing and cases illustrating pitfalls in drafting operating agreements.*

10:15 a.m. - 10:30 a.m.  Break
10:30 a.m. - 12:00 p.m.  **Program (1.5 hrs.) Delaware Case Law Update**

Lou Hering (Morris, Nichols, Arsht & Tunnell LLP, Wilmington, Delaware); Tammy Mercer (Young Conaway Stargatt & Taylor, LLP, Wilmington, Delaware); Prof. James J. Wheaton (Boston University School of Law, Boston, Massachusetts)

This panel will discuss recent LLC and partnership cases from Delaware on various topics of significance, including cases dealing with fiduciary duties, the implied covenant, dissolution, application of the void and voidable doctrine and cases illustrating issues arising in drafting operating agreements. Jim Wheaton will provide an update on recent bankruptcy decisions of interest.

12:15 p.m. - 1:30 p.m.  **Luncheon & Keynote Address** (included in registration)

Keynote Address by Donald J. Weidner, Dean Emeritus and Alumni Centennial Professor at Florida State University College of Law and Reporter on the Revised Uniform Partnership Act (1994)

1:30 p.m. - 3:30 p.m.  **Program (2 hrs.) Contribution Default Remedies in LLC Operating Agreements**

Prof. Bradley T. Borden (Brooklyn Law), Michael D. Soejoto (Pircher, Nichols & Meeks LLP, Los Angeles, California)

This panel will discuss the economic, tax, and legal aspects of contribution-default remedies, which often appear in LLC operating agreements. Such remedies include member-to-member loans, member-to-entity loans, interest dilution, and distribution offsets. Some agreement mix and match remedies. The economic and tax effects of contribution-default remedies can vary significantly from remedy to remedy. The dilutive effect can be either natural or punitive and latent or patent. Despite the ubiquity of such remedies, they have received relatively little attention in commentary or seminars. Although contribution-default remedies appear to be drafted with hopeful prospects of profitability in mind, the few cases that have considered their legal effect relate to failed arrangements. This panel will also discuss those cases and drafting ideas that can addresses the legal doctrines that emerged from the case law.

3:30 p.m. – 3:45p.m.  Break
3:45 p.m. - 5:45 p.m. **Program (2 hrs.) LLC Agreements That Went Wrong, and How to Fix Them: Case Studies and War Stories**

Peter A. Mahler (Farrell Fritz, P.C., New York, New York); Ladd Hirsch (Winstead, Dallas, Texas); Prof. Meredith R. Miller (Touro Law, Central Islip, New York, New York); Louis T.M. Conti (Holland & Knight LLP, Tampa, Florida)

This panel will examine recent case law involving LLC member disputes involving interpretation of operating agreement provisions which were not carefully considered, properly drafted, or which resulted from unequal leverage; as well as how the panel members have addressed those issues in counseling their clients, including a few war stories from the trenches.

7:00 p.m. - 8:00 p.m. **Cocktail Hour**

8:00 p.m. - 10:00 p.m. **Lubaroff Award Dinner** - (ticket price included in registration)

**Friday, November 8, 2019**

7:30 a.m. - 8:00 a.m. Breakfast (included in registration)

8:00 a.m. – 9:15 a.m. **Program (1.25 hrs.) Re-Imagining the Business Trust as a Sustainable Business Form**

Prof. Lee-ford Tritt (University of Florida College of Law); Prof. Peter Molk (University of Florida College of Law)

By drawing upon trust law and corporate law, this program will articulate and discuss an interdisciplinary, systematic application of business trusts as an alternative organizational form to corporations for the socially-conscious business management construct.

9:15 a.m. – 10:45 a.m. **Program (1.5 hrs.) Federal and State Tax Issues Relating to Compensation and Pass-Through Entities**

Cristin C. Keane (Carlton Fields, P.A., Tampa, Florida); Prof. Gregg Polsky (Univ. of Georgia, Athens, Georgia); Warren P. Kean (Shumaker, Loop & Kendrick, LLP, Charlotte, NC)

This panel will discuss the current state of taxation of service providers to pass-through entities, including choice of entity issues, incentive compensation structures, equity-based compensation, carried interests, treatment of LLC members as limited partners for self-employment tax purposes, Section 83, and Section 409A.
10:45 a.m. – 11:00 a.m. Break

11:00 a.m. – 1:00 p.m. **Program (2.0 hrs.) Ethics**

A.J. Singleton (Stoll Keenon Ogden PLLC, Lexington, Kentucky); Robert R. Keatinge (Holland & Hart LLP, Denver, Colorado); Gerald V. Niesar (Niesar & Vestal LLP, San Francisco, California)

*This program will address a lawyer practicing in a law firm has duties to clients, partners, and self that must be balanced. These relationships and interests are governed not only by the law of the particular entity, but also very much by the Rules of Professional Responsibility. This program will consider the interaction of the ethical, professional liability, and business law rules to which attorneys who practice as partners or members of a law firm face in the organization, operation and dismemberment of a law firm. Among the topics that will be discussed are balancing fiduciary duties to clients with fiduciary duties to partners, the ethical considerations attendant to novel relationships within the firm such as the non-equity partner, non-lawyer time keepers, issues surrounding dissociation from, and dissolution and merger of, a law firm.*

1:00 p.m. - 1:30 p.m. **Luncheon: Working Committee Meeting (included in registration)**

1:30 p.m. - 2:30 p.m. **Program (1.0 hrs.) The Lightning Round**

Professor Christine Hurt (Brigham Young University, Provo, Utah); Scott E. Ludwig (Bradley Arant Boult Cummings LLP, Huntsville, Alabama); Suzanne C. Odom (Montgomery & Andrews, PA, Santa Fe, New Mexico); Stuart L. Pachman (Brach Eichler LLC, Roseland, New Jersey); Thomas E. Rutledge (Stoll Keenon Ogden PLLC, Louisville, Kentucky)

*This lightning round panel will address a variety of topics, each presenter spending no more than 10 minutes on a discrete recent development or issue. For example, Stuart Pachman will address his recent article on succession in single-member LLCs, Suzanne Odom will address LLCs formed under Tribal Laws, and Tom Rutledge will address recent developments in diversity jurisdiction and unincorporated entities.*

2:30 p.m. – 2:45 p.m. Break
2:45 p.m. – 4:15 p.m. **Program (1.5 hrs.) Developments in Series LLC’s, Divisions and Other Organic Transactions**

Tarik Haskins (Morris, Nichols, Arsht & Tunnell LLP, Wilmington, Delaware); Marla Norton (Bayard, P.A., Wilmington, Delaware); Prof. Elizabeth “Beth” Miller (Baylor Law School, Waco, Texas)

This program will examine recent amendments to the Delaware LLC Act regarding series LLCs and panelists will discuss some of the issues confronted by practitioners in using series LLCs and how practitioners can draft provisions in their LLC Agreement to improve the likelihood that the applicable horizontal liability shield will be respected outside of the jurisdiction of formation of the series LLC.

4:15 p.m. - 4:30 p.m. **Wrap-Up**
Daniel S. Kleinberger to Receive the 2019 Marin I. Lubaroff Award

Professor Daniel S. Kleinberger, emeritus from Mitchell Hamline School of Law and previously with the William Mitchell College of Law, is the 2019 recipient of the Martin I. Lubaroff Award.

Holding an undergraduate degree from Harvard and his law degree from Yale, Dan began his legal career in the office of the Attorney General for the State of Minnesota. From there he transferred to the office of the Office of the General Counsel of 3M. In 1986 he joined Mitchell Hamline School of Law where he taught for the next 29 years, taking emeritus status in 2015.

At the risk of leaving something off, Dan has served as:

- Reporter, Uniform Law Conference Drafting Committee on Series of Unincorporated Business Entities (2012);
- Consensual Special Master, State of Minnesota Conciliation Court Appeals Alternative Dispute Resolution Channel (2012);
- Chair, Task Force of the ABA LLC Committee (Business Law Section) to review the Uniform Power of Attorney Act and the Uniform Power of Appointment Act (2012-);
- Co-Reporter, Uniform Law Commissioners – Drafting Committee to Harmonize the Unincorporated Business Entity Acts;
- Co-Reporter, Revised Uniform Limited Liability Company Act of the National Conference of Commissioners on Uniform State Laws, (2003);
- Reporter, Uniform Limited Partnership Act (2001) of the National Conference of Commissioners on Uniform State Laws (1997-2001);
- Member, American Law Institute;
- Member, ALI Members Consultative Group for the Restatement (Third) of Agency;
- ABA Business Law Section Advisor to the NCCUSL-ABA Omnibus Organization Code Study Committee (2005);
- Chair, American Association of Law Schools Section on Agency, Partnerships, LLCs and Unincorporated Business Associations (2007);
- Referee, Ramsey County Conciliation Court; Member, Executive Council, Business Law Section, Minnesota State Bar Assn.;
- Reporter, Minnesota State Bar Assn. Joint Committee on the Minnesota Limited Liability Company Act (1991-92) and Amendments (1993, 1999);
- Reporter, Minnesota Limited Liability Partnership Provisions (1994) and Amendments (1995);
- Reporter, Chapter 319B Task Force of the Business Law Section of the Minnesota State Bar Assn. (1996-97);
- Chair, Minnesota State Bar Assn. Joint Task Force on the Model Entity Transactions Act (2006-).

At its 2018 annual meeting, Dan was recognized by the Uniform Laws Comission for his contributions to numerous unincorporated business organization acts.

Dan is co-author of Bishop and Kleinberger on LLCs, and he is as well the author of the Aspen student treatise Agency, Partnerships and Limited Liability Companies: Tax and Business Law.
Dan has written innumerable law review and shorter articles, the best-known of which is likely *The Plight of the Bare Naked Assignee*, XLII Suffolk L. Rev. 587 (2009).

Dan has participated in a numerable of our Committee’s meetings, our CLE and other programs, and in our various webinars. He as well devoted significant effort to the drafting of the Committee’s hugely successful LLC Organizational Checklist.

Carter Bishop writes:

Dan and I met pursuing our mutual interest in legal education, mine in 1984 and his in 1985. Our mutual interest in business and commercial law filled a deeper interest in debate and discussion that remains with us to this day. In the late 1980s our dean, and mutual friend Jim Hogg requested we join forces and lead an effort to form a state wide consensus committee of legal educators, lawyers, and government officials. Our committee task was to draft an LLC Act for Minnesota. We acted as joint reporters drafting, discussing, advising until we arrived at a final draft. We took it to the state legislature, offered supporting testimony, and eventually watched as the final bill was signed by the governor in our presence. It was thrilling. Not long thereafter we convinced Warren, Gotham and Lamont to publish our LLC treatise and another multi-year journey was underway. Work with the ABA, meeting new friends, and work as reporters on various partnership and LLC uniform acts kept us linked in an intellectual vineyard where we both enjoyed the labor and its fruits. Through it all, Dan and Carrie, his very talented painter spouse, have become best friends to Margaret and I. A journey ben in work has continued in work and blossomed into a lifelong friendship. There is no colleague who I value more, in life or in work. It will continue that way and in the end, it is I who have been enriched by the greatest gift of all - a lifelong friend.

Carter Bishop writes:

Lou Conti writes:

What can one say about Dan Kleinberger? Well, for starters, he married above his station! Carrie Sachs Kleinberger, Esq. and artist in residence, is not only smarter than Dan, but she has real talent as a creative artist with a significant following of admirers. So he has that going for him above all else! Ok, as to Dan, he has achieved some level of recognition for his legal studies, teaching, writing, legislative drafting, and speaking on areas of law of interest to those select few who engage in the deeper consideration of alternative entities. Dan usually can be found to have opinions on most matters, and some folks actually enjoy hearing these opinions. Naturally, an equal number will take grave issue with Dan’s views, not least of which become quite animated when it comes to Harmonization. As to his real interest – Talmudic Law scholar, one can only say that to engage in this aspect of Dan’s predilections is to require infinite patience and some quantity of substances which can be abused. As to his outward presentations, one is reminded of Paladin (for those too young to have appreciated that exceptional Western series, the “man in black” says it all when one thing about the gunslinger). Although Dan prefers to think of himself as a Ralph Lauren model in striking black fashion, his reality is more hip-hopish, without the bling. When he must appear as an expert witness in court, he can be quite eloquent, and some would say, captivating. In my view, Dan is more than the sum of his parts - he is a caring, compassionate, thoughtful, engaging, enlightened, erudite, stalwart friend.
and amiable companion to those who take the
time to get to know him. Congratulations Danno!

John Williams writes:

I met Dan Kleinberger on the phonewhen the ULC was just starting the Series LLC project. He and "Frosty" were calling to ask about my experience with Series LLC formations. I was one of the green horn committee members, but nevertheless he was receptive in receiving ideas and thoughtful in responding to my unbridled enthusiasm for the series LLC. They had a rather narrow question: How are people using the series? Although I mentioned about 4 uses, I went on for about an hour about everything I loved and loved to criticize about the existing series LLC laws. He quickly dubbed me the Sears Roebuck of the Series LLC. He later said that was not intended to suggest anything about bankruptcy, just trying to offer something at a discount to the masses. There was an easy decision that could have been made to limit the series to regulated financial institutions, Dan resisted that with skeptics relenting to allow open for all, even at the risk that some small-time entrepreneur would create a set of bad facts resulting in a precedent that would ruin it for the big money guys.

I was excited for the Series LLC Uniform Law project because this was going to be an opportunity for "Series version 2.0." His calm, warm, inviting voice never stopped me to stay, "thanks, I have to run, I'm late for a meeting." He was like an academic sponge just absorbing every drop of water from the world around him, perhaps parsing, organizing and filing every rapid-fire, lightening round comment somewhere in his encyclopedic mind of alternative entity law. I knew he was a big deal when he called, but I had no idea exactly the role of a "reporter" at the time. When I later attended the ULC Series meetings as an observer and then an ABA section advisor, I came to understand his true powers. He was the Jedi master of all things LLCs (and so much more). It was exciting to see him assemble, disassemble and reassemble the proposed Uniform Protected Series Act from its humble beginnings. It was like receiving a PhD in alternative entities watching him pose questions and propose solutions. The brain power required just to keep up with his thoughts was invigorating. This committee also had its share of outspoken participants whose voices were often difficult to accommodate in the revisions. Then the footnotes. Oh the footnotes. That seemed to play a big part in the accommodation process. He was like Oppenheimer and we were out at Los Alamos Labs trying different ways to tame the power of the series LLC to make sure it was controlled, and could not be used as a shell game when in the hands of someone looking to do harm. I gained a deep respect for his leadership and volunteer commitment. He was also something of a mentor and trusted confidant who was wise in the ways of the outside world. I really enjoyed all of the destination meetings and eventually video conferences with that group and he was the one doing the heavy lifting. He was riding a bucking bronco and he set a record in holding onto it until all of the holdouts had run out of steam and tamed the savage beast. One of his greatest devices in quelling those holdouts was listening and education. Through a careful pedagogical process he was able to dafly rewire others preconceived notions to share his deeper understanding. I am excited Dan is the recipient of the Luberoff Award.

Very well deserved.

David Walker writes:

I've been with Dan on the Drafting Committees for Limited Partnerships, LLCs, META (he as an Observer, I believe), Harmonization, and Protected Series, and I've done a number of programs with him. He's quite simply one of the smartest, most thoughtful and insightful lawyers, persons, I've ever known. He has strong opinions, well based of course, but is unfailingly willing to listen and sometimes alter his view.

Apropos this point, he's also incredibly literate and quick. At one point during the RULLCA saga we were exchanging emails; and as I remember, he wrote about changing position on some substantive point long held, "As Henry IV said, 'Paris vaut une messe.' I answered with question marks, and he explained that Henry IV converted to Catholicism from being a Protestant (Huguenot) to unite France. "Paris is worth a mass." I had to laugh. I can't remember what the issue was (but there are a couple which come to mind) but I've always remembered the moment and appreciated his wit and intellect apart from law and drafting issues.
Great choice for the award!

Beth Miller writes:

“Hasn’t he already received the award?” was probably the first thought that came to mind for many folks when the announcement was made that Dan Kleinberger would be this year’s recipient of the Lubaroff Award. Dan has toiled so long and faithfully and productively in the area of unincorporated entities that this recognition has been earned several times over.

The list of Dan’s contributions by way of books, articles, statutes, and CLE programs is beyond impressive, but the nature and extent of his contributions cannot be fully captured in a CV. Dan is a dedicated teacher in every respect. The impact he has made by passionately enlightening countless law students regarding the oft-neglected subject of unincorporated entities cannot be overstated, and his “teaching” has not been limited to the law school classroom. Practitioners and academics have learned much from his many excellent publications and CLE and symposia presentations, but equally impactful for many of us have been the opportunities we have had to be his “students” as we listen to the questions he poses and insights he provides in bar meetings, drafting sessions, informal gatherings, and chance encounters.

Dan’s publications have often been cited and relied on by advocates and courts, thus revealing his influence on the developing jurisprudence involving unincorporated entities. Additionally, Dan’s work as a consulting and testifying expert has been a means for him to educate litigators and members of the judiciary, many of whom ordinarily would not be particularly interested in, or even exposed to, the law of unincorporated entities. (While it is true that he may be well-compensated for this latter role, a distinguishing feature of Dan in this regard is his true passion for the subject matter and his dedication to increasing the understanding of it by litigators and courts.)

In sum, we owe Dan a debt of gratitude for his tireless devotion to the development and understanding of the law of unincorporated entities. His receipt of the Lubaroff Award is well-earned.

Donald Weidner writes:

Dan has for years been a leading figure in American business law. Throughout both the academic world and the world of practice, he has long been known as a stellar contributor. In particular, his contributions to the statutory law reform of business law, and to legal scholarship, have been excellent, prodigious, and sustained. He most assuredly merits our highest recognition.”

Johnny Lyle wrote:

I first started forming LLCs as an associate at a law firm in Georgia when Georgia passed its LLC Act in 1992. We moved to Alabama in 1993 just in time for Alabama to pass its LLC Act. My initial Operating Agreements were Frankensteins - cobbled together from limited partnership agreements, partnership agreements and Bylaws. I stumbled blindly through the wilderness until a book was published in 1994 - Bishop and Kleinberger, Limited Liability Companies - Tax and Business Law. Finally I was able to read something authoritative about an entity that was a huge amount of my practice. They were officially my heroes. I did not get to meet Dan until about 10 years ago, when I attended my first LPUE Committee meeting. I sat next to an intense, bearded man who was wrestling with a thorny LLC issue. To my surprise, it was Dan Kleinberger. I didn't say much, just soaked it all in. It was a fantastic experience, and I have been hooked ever since. They say don't meet your heroes or you will be disappointed. They are wrong.

Warren Kean writes:

Dan is one of the most valued members of the LLC and Partnership bar and a dear friend to us all. Dan is one of those members of the LLC and Partnership bar who fully embodies the spirit of Marty Lubaroff. He is a true scholar of the law and is constantly assisting the rest of us through his writings, seminar presentations, NCCUSL interactions and cocktail discussions to become more knowledgeable about not only the law on LLCs and partnerships but how that law intersects and corresponds with other areas of the law and how to harmonize competing legal principles and public policy.

Dan's commitment to us all is second to
no. I recall chairing the North Carolina Bar Association’s Committee responsible to modernizing and re-writing the North Carolina Limited Liability Company Act in 2013. I am forever grateful for Dan's many acts of kindness and patience with me for serving as an indispensable sounding board for the difficult questions that arose during that project. Dan even flew down and joined our committee at the end when we were finalizing the proposed legislation, spending the evening with the members of our committee the night before and all of the following day as we went through the proposed legislation from beginning to end. His advice and insight substantially improved the legislation and any deficiency in the Act can only be attributable to not being more mindful of his recommendations. What is most remarkable about Dan agreeing to be available to us, purely gratis, is that he did the same for many, many other state bar associations who also organized committees to redraft their LLC statutes, particularly those states that adopted the Revised Uniform Limited Liability Company Act, a NCCUSL project for which Dan was and is so instrumental. While we all owe Dan a debt of gratitude, I am particularly indebted to Dan and am extremely fortunate for his friendship. I sincerely appreciate this opportunity to express my thanks and appreciation to our dear friend, colleague, and teacher, Dan Kleinberger.

John Small writes:

My best memory of Dan has nothing to do with a Committee Meeting. Several years ago, we ended up as competing experts on Delaware and U.S. Alternative Entity Law. We testified at what was close to a week-long trial in the Canadian Tax Court in Toronto. I was the expert for “the Crown”. Along with Walt Tuthill, Dan was an expert for the alleged Tax dodger. We had a good time, both on the stand and otherwise. As we all know, Dan is a great gentleman and excellent company. By the way, the Tax Court rejected our testimony as irrelevant to his decision on a matter of Canadian Law! Congratulations, Dan.

Lauris G.L. Rall writes:

My earliest memories of Dan were in connection with the NCCUSL Drafting Committee for the Revised Uniform Limited Partnership Act (2001) or whatever we ended up calling that. Many participants in that drafting process who had been seduced by the ever expanding use and appeal of the limited liability company wondered about the future of the limited partnership. As Dan himself recently exclaimed at an LLC/Partnership Committee meeting, why would anyone ever form a limited partnership any more? But during that drafting process, which our friend and departed captain Marty helped shepherd until his too early demise, I observed close hand how Dan could hold his own in both analytical abilities and knowledge of alternative business entity laws and judicial precedents. Marty could “break it down” for those of us who needed to be led, and as Marty left us to our own devices, Dan did and has done the same to help the evolution of the statutes that our Committee breathes and bleeds. And like Marty, Dan understands to the core the human element of all this. Unlike some professorial types, he is not locked in an ivory tower, but instead, through his expert witness work and many appearances at our conferences and other gatherings, he has acquired the connection between the theories and practicalities of what we do. And on top of all that, just like Marty, Dan is a quality and fun person, whom we all are thrilled to call our colleague and friend.
Dan Sheridan writes:

It is a rare treat in life to chance upon a person fortunate enough to have found his or her true “calling”. Based on my limited period (and powers) of observation, I can say with some confidence that Dan Kleinberger is one of the fortunate few. As a matter of first impression, I will confess that the title “Rabbi” seemed more apropos to Dan than did the title “Professor” (unless you consider that they both derive from the core vocation of “teacher”). And that is the point. Dan Kleinberger is a teacher. And not only a teacher, but one of those rare teachers who seek as much to garner as to impart knowledge. Dan’s amazing command of the law, combined with his intellectual curiosity and mastery of the written and spoken word, give him an extraordinary capacity for contribution – a capacity he amply demonstrates. There are few who can match his extraordinary body of work. From point person on key statutory drafting projects to author of cutting-edge scholarship, Dan consistently and generously shares his experience, wisdom and knowledge. But more importantly, he does so with kindness, humor and humility. Mazel tov, Dan. It is a well-deserved honor!

Laura Holoubek writes:

I’ve known Dan since my early participation on the Committee when attending our smaller meetings in D.C. Dan always made me feel at home on the Committee (even when I had no idea what was going on) and was always willing to explain - in a thoughtful way - any LLC/partnership or related issue about which I had a (potentially dumb) question. I enjoy Dan’s educational commentary not just on unincorporated entities, but on broader issues of culture and world politics. Not to mention, it’s always a pleasure to share a nice glass of wine over such topics. Congratulations Dan and well deserved!

Steve Frost writes:

Marty Luberoff was one of the best lawyers I ever met. He cared about partnership and LLC law and spent untold hours working on state law drafting committees, NCCUSL drafting committees and ABA Business Section projects. I think his ultimate goals were to improve the law and to educate practitioners. I’ve shared many of my experiences working with Marty with this group before, and I won’t repeat them again now, but I can tell you that it is uncanny how much Dan reminds me of Marty. Dan has also worked tirelessly to improve the state of partnership and LLC law. Not only has he been the reporter on virtually every business entity NCCUSL drafting project, but he was the research director for the Joint Editorial Board, and he has been on more CLE panels than anyone can count. I will never forget how he rolled up his sleeves and worked with the International Association of Commercial Administrators to understand the intricacies of filing obligations to make sure the Protected Series statute addressed the concerns of people who will deal with protected series filings. In my experience, even when Dan has his own views on an issue, he is always willing and eager to hear opposing views and to thoroughly vet all positions. He wants to do what is right. While he was teaching, his relationships with his students were very important to him. He maintained friendships with many of his students. Finally, like Marty, nothing is more important to Dan than his family, Carrie and Dan’s children, Rachel and Sam. He loves each of them dearly. I am proud to count Dan as one of my friends. Frankly, in my opinion, there is no more deserving recipient of the Martin I. Luberoff Award than Dan Kleinberger. Congratulations Dan!!!

Tom Geu writes:

On one hand, the world sees Dan as a teacher in the classroom and outside it as a “loose-leaf” treatise co-author and frequent CLE presenter. On the other hand, Dan describes himself as a craftsman; that is, a technician. And he is a technician both as an expert witness and a statutory drafter. Make no mistake, however, he is a theoretician that can “bend light,” too (not that we’ve always agreed, mind you). Finally, he is a friend of many and, perhaps, one of his greatest abilities is that he can distinguish between Kettle One and Grey Goose in blind taste tests. Godspeed, Dan.

Scott Ludwig writes:

The “Man in Black” has positively impacted the law of unincorporated entities for over three decades. He has been the reporter or co-reporter for every major Uniform Law Commission Act in the area of unincorporated
entities, including, the Uniform Protected Series Act, the Harmonization of the Unincorporated Business Entity Acts (partnerships (including LLPs), limited partnerships, LLCs, Limited Cooperative Associations, Unincorporated Nonprofits Associations, Statutory Trust Entities, and the Model Entity Transactions Act), the Uniform Business Organization Code, the Revised Uniform Limited Liability Company Act, and the Uniform Limited Partnership Act.

He also served as the first Research Director for the Joint Editorial Board on Uniform Unincorporated Organization Acts, taking that Board to a new level of understanding of the various Acts at the same time elevating the Board, in the eyes of the Uniform Law Commission, to one that now has the ability to make meaningful changes in the various Acts.

During those decades he also served as a Professor of Law at William Mitchell College of Law, a Founding Director in the Mitchell Fellows Program, and the Vice Dean for Academic Programs. He currently serves as Professor Emeritus at the Mitchell Hamline School of Law. And in his spare time he authored, co-authored, or assisted in writing the following treatises: Limited Liability Companies: Tax and Business Law (Warren Gorham & Lamont); and Agency, Partnership and LLCs: Examples and Explanations (Wolters Kluwer) (including the essay Agents of the Good, Servants of Evil: Harry Potter and the Law of Agency). In addition, although his publications are too numerous to list, I was able to locate over 50 different articles that he has written on the subject of unincorporated entities.

He has been amazingly active with his state bar (Minnesota), acting as the reporter, co-reporter, or chair for the Minnesota Limited Liability Company Act, the Minnesota Limited Liability Partnership Act, the Minnesota Joint Task Force on the Model Entity Transactions Act, the Chapter 319B Task Force of the Minnesota Business Law Section, the Minnesota Professional Firms Act, the Minnesota Manufactured Housing Sales and Lot Rental Reform Act, the Minnesota Economic Loss Statute, and the Minnesota Plain Language Contract Act.

Dan is a member of the American Law Institute where he has served on the Members Consultative Group for the Restatement (Third) of Agency.

He also served as the Chair of the American Association of Law Schools Section on Agency, Partnerships, LLCs and Unincorporated Business Associations.

Dan is a consistent presenter of CLE for the ABA and for our committee. His contribution to CLE is outstanding having presented well over 100 different CLE courses that I could find (I feel certain it is much more than that).

He has also served our committee in numerous roles, including, being the chair of the Task Force to evaluate Low Profit Limited Liability Companies (L3C), and the chair of the Task Force review the Uniform Power of Attorney Act and the Uniform Power of Appointment Act.

And of course, his educational background is impeccable having received his undergraduate degree from Harvard College where he received an A.B. (Summa Cum Laude) with a combined major in government, history, and economics, and was the recipient of the Junior Twelve, Harvard Phi Beta Kappa (12 juniors elected from a class of 1200) and the Philo Sherman Bennet Prize for Senior Honors Thesis. Dan then went on to obtain his J.D. from Yale Law School.

Having said all of the above, the “Man in Black” is best known in our committee as being open to new thoughts and theories, patient with those who do not know as much as he does, eager to learn from other’s experiences, and, to our delight, willing to bring his teaching skills into our discussions so that we all understand the issues.

Dan has especially been kind to this poor Alabama Dirt Farmer, leading me down the correct path, and being patient with my understanding or misunderstanding of matters. He has over the time we have worked together become a friend that I respect and appreciate more with each passing day.

On the personal side, he is quick to let you know that his wife is a world class artist, and is not shy about sharing information about her art shows—a tribute to the love of his life which speaks volumes about what a good man the
“Man in Black” is.

Congratulations to the “Man in Black,” Dan Kleinberger. I look forward to celebrating with you at the LLC Institute!

Allan Donn writes:

The award to Dan Kleinberger, scholar and teacher, of the Lubaroff Award for 2019 is an appropriate recognition of his prodigious contributions to the law of unincorporated business organizations.

His most recent contributions were his service as Reporter for the Uniform Protected Series Act and as Director of Research of the Joint Editorial Board on Uniform Unincorporated Organization Acts.

Those projects were preceded by his work with Carter Bishop as co-Reporters of Drafting Committees for the Harmonization of the Uniform Business Organizations Acts.

For those of us who work with unincorporated business organizations we have the rich resources of his work with Carter on their treatise on Limited Liability Companies and his Agency, Partnerships, and LLCs (5th ed. 2017). On a personal basis, I benefit, as I know that others do as well, from his willingness to respond to individual questions and participate in CLE programs, such as the Committee’s LLC Institute.

Dan - thanks for all that you do for all of us.

Tom Rutledge writes:

I have no recollection of when I first met Dan, but as my involvement with this Committee was precipitated by what was ultimately ULPA (2001), I’m sure it was early on. Since then the “Man in Black” has been a constant presence. I have had the pleasure of working with him on RULCCA (2006) and the Uniform Protected Series Act, on seminars and on articles. While we certainly have disagreed on certain points (and I really wish he had a deeper knowledge of Jewish history (grin)), I’ve always come away knowing something new.

Dan is of course famous (infamous) for his intricate PowerPoint presentations. A number of years ago several of us were scheduling our next call. In response to one date thrown out, Dan responded “That is Yom Kippur, and I will be at Temple confessing my errors to my Maker.” I asked “Will there be a PowerPoint?” He never has answered me.

Dan, congratulations on receiving the Martin I. Lubaroff Award.

The Martin I. Lubaroff Award was established in 2001 to honor the memory of Marty Lubaroff, who untimely passed away on January 1, 2001. Marty was the quintessential lawyer--careful, thorough, exacting, engaging, insightful, precise, provocative and persistent, while gentle, kind and courteous. He was a good friend and mentor to scores of lawyers in Delaware and throughout the United States and was an esteemed Delaware practitioner with the law firm of Richards, Layton & Finger. Marty was a long-time member of, and key participant in, the LLCs, Partnerships and Unincorporated Entities Committee. He chaired the Limited Partnerships Subcommittee at the time of his death.

WHAT HAPPENED IN WASHINGTON DC  
(And What You Missed If You Were Not There)

The Committee had a number of successful activities at the recent Annual Meeting of the Section of Business Law. If you were there, this is a recap. If you were not there, this is what you missed.

Thursday morning began with a program, moderated by Tom Rutledge and featuring Professors Bob Thompson and Jim Wheaton. The program, entitled Operating Agreements from the Minority Perspective: Rosencrantz and Guildenstern Are Dead, focused upon the means by which the majority/control faction of an LLC (however defined) may utilize that power to the disadvantage of the minority members, steps the minority members may take to limit the possibility of those circumstances coming to pass and practical limitations upon the majority faction doing so. The Committee’s Model LLC Organizational Checklist was identified as a resource for identifying important issues upon which the minority may want to insist upon a vote/blocking right.

It was nice to have an audience of approximately 65 for an 8 a.m. program, an audience that was engaged in the way of questions and comments.

Thursday morning continued with our open committee meeting. It began with reports on a myriad of topics including the upcoming LLC Institute, the upcoming meeting in Boston and where we stand on a variety of publication projects including the Model LLC Agreement for a Delaware Protected Series LLC.

Much of the meeting was devoted to a discussion of where we stand on the beneficial ownership resolution that has been previously approved by the Section of Business Law Council and tendered to the House of Delegates. Cutting to the chase, at the Annual Meeting of the ABA in San Francisco at which the House of Delegates met, certain members of the Section of International Law and its constituent committees raised an objection to the resolution and the supporting white paper jointly drafted by our Committee and the Committee on Corporate Laws (that resolution and the supporting white paper have been previously circulated to all members of the Committee). It is a fair summary that the only objections they had to the resolutions/white paper were the form and content.

As to form, they had a vehement objection that they were not invited to participate in the drafting of our recommendations. The fact that we are doing our work in the context of responding to US legislation governing US organized entities had not seemed to have occurred to them. Also, they failed to acknowledge that the Gatekeepers Task Force, whose resolution was being considered, has a representative from the International Law Section.

As for substance, the objections included: (a) that we are against the adoption of a publicly maintained database; (b) that our focus is upon record, as contrasted with ultimate beneficial, ownership; (c) our restriction of the availability of the information to members of law enforcement, they suggesting it should be available as well to party’s undertaking due diligence; (d) an objection to our insistence that the information, however maintained, be provided to members of law enforcement only with appropriate Fourth Amendment protections; and (e) client confidentiality is a “red herring.”

Since the San Francisco meeting there has been a phone call between members of the International Law Section and members of the joint task force of our Committee and that of Corporate Laws. We have asked them to markup our resolutions and report so that we can respond to specific, rather than generalized, objections.

Stay tuned for further developments.

While not fully effective until the close of the Annual Meeting, our open Committee meeting concluded with the passing of the torch from Garth Jacobson, whose term as chair came to an end, to Christina Houston, our incoming chair. Please be looking to the From the Chair to appear in the next issue of the LLC & Partnership Reporter for thoughts from Christina as to the direction of our Committee.

On Thursday afternoon the Committee sponsored a program titled 10 Things Corporate
Lawyers Must Understand About How A Limited Liability Company Is Not A Corporation. Chaired by Dan Kleinberger and including Carmen Fonda, Lisa Jacobs and Chip Lion, the program began with a brief discourse on the mythical 'limited liability corporation. The presentation accomplished what its title promised - a lively discussion of various ways in which LLCs and LLC law differ materially from corporations and corporate law and the resulting practical consequences. Among the major topics: the bifurcated nature of an ownership interest in an LLC contrasted with the very different construct we call "shares"; different meanings of and processes and grounds for dissolution; capital structural differences: units (never? sometimes? why? how?) and the use of blocker corporations by VCs in venture-backed LLCs. The panel also touched on mergers and acquisitions of LLCs including dissenter and appraisal rights (or lack thereof) issues, and the use of freeze-out and end-run mergers. The discussion also included the chair's brief excoriation of the legal academy for, for the most part, continuing to give LLCs short shrift.

The next event on Thursday was a meeting of the Joint Task Force on Security Interests in LLC Interests. But for some technical revisions, that long-awaited document is finished and will be submitted for publication in The Business Lawyer. Stay tuned for what new fact pattern will be considered in the next series of documents to be produced by this task force.

Thursday evening came to a conclusion with our Committee dinner. It was great to have so many people attend, including a number of spouses, children and friends. We as well enjoyed the company of Judge Elizabeth Paris of the Tax Court, a longtime member and a huge supporter of our Committee.

The materials from our and all of the programs from the BLS Annual Meeting are available through the ABA website.

We will next meet November 7-8 in Tampa, Florida for the LLC Institute.

Annual Reports for Connecticut LLCs

In 2019, pursuant to section 3 of Connecticut S.B. 1093, the LLC Act was amended as to annual reports filed by domestic and foreign LLCs to require (7) "Such additional information, including the North American Industry Classification System Code, that the Secretary deems pertinent for determining the principal purpose of the limited liability company." See Conn. Stat. § 34-247k(a) as amended by Public Act No. 19-40.

The new law if effective January 1, 2020.

Michigan Waiver of Fees for Veteran Owned Businesses

Under certain 2019 amendments to various of Michigan’s business entity states, certain fees for business corporations, nonprofit corporations and LLCs majority owned by honorably discharged veterans are waived.

For LLCs, the provisions are substitutions (7)-(1) of MCL § 450.5101.
**General Partnership Interests are Securities – Sometimes: The 5th Circuit Revisits Williamson**

By: Peter D. Hutcheon  
Norris McLaughlin P.A.  
Bridgewater, New Jersey

In 2016, the United States Securities and Exchange Commission (“SEC”) brought a civil suit in the United States District Court for the Northern District of Texas, Dallas Division, against Arcturus Corporation, a Texas corporation (“Arcturus”), Aschene Energy LLC (“Aschene”), a Texas limited liability company, along with Leon Ali Parvizian, a UK citizen and permanent US resident, who was the founder and owner of each entity. From 2007 through 2011 the entities and Parvizian offered and sold ownership interests in six oil and gas well drilling projects. The District Court decision, SEC v. Arcturus Corporation, reports that each project had a “Managing Venturer” which supervised and managed that project and received “Management Fees.”

The SEC asserted that the drilling projects were securities, not joint venture interests where all the venturers were involved in the Manager’s ventures. The defendants countered that the joint venture interests came with powers, rights, and liabilities and management obligations. In a 25-page, carefully reasoned decision, Judge Kinkeade of the District Court concluded in response to a motion for summary judgment, that the SEC enforcement action brought in 2013 was well-founded based on the definition of “security” in both the Securities Act of 1933, as amended (the “1933 Act”) and the Securities Exchange Act of 1934, as amended (the “1934 Act”). The District Court found that the term “security” includes “investment contracts” (a term neither separately defined nor explicated in either the 1933 Act or the 1934 Act). However, in SEC v. W.J. Howey Co., the United States Supreme Court supplied the missing definition of “investment contract” as a type of “security”:

> ... a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of a promoter or a third party.  

The District Court also cited with approval Williamson v. Tucker for the proposition that interests in business entities although they might be called general partnership interests, may well be securities for purposes of Howey, if there is a dominant, managing partner, even though the other investors have some power and rights with respect to managing the efforts of the entity.

Howey was seen as having three prongs: i) an investment of money; ii) a common enterprise; and iii) an expectation of profits solely from the efforts of others (emphasis added). The Arcturus District Court found that the first two prongs were clearly satisfied. It then considered the third prong and found the joint venturers had little or no actual power; that the venturers were inexperienced (and, hence, vulnerable) in assessing oil and gas drilling decisions, and that the venturers were dependent upon the defendants’ expertise in the business. Accordingly the District Court found that the defendants had violated the 1933 Act by selling the joint venture interests without registering them as securities with the SEC AND had violated the 1934 Act BOTH by fraudulently failing to provide complete statements of material facts relating to the investment AND by failing to provide material information necessary to prevent statements to the venturers from omitting material facts necessary to keep those statements from being misleading. Hence, the District Court granted the SEC’s countermotion for summary judgment.

On June 27, 2019, the Fifth Circuit Court of Appeals, in SEC v. Arcturus Corporation, issued a substitute opinion for its January 7, 2019 opinion in each case authored by Chief Judge Stewart, addressing these same issues. The Fifth Circuit’s conclusions (including the revisions found in the substitute opinion) were both enlightening and cautionary.

The Arcturus drilling projects were complex, in part because each project was split into multiple stages. The first stage of each project was termed by the Circuit Court the capitalization stage. Each investor would pay a fixed price for a “Turnkey Drilling Contract.” The project manager would use those funds to purchase a working interest in a project oil well. That working interest would entitle that project to drill the well, test it for oil or gas and complete the well. That working

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1 171 F.Supp.3d 512 (N.D. Texas, 2016).  
2 328 U.S. 293 (1946).  
3 328 U.S. at 298-99.  
4 645 F.2d 404 (5th Cir., 1981).  
5 2019 WL 2622534.  
6 912 F.3d 786 (5th Cir., 2019).
interest also entitled the project to a share of the well’s net proceeds, if any.

The project manager would subcontract with a drilling operator to drill and test the well. Based on the results of drilling and testing the well, the project manager would recommend whether or not to complete the well. The venturers would then vote. If the majority of the investors voted in favor of completing the well, the venturers would be required to pay a completion assessment. If a venturer did not pay the completion assessment, he, she or it forfeited the investment in that project well, subject to the right to buy back in later where the “buy back” price included a penalty to compensate those who stayed in the project.

After completion, the venturers could elect, again with the project manager’s recommendation, to “engage in special operations” such as: drilling deeper, fracking or completing additional zones. Each of these operations involved a special assessment on the participating venturers, with a loss of investment if a venture did not participate when the project manager recommended something and a majority of venturers agreed.

The Arcturus defendants called the projects “joint ventures” and the investors “partners.” The SEC and the District Court concluded that the interests in the drilling projects were securities, reasoning that they were “investment contracts” under the Howey analysis. The defendants agreed with both the SEC and the District Court that each of the drilling projects was a common enterprise, where the investors expected to profit, i.e., two of the three Howey factors. At issue was, were those expectations of profits tied “… solely [to] … the efforts of others,” namely the defendants?

Here the abstract metaphysics of the relationships among the parties come into play. In a corporation, a limited partnership or a manager-managed limited liability company there are relatively passive investors (shareholders, limited partners, non-manager members); and active managers with the actual and apparent authority to run the enterprise. In contrast stands a general partnership, where all partners are more or less equal, especially in management authority. Hence, general partnership interests are not necessarily or even typically securities – unless the Animal Farm rule applies, i.e. some general partners have much greater power and/or control of information so that the other “general partners” are seen more like relatively passive investors.

Perhaps the leading judicial authority dealing with this type of fact pattern is Williamson v. Tucker where the Fifth Circuit Court said at 418:

[The Supreme Court has repeatedly emphasized that economic reality is to govern over form …

Indeed, the Williamson Court, which was addressing an interrelated series of joint ventures owning interests in what became Dallas-Fort Worth Airport, where those ventures were “managed” by a single entity (which was a co-venturer in each venture) said at 423:

Thus, a general partnership in which some agreement among the partners places the controlling power in the hands of certain managing partners may be an investment contract with respect to those other partners.

The Williamson Court had previously looked to the experience of the putative “general” partners and their dependence, if any, on the management skills and authority of one or more partners.

The Arcturus Court, in an echo of Howey, finds that Williamson has three factors: i) whether the drilling projects left the venturers with so little power “that the arrangement in fact distributed power as would a limited partnership; ii) whether the venturers were “so inexperienced and unknowledgeable in business affairs” that the venturers were “incapable of intelligently exercising” their powers; and iii) whether the venturers were so “dependent upon unique entrepreneurial or managerial ability of the [project managers] that they cannot replace those manager[s] … or otherwise exercise meaningful partnership or venture powers.” These three factors were to “guide courts in applying the third prong of Howey to the facts of what the Arcturus Court termed “in-between situations.” The Court also noted that a plaintiff “faces a factual burden” when proving one of the Williamson factors.

The Court analyzes each factor in turn but devotes far greater amount of its opinion to the first one: whether the venturers had real power? The Court looks at both the documents and at how the drilling projects actually functioned. The Court notes that the project managers had very significant powers, including: oversight of day-to-day operations through the hiring and direction of

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7 Animal Farm, by George Orwell (1945). “All animals are equal but some are more equal than others.”

8 45 F.2d 404 (5th Cir. 1981).
subcontractors; the authority to incur expenses on behalf of the venture; and the sole power to interpret ambiguous or unclear provisions in the documents.

Balanced against the project managers’ powers was the power of the venturers to remove a project manager with a 60% vote. Further the documents gave the authority to manage and control each drilling project to a majority of the venturers, including the power to develop rules and procedures governing meetings and voting, amend the documents, call a meeting, receive financial information and information about third-party contracts and the right to inspect books and records. Indeed, the Court notes that in any case where a venture did not send money in response to an assessment had to be counted as a “no” vote.

The Court then notes that the venturers regularly did vote, citing affidavits from 15 investors as to voting on matters. The Court addresses how voting and subsequent assessments, where the venturer’s interest, if he or she elected not to pay. The Court characterizes the initial investment as the price to participate, so that a venturer faced with a completion assessment and not believing in the well’s profitability, simply steps aside and thereby avoids further loss (if the investor is correct about the well), citing with approval a Texas Tech Law Review article about the so-called “Industry Deal” in the oil and gas business.\(^9\) The Court also notes, as stated above, that the venturer, if wrong, can buy back in by paying a penalty amount. The Court sees this penalty arrangement as compensating the risk-taking venturers who paid the completion assessment.

The Court then considers the amount and timing of communications to the venturers and finds evidence of many and regular update e-mails and even the installation at one remote operation of a visual surveillance system. Venturers were regularly invited to visit drilling sites. All of this was confirmed in affidavits from 15 of the venturers and other information about another 10 or so of the venturers. Although the Court recognize that this is a small sample of the over 340 venturers in all of the projects. Thus, the Court notes that it does not have the trial testimony of witnesses and experts to allow it to conclude that the communications were sufficient to empower the venturers by allowing them to make informed decisions. Further the Court expresses concern that the venturers were not in a position to contact each other as the project managers intentionally kept the identification of other investors from those who asked to contact their fellow investors, although there was some evidence of group telephone calls and group e-mails. This disparity alone in the Court’s view called for “full factual hearing with cross-examination.” The Court noted that the drilling projects had between 35 to 108 investors, which it saw as suggestive that the projects may have had too many investors to be seen as general partnerships and signaled the need for further factual development.

The Court then reviews the knowledge and experience of the investors to apply the second Williamson factor. The SEC had asserted that the investors were inexperienced based upon i) the fact that the venturers were recruited in a cold calling campaign and (ii) four venturers stated to the SEC that they were inexperienced in oil drilling investments. The Court found recruiting by cold-calling had probative value. But the Court in the substitute opinion described in some detail a venturer recruiting process used by defendants that seemed very focused on weeding out the persons unable to bear and to assess the risks involved in he projects. The Court also pointed to submissions by the defendants of statements from many venturers of extensive knowledge of the oil and gas industry and similar investments. This area of the substitute opinion contains a substantial amount of addition information compared to the January 2019 opinion about at least some of the venturers, their knowledge and experience. The Court also noted that the documents required each venturer to attest that he or she was an accredited investor, had substantial business experience and would be able intelligently to exercise his or her management powers. The substitute opinion notes, for example the level of geologic knowledge of one venturer who said he relied on the project manager. Again, the Court finds this raises substantial fact questions.

Finally, the Court addresses the third Williamson factor: whether the investors were so dependent on unique entrepreneurial or managerial ability of the project managers, that they were unable to exercise their management powers as a practical matter. Here the Court found that, if the project managers were removed, enforceable contracts with the subcontractors to drill, test and if approved, complete a well would still exist. Further the Court finds that the project managers did not control all the venturers’ funds – only the upfront participation payment, which would only be recovered IF the well turned out to be productive.

Here the segmentation of each drilling project left both the power to decide and the funds remaining in the hands of each venturer.

Accordingly, the Arcturus Court found that the defendants had raised genuine issues of material facts entitling them to a new trial. Thus, the Arcturus Court while reemphasizing the importance of Williamson, also made clear the critical need to analyze the very particular facts of the sale of general partnership interests to determine whether those interests might be securities for purposes of the 1933 and 1934 Acts. Moreover, the detail discussed in the Fifth Circuit substitute opinion provides very helpful guidance on how to structure deals involving a general partnership to avoid coming within the regulatory ambit of Howey and Williamson.

### New York Election Law and LLC Ownership Disclosure

New York state’s election law has been amended to require the disclosure of the membership of LLCs that are engaged in political activity. N.Y. Election Law § 14-116(3) now provides:

Each [LLC] that makes an expenditure, or contribution, for political purposes shall file with the state board of elections, by December thirty-first of the year in which the expenditure is made, on the form prescribed by the state board of elections, the identity of all direct and indirect owners of the membership interests in the [LLC] and the proportion of each direct or indirect member’s ownership interest in the [LLC].

It is not clear whether those reports will be available for public inspection.

Thanks to Bruce Rich for the lead.
A Clear Case of ‘Passive Aggressive’ in Nonresident Tax

By: Michael Bowen
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The U.S. Supreme Court of the United States is poised to hear a challenge to the state of California's taxation of nonresident members of California limited liability companies and nonresident shareholders of California corporations.1

Specifically, the state of Arizona asserts that California's aggressive efforts in taxing nonresident passive investors in such entities violates the due process clause and the commerce clause of the U.S. Constitution. In its filed opposition brief with the court, California argues that the court lacks jurisdiction to hear Arizona's challenge.

Although the court does have original jurisdiction to hear the case, California contends that the court is not the appropriate forum for such an action where the constitutional questions relating to "thousands of individual taxpayers' refund claims" require a fact-intensive review of each individual case. If the court decides to hear the case, a ruling in Arizona's favor will have an unquestioned impact on the state and local taxation of nonresidents.

The crux of the dispute relates to California's "doing business" tax on all entities that conduct business in the state. The tax is a flat $800 for limited liability companies and is a minimum of $800 for corporations.

Despite a successful challenge to the tax in Swart Enterprises Inc. v. Franchise Tax Board,2 California has remained defiant in its application of the tax to nonresidents. In published notice FTB 2017-01, the California Franchise Tax Board made clear that it would adhere to the holding of the California Court of Appeals in Swart only in cases with identical facts.

Consistent with this approach, in the 2018 case of Satview Broadband Ltd.,3 the Franchise Tax Board affirmed the assessment of the "doing business" tax because the nonresident taxpayer's facts did not mirror those in Swart.

In its complaint filed with the United States Supreme Court, Arizona contends that it has been harmed by California's "aggressive" assertions of tax nexus over Arizona-based passive owners in California LLCs and corporations. According to Arizona, Arizona-based companies pay almost $10.6 million a year to California in "doing business" taxes.

Because the payment of these taxes is generally deductible, Arizona asserts that it loses approximately $484,000 in annual tax revenue. In further support of its case, Arizona notes that the relatively low dollar amount of the tax prevents any serious challenge by nonresidents.

The due process clause requires that there be definitive "minimum contacts" between the state and the person, property or activity it seeks to tax. Arizona argues that where cross-border investment is passive, there are insufficient "minimum contacts" between a nonresident and the in-state business to support California's jurisdiction to tax.

In its filed brief, California counters by stating that the "minimum contacts" analysis requires a careful case-by-case review of the relevant facts. For this reason, the action brought by Arizona, California maintains, is an ill-suited vehicle for such a due process clause challenge.

Under the Supreme Court's commerce clause jurisprudence, a state tax will survive scrutiny where (1) there is a "substantial nexus" between the activity and the taxing state, (2) the tax is fairly apportioned, (3) the tax does not discriminate against interstate commerce, and (4) the tax is "fairly related" to the services provided by the taxing state.

Arizona claims that California's taxation of nonresident passive investors in California LLCs and corporations violates all four of these tests because there is a legally recognizable distinction between the activities of the nonresident passive investor and the active California business.

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1 Arizona v. California, Case No. 220150 (U.S. S.Ct. Motion for leave to file a bill of complaint filed Feb. 28, 2019).


3 In the Matter of the Appeal of Satview Broadband, Ltd, OTA Case No. 18010756 (Sept 25, 2018).
California argues that the required commerce clause approach, like that of the due process clause, requires a highly factual examination of each individual case. As a result, California contends that the court should reject Arizona's request for a bright-line rule.

Assuming that it agrees to hear this case, the court's recent holdings in South Dakota v. Wayfair Inc.⁴ and North Carolina Department of Revenue v. Kimberley Rice Kaestner 1992 Family Trust⁵ may shape the required constitutional analysis. In Wayfair, the court ruled that the commerce clause's "substantial nexus" mandate does not require that a taxpayer be physically present in the taxing state.

According to the Wayfair court, the commerce clause merely asks whether the tax applies to an activity with a substantial nexus with the state. The court made clear that substantial nexus exists "when the taxpayer avails itself of the substantial privilege of carrying on business" in the taxing state. In Wayfair, the nonresident retailers were found to have substantial nexus with South Dakota based on their extensive virtual economic presence in South Dakota.

On its face, the court's reasoning in Wayfair would tend to support Arizona's commerce clause challenge. After all, it cannot be disputed that Arizona-based passive investors in California LLCs and corporations do not "avail [themselves] of the substantial privilege of carrying on business" in California. The critical premise to this argument, however, is that the activities of California LLCs and corporations are not attributed to Arizona-based passive investors. The Supreme Court's recent holding in Kaestner Trust provides needed support for this premise.

The focus of the dispute in Kaestner Trust was whether North Carolina could tax income earned by a nonresident trust. North Carolina asserted its authority to tax the nonresident trust based solely on the fact that a trust beneficiary resided in the state. The nonresident trust contended that the due process clause was a bar to the exercise of North Carolina's tax jurisdiction. Specifically, the nonresident trust argued that the in-state contacts of the beneficiary could not be attributed to the trust for purposes of satisfying the "minimum contacts" requirement of the due process clause.

The Supreme Court unanimously agreed. The court reasoned that there must be a definitive link between the in-state beneficiary and the trust assets to support North Carolina's efforts to tax the income from such assets.

The court's holding in Kaestner Trust also buttresses the arguments made by Arizona in its challenge to California's "doing business" tax. In Kaestner Trust, the court made clear that there must exist a constitutionally recognizable nexus between the in-state contact and the object of the tax. The mere existence of a contingent economic connection was insufficient to satisfy the due process clause in Kaestner Trust.

Arizona makes conceptually similar arguments in its filing. Arizona-based passive investors in California LLCs and corporations, Arizona maintains, lack any managerial or other active business connection to the in-state business. California's link to the operations of the in-state business is not properly attributable — without more — to Arizona-based passive investors for purposes of the required analysis under the due process clause.

It remains to be seen whether the Supreme Court will accept Arizona's challenge. Most recently, the court asked U.S. Solicitor General Noel Francisco to file a brief with his recommendation on whether the court should hear Arizona's constitutional challenge. The solicitor general authored a brief in support of South Dakota in Wayfair in which he argued that the commerce clause was not a bar to the imposition of the sales tax where the nonresident retailers maintained a "pervasive and continuous virtual presence" in South Dakota.

A close reading of the Wayfair decision makes clear that the court gave great weight to the solicitor general's arguments. For example, in support of its holding, the Wayfair court upheld the imposition of the tax based on the "continuous and pervasive virtual presence" of the taxpayers.

In the event the court does entertain argument, the resulting decision will undoubtedly have national implications. The constitutional challenges at issue are not unique to California. In several forms and by various methods, the tax laws of many states impose tax on nonresident passive owners based solely on the connection between the taxing state and the in-state business. Stay tuned.

Limited Partnership Dissolved at the Request of Transferees of Limited Partners

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In a recent decision from Minnesota, a limited partnership was ordered to be dissolved in an action brought by the transferees of the limited partners.¹

Nordic Townhomes was originally organized with three limited partners and three general partners. With the passage of time, all of the original limited partners died. No new limited partners were admitted, and the heirs of the various limited partners became transferees of their respective interests in the partnership. The partnership agreement of Nordic Townhomes and the present situation were summarized by the court as:

Once Nordic did not have any limited partners, the partnership was to dissolve, liquidate, and cease doing business. Despite the fact that Nordic does not have any limited partners, it continues to exist as an entity and conduct business.

The plaintiffs, they being some of the transferees of now deceased limited partners, filed a complaint seeking that Nordic Townhomes wind up its business, satisfy its debts and obligations and distribute the net proceeds to those holding the economic rights in the partnership. The limited partnership responded by claiming that the plaintiffs did not have standing to seek either judicial or nonjudicial dissolution of the partnership on the basis that they were neither limited nor general partners. The trial court granted the plaintiffs’ summary judgment, in effect finding that they could enforce the provision of the limited partnership agreement with respect to the partnership’s dissolution. This appeal followed.

Applying an “injury-in-fact” paradigm, the Court of Appeals found that the transferees of the limited partners had standing to enforce that provision of the limited partnership agreement directing that the partnership be dissolved upon having no limited partners:

Here, respondents suffered an injury-in-fact sufficient to give them standing to ask the district court to enforce the partnership agreement. The partnership agreement is clear: Nordic was to be dissolved when there were no longer any limited partners. That process involves liquidating assets, and respondents are entitled to their share of any profits remaining once partnership obligations are resolved. See Minn. Stat. § 321.0702(b)(2) (2018) (stating that “upon the dissolution and winding up of the limited partnership’s activities [a transferee is entitled to] the net amount otherwise distributable to the transferor”). Because respondents are entitled to their share of that money, and because Nordic refused to take steps to dissolve the partnership and liquidate assets, respondents suffered an injury-in-fact sufficient to confer standing.²

Further rejecting the claim that the court was allowing a non-partner to move for judicial dissolution, the court observed that “respondents’ action is more properly characterized as seeking enforcement of the partnership agreement rather than seeking judicial dissolution of the partnership. And because we conclude that respondents have standing because they suffered an injury-in-fact, respondents do not need a statutory basis to have standing.” Id. (citation omitted). Still on that same point, the court would also write:

[T]he partnership agreement clearly states that Nordic was to be dissolved when there were no limited partners. Accordingly, as transferees,


respondents had standing to ask the district court to enforce the partnership agreement and the district court correctly required Nordic to follow the partnership agreement’s mandate of dissolution and liquidation.

Finally, although our opinion rests on our application of the law, we observe that adopting Nordic’s position could effectively result in no one having standing to seek enforcement of the partnership agreement. We do not discern the Minnesota law leaves transferees like respondents without redress in cases where remaining general partners fail to abide by the partnership agreement.3

For myself, I find this decision troubling. Yes, all the court is doing is enforcing the agreement. The court is, however, enforcing the agreement on behalf of persons who are not parties to it. As transferees of an economic interest in the limited partnership, the plaintiffs in this action have no right to participate in the management of the limited partnership. While the original limited partners may have been parties to the limited partnership agreement and in that role had the capacity to bring an action for its enforcement, that right did not devolve to the transferees upon the death of the limited partners. In effect, the court is allowing non-parties to an agreement to insist upon its enforcement. What about the requirement of privity before bringing an action for enforcement?

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3 Id., *3 (footnote omitted).
New York LLC Act Amended to Permit Access By Employees to Member Names, Contributions, and Share of Profits and Losses by Employees

Under a 2019 amendment to the New York LLC Act and section 1102 thereof, it addressing the maintenance and inspection of company books and records, employees are afforded certain rights of inspection, See 2019 New York Assembly Bill No. 2006; 2019 New York Senate Bill No. 1506, adding new subsection (e) to New York LLC Act § 1102:

Paragraph 2 of subsection (a) addresses “a current list of the full name set forth in alphabetical order and last known mailing address of each member together with the contribution and the share of profits and losses of each member or information from which such share can be readily derived.”

Another Sighting of the Limited Liability Corporation

The Sealed Indictment of Lev Parnas, Igor Fruman, David Correia and Audrey Kukushkin (S.D.N.Y.) (¶ 2) charges them with “laundering foreign money through bank accounts in the names of limited liability corporations.”
Changing Your Mind Doesn’t Put Me Out of Commission

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In Gebroe-Hammer Associates v. West Green Gables, LLC, the Court dealt with a claim by the plaintiff realtor for a $250,000 commission for “procuring a purchaser” who was ready, willing and able to purchase defendant’s 21 townhouses. Jeffrey and Susan Wittman were the two 50% members of the member-managed New Jersey LLC. Susan died in 2015 and her 50% interest in the LLC was inherited by their two daughters. Susan’s brother was the executor of the estate. Under the terms of the LLC operating agreement (and under the New Jersey statute, unless varied by the operating agreement) the daughters became economic interest holders. They were not subsequently made members of the LLC. Hence, Jeffrey Wittman was the sole member of the LLC.

In August 2016 he signed the listing agreement with plaintiff.

Within a week, plaintiff produced a buyer, which offered a letter of intent to West Green Gables which accepted it. Jeffrey Wittman instructed plaintiff’s agent to forward the letter of intent to his attorney, so the attorney could prepare a contract. Thereafter he contacted his brother-in-law and then announced that he would not proceed with the sale. One may speculate as to the possible claims the executor asserted on behalf of the daughters, but the key to both the Trial Court and the Appellate Division decisions was that the daughters had no voice in governance as they were only economic interest holders. The Court ordered West Green Gables LLC to pay the commission.

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Transferring Ownership Is Not Transfer of a Lease

In a decision rendered earlier this year in Massachusetts, the distinction between transferring ownership of a LLC and its assets was reinforced. Altitude, Inc. v. Altitude Properties, LLC, 95 Mass. App. Ct. 1102, 124 N.E.3d 158 (table), 2019 WL 1092667 (Mass. Ct. App. March 8, 2019).

In this instance, the LLC was a tenant under a lease agreement that, inter alia, prohibited transfer of the lease. The owner of the LLC transferred ownership to a new member. The landlord asserted that this constituted a forbidden transfer of the lease.

The court rejected that assertion, holding rather that the transfer of the entire ownership of the tenant LLC is not an “assignment” of the lease that would be prohibited thereby.

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The single member limited liability company (SMLLC) is highly useful but hardly simple. State law and tax treatment render it sometimes "regarded" (but not always) and sometimes disregarded (but not always), all of which lead to some unusual results.

When first authorized about 30 years ago, LLCs, like partnerships, were designed to have two or more members. The "pick your partner" principle of partnership law became part of an LLC's DNA. This prevents a member, either during lifetime or at death, from forcing an unadmitted and perhaps undesirable member on those who remain or survive. When state statutes were subsequently amended to authorize SMLLCs, followed by the "check the box" regulations, the "pick-your-partner" principle adhered. As noted in the dissent in Olmsted v. FTC, a case involving the rights of a creditor of a sole member, when legislatures amended their LLC statutes to permit SMLLCs, they did not contemplate issues that would arise from application to SMLLCs of statutory sections designed for those with more than one member. The default rule when a sole member dies without providing for that inevitable event is another place where "pick-your-partner" protection is inappropriate.

In both a multimember and SMLLC, when a (or the) member dies, the deceased is dissociated. Without provision in an operating agreement addressing death, the decedent’s interest divides. In a multimember LLC, the economic rights pass to the decedent’s estate, but the decedent’s management rights devolve on the surviving members who are thereby protected from unadmitted heirs participating in management.

Contrast these issues with what follows the death of a sole shareholder. The shareholder's entire bundle of rights in the shares pass to the estate. The corporation does not dissolve automatically after a fixed time. There is no doubt what becomes the immediate successor shareholder. If the sole shareholder had been a sole director, the estate can "elect" a new director. If the...
corporation is governed by a board of directors, the board continues to operate the business subject to the estate’s rights as shareholder.

Some business people form SMLLCs without the benefit of counsel; some engage counsel who are not business lawyers; and some, when advised to adopt an operating agreement to avoid the default rule, are pennywise and pound foolish. Whether the member’s failure to provide for succession results from ignorance or refusal to follow sound advice, there appears to be no reason why the entire bundle of rights in the 100-percent LLC interest held by a sole member, like the entire bundle of rights in all of the corporation’s issued and outstanding shares held by a sole shareholder, should not pass to the estate. The distinction between economic and management rights in the SMLLC is an unnecessary trap for the unwary.

| New York and Identifying LLC’s Members on Transfer Tax Returns |

Legislation passed in 2019 in New York requires the listing of the members in the real property transfer tax return filed in connection with the purchase or sale of residential real estate of up to four units.


| Illinois LLC Act Amended as to Member’s Right to Inspect Books and Records |

In 2019 Illinois amended its LLC Act to provide that a (a) a member denied access to requested books and records may bring an action to enforce that right, (b) permits an award of attorney fees and costs incurred in favor of the member against the company where the LLC did not comply with the statute and (c) allows a court to impose restrictions on the access to and use of the information “based on the reasonable needs of the company and the member in question.” See 805 ILCS 180/10-15 as amended by 2019 Illinois Senate Bill No. 1495 (adding new subsection (j)), which provides:

If the company fails to provide any information required to be provided by this Section, the person entitled to the information may file an action to compel the company to provide the information and to obtain such other legal or equitable relief as may be proper. If the court finds that the company failed to comply with the requirements of this Section, the court may award the plaintiff its reasonable costs and attorney’s fees incurred in bringing and prosecuting the action. The court may, in connection with any information described in subsection (h), impose such restrictions and conditions on access to and use of such information as it deems appropriate based on the reasonable needs of the company and the member in question.
Can a Trust Really be a Member or a Partner? A potential bomb shell waiting to explode in the California Supreme Court

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California has competing Appellate Court opinions regarding the question of whether a trust can be a partner in a partnership, or a member in a Limited Liability Company. Generally, the California statutes regarding this issue track the language in the various Uniform Acts. Since the first entity in our Committee name is LLC, this short article will look at this question using the California Uniform Limited Liability Company Act provisions.

"Member" is a defined term (Section 17701.02(q)); "a person that has become a member of a limited liability company under Section 17704.01 and has not dissociated under Section 17706.02." "Person" is also a defined term (Section 17701.02(v)): "an individual, partnership, limited partnership, trust, a trustee of a trust...."

Under traditional trust law, a trust, per se, could not be a partner or shareholder. Even with the statutory definition of Member and Person, many trust attorneys still are uncomfortable with the concept of a trust being a Member because under trust law "a trust is not a person but rather a fiduciary relationship with respect to property," and "an ordinary express trust is not an entity separate from its trustees." 1

The issue of a trust being a partner in a California partnership was litigated in Presta v. Tepper. 2 Two men originally formed a partnership to hold title to certain real estate. Their first investment was pursuant to a partnership agreement with both men named individually as the partners. Two subsequent partnership agreements were executed by the two men as trustees of their respective trusts. All three partnerships contained a provision that, upon the death of a partner, the partnership was required to purchase the entire partnership interest of the deceased partner. When one of the men died, his wife, as successor trustee, took the position that, in the two partnerships where he had been trustee, the partner had not died so the interest was not subject to the buyout clause. The trial court ruled that the men, themselves, were partners in all three partnerships, not the trusts. The Appellate Court affirmed, with the following observation: "The fundamental flaw in [the successor trustee's] argument is that it assumes a trust is an entity, like a corporation, which is capable of entering into a business relationship such as a partnership. It is not. It has long been established under California law that an express trust of the type created by Presta and Tepper is merely a relationship by which one person or entity holds property for the benefit of some other person or entity." And at page 914: "The Probate Code governs the type of ordinary express trusts utilized by both Presta and Tepper in this case." So, according to the Court in Presta v. Tepper, the California Probate Code trumps the various entity acts that expressly say that a trust can be a partner or a member. It should be noted that the Presta Court also appears to base its holding on the language of the two partnership agreements which had not been carefully edited from the original agreement to eliminate references to the partners as "he" or "him" instead of "it". And the weight of authority of the Presta holding that a trust cannot be a partner is further subject to attack by the fact that the partners entered the agreements as: "Presta as Trustee for The Ron E. Presta Revocable Trust.....", and likewise for Tepper. For these reasons, it is arguable that the part of the holding that contends a trust cannot be a partner is dicta.

In Han v. Hallberg, 3 the Court of Appeal disagreed with the Presta opinion and held that in California the Revised Uniform Partnership Act adopted in 1994 trumps trust law because it contains a definition of "partner" that specifically includes a trust as a thing (we hesitate to use the word entity) that can be a partner in a California partnership. It would appear that, at least in the Second Appellate District, the Han case would be authority for a trust as a Member of a California LLC as well as a partner in a California partnership. What the result would be in Districts other than the Second and Fourth

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1 California’s RUPA definition of “Person” includes “business trust, estate, trust” but not “trustee of a trust”. The inclusion of “trust” is important for this discussion; it does not appear that leaving out “trustee of a trust” matters since the definition ends with “or any other legal or commercial entity”.

2 Moeller v. Superior Court, 16 Cal. 4th 1124, 1132 fn. 3 (1997).


4 Id at 913. 2d Dist. (2019).

5 35 Cal.App.5th 621
is a guess at this time, and with such a clear split between two Appellate Districts on this issue, it would appear that only a California Supreme Court opinion will set the matter to rest.

As if to respond to our fervent wish, a petition for review of the Han v. Hallberg case was granted on August 21, 2019 by the California Supreme Court, so we may soon have our definitive answer. The grant of the petition specified “The issues to be briefed and argued are limited to the following. Can a trust be a partner in a partnership? Does the death of a partner who has transferred the partnership interest into a trust trigger the buyout-on-death term in the partnership agreement?” The second issue is germane to the case being reviewed. The first issue, if decided in the negative, could create reverberations around the entire country, i.e., in the lesser 49 states. With the definition of “partner” and “member” in virtually all state statutes specifying that a trust may be a partner or member, there must be thousands of agreements in effect with a trust as a partner or member. Each of those agreements may be the subject of litigation in the future. Not only in the case of buyout-on-death triggers, but in questions involving inspection rights of equity holders, standing to bring a lawsuit by the equity holder trust, and so forth. For these, and many other reasons, it would appear to be prudent in all cases to name the trustee as the Member and not the trust.

Let us assume, for the moment, that the California Supreme Court determines that a trust cannot be a partner, i.e., the Probate Code trumps RUPA. What does that mean in the case of a California LLC? As noted at the outset, a Person can be a Member under California law. The full definition of Person is:

“Person” means an individual, partnership, limited partnership, trust, a trustee of a trust, including, but not limited to, a trust described under Division 9 (commencing with Section 15000) of the Probate Code, estate, association, corporation, limited liability company, or other entity, whether domestic or foreign. Nothing in this subdivision shall be construed to confer any rights under the California Constitution or the United States Constitution.

Division 9 of the California Probate Code is essentially the entire law of trusts in California. So, if the Supreme Court determines that the RUPA trumps our Probate Code, will that same result occur in the LLC context where the definition points directly to the Probate Code? Or does the clause in the definition “a trust described under Division 9…of the Probate Clause” refer back only to “a trustee of a trust”?

Inquiring minds seek the answers to these questions.

**Technical Amendments to the New York LLC Act**

Sections 203(e), 206(a), 211(d), 211-A, 213(b), 301(c), 301(e), 301-A(a), 301-A(e), 303(a), 305, 802(a), 804-A, 806(b), 1003(a), 1203(c), 1306(a) and 1306(d) of the New York Limited Liability Company Act were amended by 2019 New York Assembly Bill No. 2008. These amendments relate generally to service of process.
**2019 Amendments to the Kansas LLC Act**

In 2019, the Kansas legislature approved significant amendments to the Kansas Revised LLC Act, particularly with respect to series. Following is a summary of legislation drafted by the Kansas Legislative Research Department as to that legislation (HB 2039).

**Limited Liability Companies; Registration of Animal Shelters; HB 2039**

HB 2039 amends the Charitable Organizations and Solicitations Act to exempt from its registration requirement any charitable organization that is an animal shelter licensed pursuant to the Kansas Pet Animal Act.

The bill also creates and amends law related to limited liability companies (LLCs) in the Kansas Revised Limited Liability Company Act (RLLCA), Business Entity Standard Treatment (BEST) Act, and other statutes, as follows.

**Series LLCs**

The bill creates and amends law related to series LLCs, as follows. [Note: Series LLCs were originally implemented in the RLLCA by 2012 Sub. for HB 2207.]

**Merger or Consolidation of Series LLCs [Section 3]**

The bill creates law effective July 1, 2020, allowing merger or consolidation by one or more series with or into one or more other series of the same LLC with such series as the agreement provides being the surviving or resulting series.

Unless otherwise provided by the operating agreement, the bill requires merger or consolidation to be approved by the vote of the members of each series that is to merge or consolidate who own more than 50 percent of the then-current percentage or other interest in the profits of such series owned by all the members of the series.

The bill allows exchange or conversion of rights or securities of or interests in the constituent series, or allows them to be canceled or remain outstanding. An agreement of merger or consolidation can be terminated or amended pursuant to a provision for such in the agreement.

The bill requires the surviving or resulting series to file with the Secretary of State a certificate of merger or consolidation, executed by authorized persons, which must include:

- The name of the series to be merged or consolidated and the name of the LLC that formed the series;
- That a merger or consolidation agreement has been approved by each series that is to merge or consolidate;
- The name of the surviving or resulting series;
- Any amendment to the certificate of designation of the surviving or resulting series to change the name of the surviving series through the merger;
- The future effective date or time certain, if not effective upon filing;
- That the agreement is on file at a place of business of the surviving or resulting series or the LLC that formed the series, with the address; and
- That a copy of the agreement will be furnished upon request and without cost to any member of any merging or consolidating series.

Unless otherwise provided in the certificate, the merger or consolidation is effective upon the filing of the certificate with the Secretary of State.

A certificate of merger or consolidation acts as a certificate of cancellation of the certificate of designation of the series that is not the surviving or resulting series, and a certificate amending the name of the surviving or resulting series is deemed to be an amendment to the certificate of designation of the surviving or resulting series, with no further action required for such amendment. Any requirement in this section that a certificate of merger or consolidation be filed is deemed satisfied by the filing of a merger or consolidation agreement containing the information required in a certificate of merger or consolidation.
A merger or consolidation agreement may amend the operating agreement of the constituent series, and any amendment relating solely to such series is effective at the effective time or date of the merger or consolidation. Such amendment or adoption is effective notwithstanding any provision in the operating agreement regarding amendment, other than such a provision applicable in connection with a merger or consolidation. These provisions may not be construed to limit the accomplishment of a merger or of any of the referenced matters by any other means provided by an operating agreement or other agreement, or otherwise by law.

The bill provides for various items upon a merger or consolidation becoming effective, including vesting of rights, privileges, powers, property, and debts and attachment and enforcement of rights of creditors, liens upon property, debts, liabilities, and duties.

Unless otherwise agreed, a merger or consolidation of a series that is not the surviving or resulting series does not require such series to wind up its affairs or pay its liabilities and distribute its assets, and the merger or consolidation does not constitute a dissolution of such series.

An operating agreement may provide that a series of the LLC shall not have the power to merge or consolidate.

Series Reinstatement [Section 4]

The bill creates law effective July 1, 2020, allowing a series whose certificate of designation has been canceled to be reinstated by filing with the Secretary of State a certificate of reinstatement, accompanied by payment of the required fee, annual report fee, and all penalties and interest due at the time of the cancellation. The bill requires the certificate to contain the name of the LLC at the time of cancellation and at the time of reinstatement, if changed; the name of the series at the time of cancellation and the name under which the series is to be reinstated, if the original name is not available; a statement that the certificate is filed by persons authorized to do so; and any other matters such persons include.

The certificate of reinstatement is deemed to be an amendment to the certificate of designation and, upon its filing, the series will be reinstated with the same force and effect as if the certificate of designation had not been canceled. The bill sets forth the effect of reinstatement on contracts; acts; matters and things made, done, and performed by the series, its members, managers, employees, and agents during cancellation; real and personal property; all rights and interests; and liability for all contracts, acts, matters, and things made, done, or performed in its name prior to reinstatement.

Restated Certificate of Designation [Section 21]

Effective July 1, 2020, the bill amends the RLLCA statute governing restated articles of organization to add provisions regarding restated certificates of designation. These provisions allow an LLC series to integrate into a single instrument all the provisions of its certificate of designation that are then in effect and operative as a result of certificates or other instruments previously filed with the Secretary of State. The series may, at the same time, further amend its certificate of designation by adopting a restated certificate of designation.

A restated certificate of designation that restates and integrates, but does not further amend, is specifically designated a “restated certificate of designation” and is executed by an authorized person and filed with the Secretary of State as provided in the BEST Act. A restated certificate of designation that restates and integrates, and also further amends, is specifically designated an “amended and restated certificate of designation” and is executed and filed in the same manner as described above.

The bill requires a restated certificate of designation to state the name of the LLC, the present name of the series, the name under which the series was originally filed (if different), and the future effective date or time certain of the restated certificate (if not effective upon filing). The certificate also must state it was duly executed and is being filed in accordance with this section. If the restated certificate only restates and integrates, without further amendment, and there is no discrepancy in provisions, the bill requires the certificate also state this fact.

Upon filing of the restated certificate (or upon the future effective date or time, if provided), the initial certificate of designation is superseded, and the restated certificate is the certificate of designation of the series, but the original effective date of formation of the series
remains unchanged.

Any amendment or change effected in connection with the restatement and integration of a certificate of designation is subject to any other provision of the RLLCA, not inconsistent with these provisions, which applies if a separate certificate of amendment was filed to effect such amendment or change.

Restructuring and Amendment of Series LLC Requirements [Section 39]

Effective July 1, 2020, the main statute governing series LLCs is extensively amended, restructured, and expanded, as follows.

The bill removes much of the current law regarding names, formation, limits on liability, certificates of designation, dissolution, standing, resident agents, management, applicability of law, and foreign LLCs.

Restructuring. Some provisions within the removed law are moved or reworded (without substantive changes) within the statute, including provisions regarding:

- Formation by filing of a certificate of designation with the Secretary of State;
- Notice of limitation on liabilities provided by the articles of organization on file with the Secretary of State;
- Providing for classes or groups of members or managers and voting in an operating agreement;
- Effect of events on a member or manager of a series with regard to any other series or the LLC; and
- Dissolution of a series without dissolving the LLC or affecting the limitation on liabilities.

Additions. The bill adds numerous provisions to law governing series LLCs, as follows.

The bill states a series may be formed by complying with this statute if an operating agreement provides for the establishment or formation of one or more series. A series is prohibited from merging, converting, or consolidating pursuant to any section of the RLLCA, the BEST Act, or any other statute, other than pursuant to the provisions included elsewhere in the bill.

The bill requires notice of the limitation on liabilities of a series be set forth in the articles of organization of the LLC, which is sufficient regardless of whether the LLC has formed any series when such notice is included in the articles of organization, without any specific series of the LLC being referenced in the notice.

The bill adds language stating current and amended language regarding limitation on liability does not restrict a series or LLC from agreeing that debts, liabilities, obligations, and expenses of the LLC may be enforceable against the assets of the series, or vice versa. The bill adds additional provisions regarding holding of assets associated with a series, accounting for the assets of a series, and references to assets, members, or managers of or associated with a series.

The bill provides a series may carry on any lawful business, purpose, or activity, whether or not for profit, except for granting insurance policies, assuming insurance risks, or banking. The bill states a series shall have the power and capacity to contract, hold title to assets, grant liens and security interests, and sue and be sued.

No member or manager of a series is obligated personally for any debt, obligation, or liability of the series, unless the member or manager otherwise agrees or as otherwise provided in the RLLCA.

The bill sets forth various voting provisions that may be included in an operating agreement and states voting may be on any basis, including several specifically listed.

Unless otherwise provided in an operating agreement, the bill vests management of a series in the members associated with such series in proportion to the then-current percentage or other interest of members in the profits of such series owned by all of the members associated with such series, with the decision of members owning more than 50 percent of such percentage controlling. However, if an operating agreement provides for management by a manager, management is vested in the manager accordingly, and the bill gives effect to other operating agreement provisions regarding managers. A series may
have more than one manager.

The bill adds provisions regarding distributions with respect to a series, including status and remedies of a member entitled to a distribution, establishment of a record date by an operating agreement, limitations on distributions related to certain liabilities and the fair market value of the series assets, liability of a member for a distribution in certain circumstances, and the effect of these provisions on certain obligations or liabilities of members.

Unless otherwise provided in the operating agreement, a member ceases to be associated with a series and to have the rights and powers of a member of the series upon the assignment of all the member’s LLC interest in the series.

The bill states a series is dissolved and its affairs shall be wound up upon dissolution of the LLC or upon the first of the following: at the time specified in the operating agreement; upon the happening of events specified in the operating agreement; unless otherwise provided by the operating agreement, upon the vote of series members who own two-thirds or more of the then-current percentage or other interest in the profits of such series of the LLC owned by all the members of the series; or the dissolution of the series under this statute.

Unless otherwise provided in the operating agreement, a series manager who has not wrongfully dissolved the series, or the series members or a person consented to or approved by the series members, by a vote of the members who own more than 50 percent of the then-current percentage or other interest in the profits of such series owned by all of the series members, may wind up the affairs of the series. The district court, upon cause shown, may wind up the affairs of a series and appoint a liquidating trustee upon application by certain persons. The bill sets forth the authority and requirements of the persons winding up the affairs of the series, which do not affect the liability of members or impose liability on a liquidating trustee. On application by or for a member or manager associated with a series, the district court may decree dissolution of the series whenever it is not reasonably practicable to carry on the business of the series in conformity with an operating agreement. A series is an association for all purposes of Kansas law, regardless of the number of members or managers.

The bill sets forth required contents of a certificate of designation filed to form an LLC series, but a certificate of designation properly filed with the Secretary of State prior to July 1, 2020, is deemed to comply with these requirements. The bill requires the certificate of designation be executed and filed in accordance with the BEST Act and states a certificate of designation is not an amendment to the articles of organization of the LLC.

The bill permits amendment of a certificate of designation pursuant to requirements set forth in the bill for a certificate of amendment, but a certificate of designation properly filed with the Secretary of State prior to July 1, 2020, changing a previously filed certificate of designation is deemed to be a certificate of amendment.

The bill requires a manager or member of a series who becomes aware that any statement in a certificate of designation was false when made, or that any matter has changed making the certificate false in any material respect, to promptly amend the certificate of designation. A certificate of designation may be amended at any time for any other proper purpose.

Unless otherwise provided in the RLLCA or unless a later effective date or time certain is provided in the certificate of amendment, the certificate is effective at the time of filing.

The bill sets forth the circumstances under which a certificate of designation must be canceled, including by the filing of a certificate of cancellation pursuant to requirements set forth by the bill. A certificate of designation properly filed before July 1, 2020, dissolving a series is deemed a certificate of cancellation. The bill provides for correction of a certificate of cancellation and prohibits the Secretary of State from issuing a certificate of good standing for a series if the certificate of designation is canceled or if the LLC has ceased to be in good standing.

The bill specifies requirements for the name of the series to be set forth in the certificate of designation.

The bill modifies the required statements related to the series to be included in an application for registration as a foreign LLC.

Other Series LLC Amendments in RLLCA

The bill amends the RLLCA definitions
Effective July 1, 2020, the bill amends RLLCA statutes regarding cancellation of articles of organization, notice by filing with the Secretary of State, fees for documents provided by the Secretary of State, and reinstatement of canceled or forfeited articles of organization to incorporate LLC series. [Sections 17, 19, 36, and 41]

Effective July 1, 2020, the bill amends the RLLCA statute regarding annual reports to include LLC series in its continuing requirements. Additionally, if applicable law does not prescribe a time for filing an annual Kansas income tax return for a series, the bill requires the annual report to be filed at, and its tax period deemed to be, the time prescribed by law for filing the annual Kansas income tax return for the LLC to which the series is associated. [Section 38]

Series LLC Amendments in Other Acts and Codes

The bill amends BEST Act statutes regarding service of process and resignation of resident agents to incorporate LLC series. [Sections 44 and 48]

Effective July 1, 2020, the bill amends BEST Act statutes regarding LLC filings, names of covered entities, reservation of entity names, and name requirements for foreign covered entities to incorporate LLC series, merger or consolidation of series LLCs, and series LLC certificates of designation, as appropriate. [Sections 43, 46, 47, and 49]

The bill amends the Code of Civil Procedure section governing service of process to provide that service on an LLC series may be made in the same manner as continuing methods of service on various corporate entities or resident agents. If service is made on the resident, managing, general, or other agent of the LLC upon which service may be made or the Secretary of State on behalf of any series, the bill requires the service to include the name of the LLC and the name of the series. [Section 50]

The bill amends the Uniform Commercial Code (UCC) general definitions statute (effective July 1, 2020) to include a series within the definition of “person” and amends the UCC Article 9 definitions statute to include a series of a registered organization within the definition of “registered organization,” if the series is formed or organized under the law of a single state and the statute of the state governing the series requires the public organic record of the series be filed with the state. [Sections 51 and 52]

Statutory Public Benefit LLCs [Sections 5-12, 18]

The bill creates (Sections 5-12) and amends (Section 18) law to create a type of LLC known as a “statutory public benefit limited liability company” (SPBLLC), as follows.

Applicability [Section 5]

Sections 5 through 12 of the bill apply to all SPBLLCs, and any SPBLLC is subject to all provisions of the RLLCA except to the extent Sections 5 through 12 impose different requirements, and such requirements may not be altered in an operating agreement.

Definitions and Name [Section 6]

The bill defines “statutory public benefit limited liability company” as a for-profit LLC formed under and subject to the requirements of the RLLCA that is intended to produce a public benefit or benefits and to operate in a responsible and sustainable manner. An SPBLLC is managed in a manner balancing the members’ pecuniary interests, the best interests of those materially affected by the SPBLLC’s conduct, and the public benefit or benefits set forth in its articles of incorporation. Within its articles of organization, the SPBLLC is required to identify specific public benefit or benefits to be promoted and state it is an SPBLLC.

The bill defines “public benefit” to mean a positive effect, or reduction of negative effects, on one or more categories of persons, entities, communities, or interests (other than members in their capacities as members), including various exemplary effects listed in the bill.

The bill defines “public benefit provisions” to mean the provisions of the articles of organization, an operating agreement, or both, contemplated by Sections 5 through 12.

The bill requires, if the name of the SPBLLC does not contain the term “statutory
public benefit limited liability company” or the abbreviation “S.P.B.L.L.C.” or designation “SPBLLC,” the SPBLLC must provide advance notice to any person to whom it is issuing any LLC interest that it is an SPBLLC, unless the issuance is being made pursuant to certain provisions of the Securities Act of 1933 or the Securities Exchange Act of 1934.

Voting Requirements [Section 7]

Unless otherwise provided in the operating agreement, the consent or approval of members who own at least two-thirds of the then-current percentage or other interest in the profits of the LLC owned by all members is required to:

Amend its articles of organization to delete or amend a provision required to comply with the above definition of SPBLLC;

Merge, consolidate, or divide the LLC, if the resulting interests would not be in an SPBLLC with public benefit or benefits and other specified provisions comparable in all material respects to those set forth by the original LLC; or

Cease to be an SPBLLC.

Duties [Section 8]

The members, managers, or other persons with authority to manage or direct the business and affairs of an SPBLLC (managing person) are required to manage or direct the business and affairs of the SPBLLC in a manner balancing the pecuniary interests of the members, the best interests of those materially affected by the SPBLLC’s conduct, and the specific public benefits set forth in the articles of organization. Unless otherwise provided by the operating agreement, such managing person has no liability for monetary damages for the failure to manage or direct in the manner required above.

Such managing person has no duty, by virtue of the public benefit provisions, to any person due to such person’s interest in the identified benefits or materially affected by the SPBLLC’s conduct. Such managing person is deemed to satisfy fiduciary duties to members and the SPBLLC if the managing person’s decision is both informed and disinterested and not such that no person of ordinary, sound judgment would approve.

Statements [Section 9]

An SPBLLC is required to provide to members, at least annually and at the time of the filing of the SPBLLC’s annual report, a statement regarding the LLC’s promotion of the public benefits set forth in the articles of organization and of the best interests of those materially affected by the SPBLLC’s conduct. The bill requires this statement to include objectives established and standards adopted, as well as objective factual information based on those standards regarding the SPBLLC’s success in meeting the objectives and an assessment of the SPBLLC’s success in meeting the objectives and promoting the public benefits and interests. The bill requires the statement be based on a third-party standard, as defined in this new section.

The bill requires an SPBLLC to post its most recent statement on the public portion of its website. If the SPBLLC does not have a website, it must provide a copy of the statement, without charge, to any person requesting a copy, except that compensation paid to any person and any other financial or proprietary information may be omitted from any statement publicly posted or distributed, other than a statement provided to a managing person.

The articles of organization or operating agreement may require the SPBLLC to obtain a periodic third-party certification addressing the SPBLLC’s promotion of its public benefits or the best interests of those materially affected by the corporation’s conduct, or both.

Derivative Lawsuit [Section 10]

Members or assignees of LLC interests in an SPBLLC may maintain a derivative lawsuit to enforce the managing and directing duties set forth in Section 8 of the bill if those members or assignees own (individually or collectively), as of the date of instituting such derivative suit, at least 2 percent of the then-current percentage or other interest in the profits of the LLC, or, for an LLC with LLC interests listed on a national securities exchange, the lesser of such percentage or LLC interests of at least $2.0 million in market value, unless a different percentage or market value is provided by the operating agreement.
Other Provisions

Section 11 states Sections 5 through 12 shall not affect a statute or rule of law applicable to any LLC formed under the RLLCA that is not an SPBLLC. Section 12 states Sections 5 through 12 shall not be construed to limit the accomplishment by another means permitted by law of the formation or operation of an LLC formed or operated for a public benefit, including an LLC designated as a public benefit LLC, that is not an SPBLLC.

A provision of the RLLCA regarding notice provided by documents on file with the Secretary of State is amended to reference the content required to be included in an SPBLLC’s articles of organization by Section 6 of the bill.

Division of LLCs [Sections 2, 16, 20, 35, and 42]

The bill creates and amends law to provide for division of LLCs, as follows.

Dividing a Domestic LLC

The bill creates law (Section 2) allowing a domestic LLC to divide into two or more domestic LLCs, which are not deemed to affect liabilities of persons or obligations or liabilities of the dividing company prior to the division. Such obligations or liabilities are allocated to the division company or companies pursuant to the plan of division. Each resulting company must be formed in compliance with the RLLCA and the provisions created by the bill. The bill defines key terms related to division.

A manner of adopting a plan of division may be specified in an operating agreement. Otherwise, a plan of division may be adopted in the same manner as specified in the operating agreement for a merger or consolidation, if the operating agreement does not prohibit division. If the operating agreement does not provide for merger or consolidation and does not prohibit division, a plan for division may be authorized by the affirmative vote of members who own more than 50 percent of the then-current percentage or other interest in the profits of the dividing company owned by all members.

Unless provided otherwise in the division plan, division does not require an LLC to wind up its affairs or pay its liabilities and distribute its assets and does not constitute a dissolution of the LLC.

The bill allows exchange or conversion of rights or securities of, or interests in, the dividing company, or allows them to be canceled or remain outstanding.

A plan of division may amend the operating agreement of or adopt a new operating agreement for the dividing company if it survives the division and effects the adoption of a new operating agreement for each resulting company, which is effective at the effective time or date of the division. Such amendment or adoption is effective notwithstanding any provision in the operating agreement of the dividing company regarding amendment or adoption of a new operating agreement, other than such a provision applicable in connection with a division, merger, or consolidation.

The bill requires the plan of division to include the terms and conditions of the division, including those regarding conversion, exchange, or cancellation of LLC interests of the dividing company, or whether such shall remain outstanding; allocation of assets, property, rights, series, debts, liabilities, and duties of the dividing company among the division companies; names of the resulting and surviving companies; name and business address of a division contact, who serves for six years following the division and has custody of a copy of the plan of division, which the bill requires the contact to provide to creditors as specified in the bill; and any other matters the dividing company includes.

The bill requires the surviving company and any other division company to file a certificate of division with the Secretary of State for each resulting company. The bill specifies required contents of such certificate of division. The bill requires the articles of organization for each resulting company to be filed simultaneously with the certificate of division, with the same effective date or time if not effective upon filing. A certificate of division acts as a certificate of cancellation for a dividing company that is not a surviving company.

An operating agreement may provide that a domestic LLC shall not have the power to divide.

The bill provides for various items upon a division of a domestic LLC becoming effective, including the effect upon the resulting companies and the dividing company if it is not a surviving company; allocation and vesting of
rights, privileges, powers, property, and debts; liability for allocated debts, liabilities, and duties of the dividing company; allocation and enforcement of debts, liabilities, and duties; liability for fraudulent transfer; liability for non-allocated debts and liabilities; reasonable identification of assets, property, rights, series, debts, liabilities, and duties; vesting of allocated rights, privileges, powers, and interests in property; and continuation of actions or pending proceedings against surviving or resulting companies.

The bill provides, in applying the provisions of the RLLCA on distributions, a direct or indirect allocation of property or liabilities in a division is not deemed a distribution. The new division provisions are not be construed to limit the means of accomplishing a division by any other means provided for in an operating agreement or other agreement or as otherwise permitted by the RLLCA or other law.

The bill provides this section applies to all LLCs formed on and after July 1, 2019. Additionally, it applies to all LLCs formed prior to that date, except that any restriction, condition, or prohibition regarding merger or consolidation in any written contract, indenture, or agreement entered into prior to that date to which the dividing company is a party is deemed to apply to a division.

Amendments to Law

The bill amends the RLLCA statute governing cancellation to include cancellation upon the filing of a certificate of division if the LLC is a dividing company that is not a surviving company. [Section 16]

The RLLCA statute governing restated articles of organization is amended to include a reference to division. [Section 20]

A $20 fee is added for filing of a certificate of division. [Section 35]

The BEST Act statute regarding LLC filings is amended to include certificates of division. [Section 42]

Power of Attorney [Sections 1 and 45]

The bill amends the power of attorney statute in the BEST Act to remove provisions related to formation, internal affairs, or termination of a covered entity or granted by persons in certain roles and focusing the statute on those documents filed with the Secretary of State pursuant to the BEST Act. The statute’s applicability also is limited as otherwise provided in a covered entity’s public organic document or organic rules.

The bill creates a new section in the RLLCA addressing power of attorney. This section provides that, unless otherwise provided in an operating agreement, a person may enter into an operating agreement or amendment by an agent, including an attorney-in-fact, and authorization to do so need not be in writing, sworn, verified, or acknowledged. The section also contains provisions regarding irrevocable powers of attorney and proxies substantially similar to those previously applicable under the BEST Act statute discussed above. The section states it shall not be construed to limit enforceability of a power of attorney or proxy that is part of an operating agreement.

Other RLLCA Provisions

Domestic and Foreign LLCs [Sections 14 and 37]

The definitions section and taxation section are amended to clarify language relating to domestic LLCs and foreign LLCs.

Time of Formation [Section 15]

The bill adds language providing that an LLC is formed at the time provided by the BEST Act statute governing effective date if there has been substantial compliance with RLLCA requirements regarding execution and filing of articles of organization.

Certain Effective Time or Date Limitations Removed [Sections 16, 20, and 22]

The bill removes limitations on the future effective date or time of certificates of cancellation, restated articles of organization, and certificates of merger or consolidation.

Merger or Consolidation [Section 22]

A provision allowing exchange or conversion of rights or securities of, or interests in, an LLC that is a constituent party to a merger or consolidation into rights or securities of, or interests in, an LLC that is not the surviving or resulting LLC in the merger or consolidation is
amended to instead allow exchange or conversion into rights or securities of, or interests in, an entity as defined in the BEST Act that is not the surviving or resulting LLC. This provision also is amended to specify the rights or securities of or interests in the constituent party LLC may remain outstanding.

Voting [Sections 22, 32, and 33]

The bill changes certain default voting requirements for those LLCs formed after June 30, 2019. For votes on agreements of merger or consolidation or to dissolve and wind up an LLC, the required vote must be by the members owning more than the specified percentage of the then-current percentage or other interest in the profits of the LLC owned by all the members. Continuing voting requirements for those LLCs formed on or prior to June 30, 2019, are by each class or group of members, if the LLC has more than one class or group of members.

Access to Information; Records [Section 25]

A statute regarding LLC records and access to information is amended to permit an attorney or other agent for an LLC member to obtain certain information that may be obtained by the member under continuing law. Such demand on behalf of a member must be accompanied by a power of attorney or other writing authorizing the attorney or other agent to so act on the member's behalf.

This statute also is amended to require an LLC to maintain a current record identifying the name and last known business, residence, or mailing address of each member and manager, and to allow the use of electronic networks or databases, including distributed electronic networks or databases, to maintain records.

Delegation [Section 27]

The statute governing the delegation of rights and powers to manage is amended to allow the delegation of duties. The bill removes a phrase specifically allowing the delegation of the right or power to delegate. The bill adds that a delegation by a member or manager must be irrevocable if it states it is irrevocable, unless otherwise provided in the operating agreement. The bill also adds that no other provision of the RLLCA shall be construed to restrict the power and authority to delegate as provided in this section.

Limitation of Remedies [Section 30]

The RLLCA continues to provide the entry of a charging order is the exclusive remedy by which a judgment creditor of a member or assignee may satisfy a judgment out of the judgment debtor's LLC interest. The bill adds to this provision that attachment, garnishment, foreclosure, or other legal or equitable remedies are not available to the judgment creditor, regardless of the number of members of the LLC.

Membership of Single Assignee [Section 31]

The bill adds a provision that, unless otherwise provided in the operating agreement by specific reference or in connection with the assignment, an assignee of an LLC interest becomes a member upon the voluntary assignment by the sole member of an LLC of all the LLC interests in the LLC to a single assignee. An assignment is voluntary if it is consented to or approved by the member at the time of the assignment and is not effected by foreclosure or similar legal process.

Fiduciary Duties [Section 34]

The bill specifies the rules of law and equity relating to fiduciary duties are among those rules of law and equity that are to apply where not otherwise provided in the RLLCA.

Revocation of Dissolution [Section 40]

The bill amends the statute preventing dissolution in certain circumstances to specify a dissolution may be revoked in a manner specified in an operating agreement or an operating agreement may prohibit revocation of dissolution. Provisions describing the default circumstances under which dissolution may be revoked are restructured and amended to allow revocation of:

- A dissolution effected by vote, consent, or approval, pursuant to the vote, consent, or approval and by approval of any others as required by the operating agreement;
- A dissolution at a specified time or upon a specified event, by vote, consent, or approval required to
amend the provision of the operating agreement effecting the dissolution and by approval of any others as required by the operating agreement; and

- A dissolution effective upon the last remaining member ceasing to be a member, by vote, consent, or approval of the personal representative of the last remaining member of the LLC or the assignee of all the LLC interests in the LLC and by approval of any others required by the operating agreement.

This statute also is amended to include the assignee of all the LLC interests in the LLC in the procedure to be followed to admit a nominee or designee in certain circumstances, and to provide that the statute shall not be construed to limit the accomplishment of revocation of dissolution by other means permitted by law.

Consent and Approval

The bill adds provisions allowing a person to give consent or approval as a member or manager of any matter and make such consent or approval effective at a future time, including upon the happening of an event. Such consent or approval is effective as long as the person is a member or manager at the future time specified, unless otherwise provided in an operating agreement. [Sections 23 and 26]

Throughout the bill, requirements that consent or approval be in writing are removed. References to consent or to approval are standardized with references to both consent and approval.

Electronic Networks and Databases

Throughout the bill, provisions are added allowing the use of electronic networks or databases, including distributed electronic networks or databases, for certain electronic transmissions.

Non-substantive and Technical Amendments

The bill amends the RLLCA section governing resignation from an LLC to replace a reference to a previous version of the section with the actual language (with slight non-substantive revisions) of the previous version of the section. [Section 28]

Throughout the RLLCA, the bill replaces references to “this act” with “the Kansas revised limited liability company act.”

This summary of the 2019 Amendments to the Kansas LLC Act was prepared and published by the Kansas Legislative Research Department.

Diversity Jurisdiction and the Classification of Non-US Business Entities

For purposes of being able to access the federal courts via diversity jurisdiction, a crucial question is whether a business entity will be treated as incorporated, in which case it will have the citizenship of its jurisdiction of incorporation and that of its principal place of business, or unincorporated, in which it will have the citizenship of each of its members. In Jet Midwest International Co. Ltd. v. Jet Midwest Group, LLC, 2019 WL 3540060 (8th Cir. Aug. 2, 2019), the court was called upon to determine whether a limited company organized in Hong Kong would be treated as incorporated or unincorporated.

Adopting the test employed by the Seventh Circuit Court of Appeals, it was held at a Hong Kong limited company is equivalent to a US corporation for purposes of diversity jurisdiction. The decision collects a number of decisions from other jurisdictions coming to the same conclusion.
Messler v. Cotz

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Nowadays, with the use of LLCs (and before that limited partnerships), we don't see too much law involving general partnerships. A recent Dan Kleinberger article teaches that in general partnerships owners are personally liable for the debts of the business merely on account of being owners. That had been my understanding of general partnership law until Messler v. Cotz,¹ involving New Jersey law, caught my eye. In a split decision the majority affirmed summary judgment dismissing Lydia Cotz from the plaintiff's action for malpractice allegedly committed by George Cotz, notwithstanding the name of the law firm she engaged as shown on its letterhead was Cotz & Cotz, attorneys-at-law, followed by the names of both George J. Cotz and Lydia B. Cotz. Plaintiff, who had been recommended to the firm Cotz & Cotz, met only with George but signed a retainer agreement on the letterhead described above.

The majority said that plaintiff did "not assert that Mr. and Ms. Cotz were actually partners," that the sole issue was whether there was a partnership-by-estoppel; and that RUPA requires reliance by plaintiff on the fact that Lydia was George's partner. The majority was impressed that "no legal entity named 'Cotz & Cotz' existed and the Cotzs' had never entered into a partnership agreement." (And here I thought a general partnership was common law entity.)

The motivation behind partnership statutes authorizing LLPs some thirty or so years ago was, I thought, the protection innocent professionals from liability arising from the malpractice of a partner. The majority opinion appears to have granted protection to an innocent partner without the firm having taken the steps necessary to become an LLP.

I find the dissent more persuasive.

Recent Amendments to the Nevada LLC Act

Senate Bill No. 427 made several amendments to the Nevada LLC Act. Section 1 of the Bill addresses resignation of the registered agent, deleting the requirement that they submit an affidavit that each represented entity had been notified of the resignation. That is been replaced simply with a commitment to provide that notice.

Sections 11 through 28 of the Bill enable both certain creditors and certain members of an insolvent LLC to file an application for appointment of a receiver.

With respect to any insolvent or dissolved LLC, the employees are collectively afforded a lien, limited to $1,000, for the payment of wages earned but not paid in the three months before the date of insolvency or dissolution. This lien has priority over "any other debts of the company." For these purposes, neither a manager nor the managing members of the LLC constitute "employees."

2019 Amendments to Delaware’s General Corporation Law and Alternative Entity Statutes

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In its 2019 session, the Delaware legislature passed a number of amendments to the Delaware General Corporation Law and the Delaware “alternative entity” statutes—the Delaware Limited Liability Company Act, the Delaware Revised Uniform Limited Partnership Act, and the Delaware Revised Uniform Partnership Act. Except as noted below, all of the amendments became effective on Aug. 1, 2019.

The amendments to the DGCL effected a number of substantive, technical, and clarifying changes, including changes related to the electronic execution and delivery of documents and the effectiveness of electronic notices.

The amendments to the alternative entity statutes include a number of significant substantive changes to the DRULPA (which were generally based on similar changes to the DLLCA that were adopted last year) and, as described below, create a new type of limited partnership series known as registered series, permit registered series of the same limited partnership to merge or consolidate, permit a limited partnership statutorily to divide into two or more limited partnerships, and create statutory public benefit limited partnerships. The amendments to the DLLCA, the DRULPA and the DRUPA also confirm that it is permissible under those statutes to document, sign and deliver certain types of transaction documents through DocuSign and similar electronic means.

This article will first discuss the amendments to the DGCL and then the amendments to the alternative entity statutes.

Amendments to the DGCL

Organization Meetings. Section 108 governs the initial organization meeting of incorporators (or of directors, if named in the certificate of incorporation). Section 108(b) has been amended to clarify that notice and waiver of notice of an initial organization meeting may be given by electronic transmission. Section 108(c), which allows any action permitted to be taken at an initial organization meeting to be taken by consent in lieu of a meeting, has been amended to provide that any such consent may become effective at a future date or upon the happening of a future event, consistent with the provisions relating to board consents under Section 141(f).

E-Sign and E-Delivery. A new Section 116 has been added. Section 116(a) provides a “safe harbor” for memorializing, executing and delivering certain documents electronically under the DGCL or the governing documents of a corporation. For example, under Section 116(a), a voting agreement signed and delivered through DocuSign would be equally valid as a manually signed and delivered voting agreement. Section 116(a) provides that delivery by electronic transmission is deemed to have occurred when the transmission enters an information processing system designated by the recipient, and that such designation need not be express and may be determined “from the context and surrounding circumstances, including the parties’ conduct.”

Section 116(b) excludes from the safe harbor of Section 116(a) certain acts and transactions, such as documents filed with the Secretary of State, notices, stock certificates and ledgers, and board and stockholder consents, which are each governed by separate provisions of the DGCL. Corporations may opt-out of the Section 116(a) safe harbor through a certificate of incorporation or bylaw provision expressly prohibiting electronic signatures or electronic delivery (or other means of executing and delivering a document permitted by Section 116). Section 116(c) provides that the DGCL shall govern the documentation of actions, and the signature and delivery of documents, to the fullest extent that the DGCL is not preempted by the E-Sign Act. 15 U.S.C. §§ 7001 et. seq.
Resignations of Registered Agents.
Section 136, which provides that a registered agent may resign by filing a certificate of resignation with the Secretary of State, has been amended to expressly permit a registered agent of a void corporation to resign. The amendments to Section 136 also add additional requirements with respect to the certificate of resignation. The certificate of resignation must be on the form provided by the Secretary of State and must include the last known contact information for the corporation.

Effectiveness of Board Consents.
Section 141(f), which provides for board action by consent in lieu of a meeting, has been amended to clarify that a unanimous consent of a board of directors, or a committee thereof, need not be filed with the minutes of proceeding of the board or committee to become effective. Instead, Section 141(f) requires that the consents be filed with the minutes of the proceedings after the action is taken.

Notices of Redemptions and Payments on Partly Paid Stock.
Section 160(d), which provides for notice to stockholders whose shares are called for redemption by the corporation, and Section 163, which governs calls for payment in respect of partly paid stock, have each been amended to provide that the notices required by these sections may be given in the form, and delivered in the manner, permitted by amended Section 232.

Proxies.
Section 212(c) and (d), which describe the means by which a stockholder may authorize another person to act as the stockholder’s proxy, have been amended to conform to the terminology in Section 116(a), discussed above, and to clarify that a proxy may be memorialized, executed and delivered in accordance with Section 116.

Notices of Stockholder Meetings.
Section 222(a) and (b), which govern notices of stockholder meetings, have been amended to conform to amended Section 232, which permits a corporation to provide notices electronically. Under Section 222, notices of stockholder meetings can be given in writing or by electronic transmission.

Delivery of Stockholder Consents.
Section 228 permits stockholders to take action by consent in lieu of a stockholder meeting, unless action by consent is prohibited in the certificate of incorporation. Section 228(d) has been amended to permit stockholder consents to be delivered to an information processing system designated by the corporation, such as a designated email address. The amendments eliminate the requirement that stockholder consents delivered electronically must be reproduced in paper form in order to be deemed delivered. Instead, a stockholder consent delivered to an information processing system is deemed delivered when it enters the information processing system, even if no one is aware of its receipt.

Returned Mail Exception.
Under Section 230(b)(1), whenever notice is required to be given to any stockholder by the DGCL, or a certificate of incorporation or bylaw provision, notice need not be given to a stockholder if two consecutive annual meeting notices have been mailed to the stockholder’s address but returned as undeliverable (the “Returned Mail Exception”); however, the applicable notice requirements are reinstated after the stockholder provides the corporation with a current address. Under Section 230(c), the Returned Mail Exception does not apply if the returned notices were sent by electronic transmission. Section 230(c) has been amended to provide that the Returned Mail Exception also does not apply even if the corporation has an email address for the stockholder and notice to such stockholder by email is permitted by Section 232.

Electronic Notice.
Section 232 allows corporations to provide notice by electronic transmission. Section 232(a) has been amended to provide that notices under the DGCL or a certificate of incorporation or bylaw provision may be effectively given by email, unless a stockholder has notified the corporation of an objection to email notice. Email notices must include a prominent legend that the communication is an important notice regarding the corporation. Amendments to Section 232(b) (formerly Section 232(a)) provide that notices to stockholders given by other forms of electronic transmission shall be effective if given by a form of electronic transmission consented to by the stockholder and that such consent shall be revocable by the stockholder by written or electronic notice to the corporation. Section 232(d) has been amended to define “electronic mail” and “electronic mail address.”

Importantly, “electronic mail” is deemed to include attachments and any information
accessible via a hyperlink in the email if the email includes the contact information of an officer or agent of the corporation who is available to assist with accessing such files and information. The ability of a corporation to deliver notices electronically pursuant to Section 232 is subject to two important exceptions. First, under Section 232(e), a corporation may not give notice electronically after it becomes aware that two consecutive notices were not successfully delivered. Second, Section 232(g) lists certain notices under the DGCL that are not governed by Section 232 because other provisions control: Section 164 (notices in connection with the sale of stock held by a delinquent stockholder), Section 296 (notices to creditors by trustees or receivers), Sections 311 and 312 (notices of special stockholder meetings in connection with the revocation of a voluntary dissolution or revival) and Section 324 (attachment and sale of stock).

Other Conforming Amendments for Electronic Notice. Sections 251(c), 253(a), 255(c), 266(b) and 390(b), which govern mergers, consolidations, conversions, transfers and domestications, have been amended to provide that the notices of stockholder meetings required by these sections may be given in the form, and delivered in the manner, permitted by amended Section 232. Similarly, Section 275(a), which governs the notice of a stockholder meeting for the approval of dissolution, has been amended to provide that such notice may be given in the form, and delivered in the manner, permitted by amended Section 232.

Execution of Merger Agreements. Sections 251(b) and 255(b), which set forth the requirements for merger agreements, have been amended to permit any authorized person to execute an agreement of merger or consolidation. However, any such agreement filed with the Secretary of State must be executed in accordance with Section 103.

Appraisal Notices and Demands. Section 262 entitles a stockholder to the right to have the fair value of its stock appraised by the Delaware Court of Chancery when the corporation is party to certain mergers or consolidations. Section 262(d) has been amended to provide that a stockholder may deliver a demand for appraisal by electronic transmission to an email address (or other information processing system) expressly designated in the notice of appraisal rights. Similarly, Section 262(e) has been amended to provide that a stockholder may request the information described in that section by an electronic transmission directed to an email address (or other information processing system) expressly designated in the notice of appraisal rights. Additionally, amendments to Section 262(d) and (e) provide that a corporation may deliver a notice of appraisal rights and a 262(e) notice in any manner permitted by amended Section 232(a), including by electronic transmission. The amendments to Section 262 are effective only with respect to a merger or consolidation consummated pursuant to an agreement entered into on or after August 1, 2019.

Revival of Exempt Corporations. Section 313 governs the procedures for reviving an exempt corporation whose certificate of incorporation has become forfeited for failing to pay franchise tax or failing to file annual franchise tax reports. Section 313(a) has been amended to provide that the procedures of Section 313 also apply to an exempt corporation whose certificate of incorporation has become forfeited as a result of the corporation's failure to obtain and designate a new registered agent prior to the expiration of the 30-day period after its registered agent resigned.

Secretary of State Fees. Section 391(a)(11) has been amended to provide for the maximum fee payable to the Secretary of State for any certificate issued through the Secretary of State's online services. Section 391(a)(16) has been amended to increase the fee payable to the Secretary of State for a written report of a record search.

Franchise Taxes. Section 503(h) has been amended to reflect increases to the amount of annual franchise tax payable by a regulated investment company. The amendments to Section 503(h) are effective for the tax year beginning on January 1, 2019.

Amendments to the DRULPA

Registered Series and Protected Series. The amendments create a new type of series known as registered series, which are similar to registered series formed under Section 18-218 of the DLLCA. Registered series are addressed in new Section 17-221 of the DRULPA (with related and conforming amendments to a number of other sections). Section 17-218 of the DRULPA, which previously addressed series, was amended to
provide that series formed under Section 17-218(b) of the DRULPA (both before and after the amendments became effective) will be known as protected series. The provisions relating to registered series are similar to the provisions relating to protected series with several notable exceptions.

First, in order to facilitate the use of registered series in secured financing transactions, registered series are designed to qualify as registered organizations under the Uniform Commercial Code. Thus, a certificate of registered series is required to be filed with the Secretary of State to form a registered series, and the name of a registered series must begin with the name of the limited partnership and be distinguishable from the names of other Delaware business entities or business entities qualified or registered to do business in Delaware (Article 9 of the Delaware Uniform Commercial Code was also amended effective Aug. 1, 2019 to provide that a registered series constitutes a “registered organization”).

Second, one or more registered series of a limited partnership may merge or consolidate with or into one or more other registered series of the same limited partnership. Third, certificates of good standing and certificates of existence with respect to registered series will be issued by the Secretary of State. Fourth, a protected series of a limited partnership may convert to a registered series of the same limited partnership and a registered series of a limited partnership may convert to a protected series of the same limited partnership. Finally, an annual franchise tax in the amount of $75 per registered series will be required to be paid.

Division of a Limited Partnership. Pursuant to new Section 17-220 of the DRULPA, a limited partnership may divide into one or more newly formed limited partnerships, with the dividing limited partnership either continuing its existence or terminating as part of the division. A division of a limited partnership is effected by the adoption of a plan of division setting forth the terms and conditions of the division, including, among others, the allocation of assets, property, rights, series, debts, liabilities and duties of the dividing limited partnership among the resulting limited partnerships and, if it survives, the dividing limited partnership; and the filing with the Secretary of State of a certificate of division and a certificate of limited partnership for each newly formed limited partnership.

A plan of division will be given effect to divide the assets and liabilities of a limited partnership among the resulting limited partnerships and, if it survives, the dividing limited partnership, so long as the plan of division does not constitute a fraudulent conveyance under applicable law. With respect to any limited partnership formed prior to Aug. 1, 2019 that is party to any written contract, indenture or other agreement entered into prior to Aug. 1, 2019 that by its terms restricts, conditions or prohibits such limited partnership from (x) consummating a merger or consolidation with or into another party or (y) transferring assets, such restriction shall be deemed to apply to a division as if it were a merger or consolidation or transfer of assets.

The amendments also adopted a new subsection 17-301(b)(4) of the DRULPA to provide that a person is admitted as a partner of a division partnership pursuant to a division approved in accordance with Section 17-220 of the DRULPA as provided in the partnership agreement of such division partnership or in the plan of division and, in the event of any inconsistencies, the plan of division controls.

New subsection 17-301(b)(4) also provides that a person is admitted as a partner of a limited partnership pursuant to a division in which such limited partnership is not a division partnership in such division (for example, when interests are issued by such limited partnership) as provided in the partnership agreement of such limited partnership. The division provisions should prove to be valuable tools in limited partnership transactions including secondary sale transactions.

Statutory Public Benefit Limited Partnerships. Under the amendments, new subchapter XII of the DRULPA authorizes the creation of statutory public benefit limited partnerships, which are similar to public benefit corporations organized under subchapter XV of the Delaware General Corporation Law and public benefit limited liability companies formed under subchapter XII of the DLLCA. Subchapter XII of the DRULPA is intended to provide a simple and efficient “opt-in” procedure for forming a public benefit limited partnership. As with a public benefit corporation and a public benefit limited liability company, a statutory public benefit limited partnership is intended to produce a public benefit and to operate in a
responsible and sustainable manner. New subchapter XII of the DRULPA does not limit the formation or operation of a limited partnership formed or operated for a public benefit (including a limited partnership designated as a public benefit limited partnership) that is not a statutory public benefit limited partnership.

Judicial Cancellation of Certificate of Limited Partnership. The amendments include new Section 17-112, which is similar to Section 18-112 of the DLLCA and grants the Court of Chancery jurisdiction to cancel a certificate of limited partnership for abuse or misuse of such limited partnership’s powers, privileges or existence upon a motion by the Attorney General. Upon such cancellation, the Court of Chancery has the power, by appointment of trustees, receivers or otherwise, to administer and wind up the affairs of such limited partnership.

Amendments to the DLLCA

Admission of a Member to a Limited Liability Company in Connection with a Division. New subsection 18-301(b)(4) of the DLLCA provides that a person is admitted as a member of a division company pursuant to a division approved in accordance with Section 18-217 of the DLLCA as provided in the limited liability company agreement of such division company or in the plan of division and, in the event of any inconsistencies, the plan of division controls. New subsection 18-301(b)(4) also provides that a person is admitted as a member of a limited liability company pursuant to a division in which such limited liability company is not a division company in such division (for example, when interests are issued by such limited liability company) as provided in the limited liability company agreement of such limited liability company.

Amendments to the DRUPA

Distributed Ledgers and Blockchain. The amendments to Sections 15-501 and 15-403 provide express statutory authority to use networks of electronic databases, including distributed ledgers and blockchain, to create or maintain records of the entity and for certain electronic transmissions. These amendments are similar to those made last year to the DLLCA and the DRULPA and confirm that this rapidly advancing technology is available to be used with respect to general partnerships.

Amendments Common to Multiple Alternative Entity Statutes

Electronic Transactions. The amendments to the DRUPA, the DRULPA and the DLLCA enact new Sections 15-124, 17-113 and 18-113 to create a safe harbor provision that clarifies when acts and transactions contemplated by the DRUPA, the DRULPA and the DLLCA, as applicable, may be documented, signed and delivered electronically. The provisions are generally based on the electronic delivery rules under Delaware’s Uniform Electronic Transactions Act and, in recognition of the increasing prevalence of the use of electronic signatures in many investment and financing transactions, permit various contracts including operating agreements and merger agreements to be adopted, executed and delivered via DocuSign and similar electronic processes. A small class of documents is excluded from the new electronic rules, including documents filed with the Secretary of State, the Delaware Register in Chancery, or a Delaware court or other judicial or governmental body and certificates evidencing interests in partnerships, limited partnerships and limited liability companies.

Definitions of Manager, Member, General Partner and Limited Partner. Under the amendments, the definitions of manager and member in DLLCA Section 18-101(12) and (13) include a manager or member of a limited liability company generally and a manager or member of, or associated with, a series of such limited liability company, and the definitions of general partner and limited partner in DRULPA Section 17-101(7) and (10) include a general partner or limited partner of a limited partnership generally and a general partner or limited partner of, or associated with, a series of such limited partnership. These amendments make clear that references to members, managers, general partners, or limited partners in the provisions of the DLLCA and the DRULPA that do not specifically reference series include references to the members, managers, general partners or limited partners of, or associated with, the series of a limited liability company or limited partnership without having to restate that language in each provision.
Recent Amendments to Delaware’s Entity Laws

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The Delaware legislature recently adopted amendments to the Delaware Revised Uniform Limited Partnership Act (DRULPA) that permit the “division” of Delaware limited partnerships (LPs), formation of “statutory public benefit” LPs, judicial cancellation of an LP for abuse, and formation of LP “registered series.”\(^1\) Those amendments are in most respects similar to amendments adopted in 2018 to the Delaware Limited Liability Company Act (DLLCA).\(^2\) In addition, the recent amendments have, among other things, made Delaware corporations’ use of e-mail for stockholder notices valid except as to stockholders who opt out (thus switching from the prior opt-in regime) and clarified the law regarding the use of electronic transmission and electronic signatures under the DRULPA, the DLLCA, and the General Corporation Law of the State of Delaware (DGCL). Except as otherwise indicated, all of the amendments discussed below took effect on August 1, 2019.

DRULPA Amendments Corresponding to 2018 DLLCA Amendments

The DLLCA was amended last year to permit the division of limited liability companies (LLCs), the formation of statutory public benefit LLCs, judicial cancellation of an LLC for abuse or misuse, and, effective August 1, 2019, the formation of LLC registered series. Now analogues of those provisions have been added to the DRULPA by the 2019 amendments.

Division

The division provisions enable an LP to “divide” into multiple LPs and to allocate its assets and liabilities among those LPs without thereby effecting a transfer for purposes of Delaware law.\(^3\) The LP undertaking the division (termed the “dividing partnership”) may, but need not, survive the division.\(^4\) If it does not survive, the dividing partnership is not deemed by default to have dissolved as a result of the division, but instead simply ceases to exist as a separate entity.\(^5\) The terms of the division must be set forth in a “plan of division,” which shall include, among other things, the terms (if any) on which interests in the dividing partnership will be canceled or converted into interests in another entity or the right to receive cash, and how the assets and liabilities of the dividing partnership will be allocated in the division.\(^6\) A division is effectuated by the dividing partnership’s filing of a certificate of division with the Delaware secretary of state and the simultaneous filing of a certificate of limited partnership for each LP formed in the division.\(^7\)

Presumably because general partners of LPs are not afforded limited liability, division of an LP requires the approval of any person that, upon the effectiveness of the division, will be a general partner of any LP formed by or surviving the division.\(^8\) In addition, a division requires, by default, the approval of all general partners of the dividing partnership and a majority-in-interest of its limited partners.\(^9\) Any action pending against a general partner of a dividing partnership at the time of its division will be unaffected by the division and may be maintained not only against that general partner, but also against any general partner of any LP to which an asset or liability associated with the

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\(^{2}\) The 2018 amendments to the DLLCA authorizing division, statutory public benefit companies, judicial cancellation, and registered series are described in detail in the September 2018 Delaware Transactional & Corporate Law Update.
pending action is allocated in the division. 10

The 2019 amendments have also made some changes affecting the LLC division provision adopted in 2018. First, the amendments have clarified that a certificate of division must be filed by the LLC undertaking the division (the dividing company), as opposed to any entity formed in the division. 11 Second, it now appears that, in the absence of fraud, the allocation of liabilities under the plan of division will determine the identity of the defendant LLC or LLCs in the continuation, post-division, of an action that was pending against the dividing company at the time of its division. 12 Third, the amendments have added language providing that in a division, members may be admitted to an LLC formed by or surviving the division, in accordance with the operating agreement of such LLC or the plan of division. 13 Provisions parallel to these DLLCA amendments were included in the DRULPA amendments respecting division. 14

Statutory Public Benefit LPs

Like the 2018 DLLCA amendments permitting the formation of statutory public benefit LLCs (SPB-LLCs), the 2019 amendments to the DRULPA now permit the formation of statutory public benefit LPs (SPB-LPs). 15 The SPB-LP provisions generally track those adopted last year regarding SPB-LLCs. 16 An SPB-LP is a “for-profit” LP that is “intended to produce a public benefit or public benefits and to operate in a responsible and sustainable manner.” 17 Its certificate of limited partnership must state in the heading (but not necessarily in the SPB-LP’s name) that it is an SPB-LP and must “set forth one or more specific public benefits to be promoted” by the SPB-LP. 18 For purposes of an SPB-LP, a public benefit is “a positive effect (or reduction of negative effects) on one or more categories of persons, entities, communities or interests (other than partners in their capacities as partners) including, but not limited to, effects of an artistic, charitable, cultural, economic, educational, environmental, literary, medical, religious, scientific or technological nature.” 19

The general partners of an SPB-LP are obligated to manage it “in a manner that balances the pecuniary interests of the partners, the best interests of those materially affected by the limited partnership’s conduct, and the specific public benefit or public benefits set forth in its certificate of limited partnership.” 20 Importantly, however, the amendments, by default, insulate the general partners of an SPB-LP from monetary damages for the failure to manage its affairs in accordance with that duty. 21 Moreover, no general partner shall have a duty, by virtue of the statutory public benefit provisions, “to any person on account of any interest of such person in the public benefit or public benefits set forth in its certificate of limited partnership or on account of any interest materially affected by the limited partnership’s conduct[].” 22

Judicial Cancellation

Judicial cancellation of an LP upon motion by the Delaware attorney general is now provided for in new section 17-112 of the DRULPA, which tracks section 18-112 added to the DLLCA in 2018. 23 Under section 17-112, if the attorney general so moves, the Delaware Court of Chancery may cancel an LP’s certificate of limited partnership “for abuse or misuse of its limited partnership powers, privileges or existence.” 24 In the event of a cancellation under section 17-112, the Court of Chancery is empowered, “by appointment of trustees, receivers or otherwise, to administer and wind up the affairs” of the LP, and to “make such orders and decrees with respect thereto as shall be just and equitable respecting its affairs and assets and the rights of its partners and

10 Id. § 17-220(l)(9).
11 Id. § 18-217(h).
12 Id. § 18-217(l)(9).
13 Id. § 18-301(b)(4). The plan of division will control in the event that its terms conflict with the terms of an operating agreement respecting the admission of members in a division. Id.
14 6 Del. C. §§ 17-220(h), (l)(9), 17-301(b)(4).
15 Id. §§ 17-1201 to 17-1208.
16 See id. §§ 18-1201 to 18-1208.
17 Id. § 17-1202(a).
18 Id.
19 Id. § 17-1202(b).
20 6 Del. C. § 17-1204(a).
21 Id.
22 Id. § 17-1204(b).
23 Id. §§ 17-112 (for LPs), 18-112 (for LLCs).
24 Id. § 17-112(a).
Registered Series

The DRULPA and the DLLCA have permitted the establishment of series of assets, interests, and partners or members, as the case may be, since 1996. Both acts also specify certain conditions that, if met, will cause the assets associated with a given series to be shielded from claims of creditors against other series or against the entity as a whole. In the case of an LP, a general partner associated with a given series could be similarly shielded from claims against other series or the LP itself. Under the DRULPA and the DLLCA as amended, such shielded series are now termed “protected series.”

Amendments to the DLLCA adopted in 2018, but not effective until August 1, 2019, enable LLCs to establish registered series, which constitute “registered organizations” under Article 9 of the UCC. Thus, unlike the case with nonregistered series (including protected series), an Article 9 security interest in most types of assets of a registered series can be perfected simply by filing a UCC financing statement with the Delaware secretary of state, regardless of where the series’ principal place of business may be located. It is important to note, however, that a registered series will not have the shielding characteristics of a protected series unless the LLC complies with the notice and other requirements for shielding set forth in the DLLCA.

The 2019 amendments have added comparable provisions to the DRULPA, effective August 1, 2019, allowing LPs to form registered series. An LP registered series is formed by filing, with the Delaware secretary of state, a certificate of registered series, which must contain the name of the LP, the name of the registered series, and the name and address of each general partner associated with the registered series. The registered series’ name must begin with the full name of the LP, and at least one general partner must be associated with each registered series.

An LP registered series, like an LLC registered series, can be dissolved independently, can merge with another registered series of the same entity, can be revived if it loses good standing, and can convert into a protected series of the same entity. (Series conversion can also be from protected to registered.) For each registered series of an LP, an annual tax of $75 must be paid to the state.

As with divisions, the 2019 amendments have also made some changes affecting the LLC registered-series provisions adopted in 2018. These include amendments clarifying that references in the DLLCA to “members” and “managers” include members and managers associated with a series, and confirming that any shielding characteristics a protected or registered series may have will not be lost solely because a different registered series has failed to pay its annual tax in Delaware. Provisions parallel to these DLLCA amendments are included in the DRULPA amendments respecting registered series.

Notice Provided by Corporations to Stockholders by E-mail

The provisions of the DGCL that pertain generally to the means by which a corporation may give notice to stockholders have been substantially revised and reorganized. The most important aspect of these changes affects the default rules governing notice to stockholders by electronic means. Before the 2019 amendments, the DGCL provided that notice to a stockholder by electronic transmission was effective only if the stockholder had consented to receive notice

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25 Id. § 17-112(b).
26 6 Del. C. §§ 17-218 (for LPs), 18-215 (for LLCs).
27 Id. §§ 17-218(b) (for LPs), 18-215(b) (for LLCs).
28 Id. § 17-218(b).
29 Id. §§ 17-101(18), 17-218(b) (for LPs) and 18-101(14), 18-215(b) (for LLCs).
30 Id. § 18-218; U.C.C. § 9-102(a)(71).
31 6 Del. C. § 18-218(c).
32 Id. § 17-221.
33 Id. § 17-221(d).
34 Id. § 17-221(e).
35 Id. § 17-221(c)(1).
36 Id. §§ 17-221(c)(10) (dissolution), 17-224 (merger), 17-1112 (revival), 17-223 (conversion to protected series).
37 6 Del. C. § 17-222.
38 Id. § 17-1109(a).
39 Id. § 18-101(12)-(13).
40 Id. § 18-1107(n).
41 Id. §§ 17-101(7), (10), 17-1109(m).
in the form in which it was given.\textsuperscript{42} The amendments have reversed this rule insofar as it applied to e-mail. Now a corporation may give effective notice to a stockholder by “electronic mail” unless the stockholder has opted out.\textsuperscript{43} In addition, to be effective, notice by e-mail “must include a prominent legend that the communication is an important notice regarding the corporation.”\textsuperscript{44}

“Electronic mail” is defined as “an electronic transmission directed to a unique electronic mail address” and is “deemed to include any files attached thereto and any information hyperlinked to a website if such electronic mail includes the contact information of an officer or agent of the corporation who is available to assist with accessing such files and information[.]”\textsuperscript{45} An “electronic mail address” is “a destination, commonly expressed as a string of characters, consisting of a unique user name or mailbox . . . and a reference to an internet domain . . . , to which electronic mail can be sent or delivered.”\textsuperscript{46}

A stockholder who wishes to opt out of receiving notice by e-mail may so notify the corporation either in writing or by electronic transmission directed to the corporation.\textsuperscript{47} In addition, as was the case before the 2019 amendments, notice by any form of electronic transmission, including e-mail, will not be deemed effective if the person responsible for giving notice has become aware that two consecutive notices sent by electronic transmission could not be delivered.\textsuperscript{48} However, that person’s inadvertent failure to discover that the notices were undeliverable will not “invalidate any meeting or other action.”\textsuperscript{49} Notice by means of electronic transmission other than e-mail (e.g., by posting on an electronic network) continues to be ineffective unless consented to by the stockholder.\textsuperscript{50}

Notice by e-mail is deemed given when it is “directed” to the stockholder’s e-mail address.\textsuperscript{51} The amendments further specify that notice delivered by courier service is deemed given upon “the earlier of when the notice is received or left at such stockholder’s address[,]” and (as was formerly provided in DGCL section 222(b)) notice by mail is deemed given when it is “deposited in the U.S. mail, postage prepaid[.]”\textsuperscript{52}

**Delivery of Stockholder Consents to the Corporation**

The 2019 amendments also afford additional flexibility to corporations in how stockholder consents may be delivered. Under prior law, a stockholder consent by electronic transmission was not deemed delivered to the corporation until it had been printed out and delivered in paper form, unless the corporation’s board of directors provided by resolution for another means of delivery. The amendments have retained paper delivery as the default, but also provide that a stockholder consent by electronic transmission is deemed delivered “when the consent enters an information processing system, if any, designated by the corporation for receiving consents, so long as the electronic transmission is in a form capable of being processed by that system and the corporation is able to retrieve that electronic transmission[.]”\textsuperscript{53}

Importantly, a corporation’s designation of an “information processing system” for the receipt of stockholder consents may be determined not only from the certificate of incorporation and bylaws, but also “from the context and surrounding circumstances, including the conduct of the corporation.”\textsuperscript{54} In addition, a stockholder consent by electronic transmission is deemed delivered “even if no

\begin{itemize}
  \item \textsuperscript{42} See 8 Del. C. § 232 (2018).
  \item \textsuperscript{43} Id. § 232(a). The legislative synopsis accompanying the amendments explains that, as regards to notices given pursuant to the DGCL or a corporation’s certificate of incorporation or bylaws, “no provision of the certificate of incorporation or bylaws (including any provision requiring notice to be in writing or mailed) may prohibit the corporation from giving notice in the form, or delivering notice in the manner, permitted by Section 232(a).” Del. S.B. 88 syn. § 11, 150th Gen. Assem. (2019).
  \item \textsuperscript{44} 8 Del. C. § 232(a).
  \item \textsuperscript{45} Id. § 232(d). Pursuant to the quoted text, the contact information of an officer or agent of the corporation must be supplied if an email notice is to be deemed to include attached files, not just hyperlinked information. Id.
  \item \textsuperscript{46} Id.
  \item \textsuperscript{47} Id. § 232(a).
  \item \textsuperscript{48} Id. § 232(e).
  \item \textsuperscript{49} Id.
  \item \textsuperscript{50} 8 Del C. § 232(b).
  \item \textsuperscript{51} Id. § 232(a).
  \item \textsuperscript{52} Id.
  \item \textsuperscript{53} Id. § 228(d)(1).
  \item \textsuperscript{54} Id.
\end{itemize}
person is aware of its receipt.”

**Acting by Electronic Means**

The DGCL, the DRULPA, and the DLLCA (together, the Entity Acts) have been amended to provide greater specificity about how electronic transmission and electronic signatures may be used in taking actions under the Entity Acts or organic entity documents.

Before the 2019 amendments, the Entity Acts already permitted the use of “electronic transmission” for multiple purposes, such as stockholder, member, or partner consents and proxies. In addition, since its adoption in Delaware on July 14, 2000, the Uniform Electronic Transactions Act (DUETA) has provided for the use of “electronic records” and “electronic signatures” generally in business and government transactions. The provisions in the Entity Acts regarding electronic transmission were not as thorough as those in the DUETA, however, whereas the DUETA—which “does not apply to a transaction to the extent it is governed by” the Entity Acts—left unclear just when an Entity Act “governed” a transaction such that the DUETA was displaced.

The 2019 amendments to the Entity Acts have clarified when electronic means such as those permitted by the DUETA will be effective under the Entity Acts. Central to these amendments is an entirely new section added to each of the Entity Acts.

These new sections contain general authorization for the use of electronic transmission and electronic signatures in entity actions or transactions, subject to important statutory exceptions summarized below and any restrictions expressly set forth in the organic entity documents. Respecting electronic transmission and electronic signatures must be “expressly stated” to be effective. “A provision merely specifying that an act or transaction will be documented in writing, or that a document will be signed or delivered manually, will not prohibit” application of the broad authorization contained in DGCL § 116(a), DRULPA § 17-113(a), and DLLCA § 18-113(a). Del. C. § 232(d) (for corporations); 6 Del. C. §§ 17-113(a) (for LPs), 18-113(a) (for LLCs).

Respecting electronic signatures, the new sections provide that whenever a signature is required or permitted by the applicable Entity Act or the relevant organic entity documents, “the signature may be a manual, facsimile, conformed or electronic signature.” Electronic signature is defined as “an electronic symbol or process that is attached to, or logically associated with, a document and executed or adopted by a person with an intent to authenticate or adopt the document.”

The new sections also specify safe-harbor conditions under which an electronic transmission will be deemed “delivered” for purposes of the applicable Entity Act and the relevant organic entity documents. Specifically, unless “the sender and recipient” agree otherwise (or in the case of an LP or LLC, its operating agreement provides otherwise), the electronic transmission is deemed delivered to a person “when it enters an information processing system that the person has access to.”

These new sections contain general authorization for the use of electronic transmission and electronic signatures in entity actions or transactions, subject to important statutory exceptions summarized below and any restrictions expressly set forth in the organic entity documents. Respecting electronic transmission and electronic signatures must be “expressly stated” to be effective. “A provision merely specifying that an act or transaction will be documented in writing, or that a document will be signed or delivered manually, will not prohibit” application of the broad authorization contained in DGCL § 116(a), DRULPA § 17-113(a), and DLLCA § 18-113(a). Del. C. § 232(d) (for corporations); 6 Del. C. §§ 17-113(a) (for LPs), 18-113(a) (for LLCs).

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These new sections contain general authorization for the use of electronic transmission and electronic signatures in entity actions or transactions, subject to important statutory exceptions summarized below and any restrictions expressly set forth in the organic entity documents. Respecting electronic transmission and electronic signatures must be “expressly stated” to be effective. “A provision merely specifying that an act or transaction will be documented in writing, or that a document will be signed or delivered manually, will not prohibit” application of the broad authorization contained in DGCL § 116(a), DRULPA § 17-113(a), and DLLCA § 18-113(a). Del. C. § 232(d) (for corporations); 6 Del. C. §§ 17-113(a) (for LPs), 18-113(a) (for LLCs).

Respecting electronic signatures, the new sections provide that whenever a signature is required or permitted by the applicable Entity Act or the relevant organic entity documents, “the signature may be a manual, facsimile, conformed or electronic signature.” Electronic signature is defined as “an electronic symbol or process that is attached to, or logically associated with, a document and executed or adopted by a person with an intent to authenticate or adopt the document.”

The new sections also specify safe-harbor conditions under which an electronic transmission will be deemed “delivered” for purposes of the applicable Entity Act and the relevant organic entity documents. Specifically, unless “the sender and recipient” agree otherwise (or in the case of an LP or LLC, its operating agreement provides otherwise), the electronic transmission is deemed delivered to a person “when it enters an information processing system that the person has access to.”

These new sections contain general authorization for the use of electronic transmission and electronic signatures in entity actions or transactions, subject to important statutory exceptions summarized below and any restrictions expressly set forth in the organic entity documents. Respecti
designated for the purpose of receiving electronic transmissions of the type delivered, so long as the electronic transmission is in a form capable of being processed by that system and such person is able to retrieve the electronic transmission.” Whether a recipient has designated an information processing system for purposes of this safe harbor depends upon the entity’s organic documents and “the context and surrounding circumstances, including the parties’ conduct.” Finally, the new sections provide that a person need not be “aware” of the receipt of an electronic transmission for it to be deemed delivered under the safe harbor, and that an “electronic acknowledgement” from an information processing system “establishes that an electronic transmission was received” but not that the content received “corresponds to” what was sent.

As mentioned above, the new sections contain exceptions to their broad authorization of the use of electronic transmission and electronic signatures. Accordingly, that authorization does not apply to documents filed with any Delaware court or governmental body, including the office of the secretary of state; certificates of stock or of partnership or LLC interests; or acts under provisions that address registered agents in Delaware, foreign entities, or commencement of suits against entities or their fiduciaries. Also excluded from coverage specifically under the DGCL are certain documents that may take electronic form pursuant to other sections, such as notices to stockholders and director and stockholder consents. Conforming changes have been made to other sections of the Entity Acts, generally eliminating language that is now surplusage or that could be interpreted as prohibiting the use of electronic transmission for certain actions.

Communications-Contact Information Now Required When a Registered Agent Resigns

Since 2006, every Delaware corporation, LP, and LLC has been required to provide to its registered agent in Delaware (but not to the state) “the name, business address and business telephone number of a natural person... who is then authorized to receive communications from the registered agent.” Such person is known as the “communications contact” for the entity. Pursuant to the 2019 amendments, the Entity Acts now provide that when a Delaware registered agent resigns without appointing a successor registered agent for any affected entity, the information the resigning registered agent must provide to the secretary of state shall include the communications-contact information last provided to the registered agent by the entity. Such information, however, “shall not be deemed public.”

Additional Amendments to the Entity Acts

The DRULPA and the DLLCA expressly permit LP and LLC operating agreements and merger agreements to afford “contractual appraisal rights” respecting interests in LPs or LLCs in the event of certain transactions, including mergers, conversions, and transfers of the entity; operating-agreement amendments; and sales of all or substantially all of the entity’s assets. The 2019 amendments have confirmed that appraisal rights may also be made available in connection with divisions, mergers of registered series, and conversions of registered series to protected series (or the reverse).

In connection with corporate mergers, stockholders seeking appraisal of their shares may now deliver appraisal demands by electronic transmission “if directed to an information processing system (if any) expressly designated for that purpose” in the corporation’s notice of appraisal rights. Delivery of a written stockholder demand, however, remains the default.

The DGCL’s requirement that a merger agreement be signed by corporate officers has been loosened. As a result of the 2019 amendments, a merger agreement may now be signed by any person who has been authorized to do so if (as is typically the case) a certificate of merger is filed with the secretary of state in

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68 8 Del. C. § 132(d) (for corporations); 6 Del. C. §§ 17-104(g) (for LPs), 18-104(g) (for LLCs).
69 8 Del. C. § 136(a) (for corporations); 6 Del. C. §§ 17-104(d) (for LPs), 18-104(d) (for LLCs).
70 6 Del. C. §§ 17-212 (for LPs), 18-210 (for LLCs).
71 Id.
72 8 Del. C. § 262(d)(1)-(2).
73 Id.
lieu of filing the merger agreement itself.\textsuperscript{74} Although textual changes in this regard were made only to DGCL sections 251 (merger of Delaware stock corporations) and 255 (merger of Delaware nonstock corporations), cross-references in other sections cause the amended signature requirement to apply also to mergers between Delaware and non-Delaware corporations, stock and nonstock corporations, and corporations and LLCs or partnerships.\textsuperscript{75}

The provisions of the DGCL permitting a board of directors to act by unanimous written consent have been amended to remove the implication that a board consent was not effective until it had been filed with the board minutes. Although the amendment did not change the requirement that a board consent be filed with the minutes, the consent’s effective time no longer depends on such filing.\textsuperscript{76}

In 2014, the DGCL was amended to permit director and stockholder consents to be made effective as of a future time, including upon the happening of a future event, “whether through instruction to an agent or otherwise.”\textsuperscript{77} Similar amendments now make clear that the action taken by incorporators to organize a newly formed corporation may also be taken by means of a future-effective consent.\textsuperscript{78} A future-effective consent may now be used as well for an organizational action by the corporation’s initial board of directors if the initial directors are named in the certificate of incorporation,\textsuperscript{79} although an initial board was presumably already permitted to do so under the 2014 amendments.

Finally, the amendments have removed the implication that a nonprofit corporation could not be revived if its certificate of incorporation was declared forfeited because the corporation did not have a registered agent.\textsuperscript{80} This was already clear as to for-profit corporations (under DGCL section 312), but the prior wording of DGCL section 313(a) implied that a nonprofit corporation could be revived only if it was void for failure to file its annual franchise tax report.

\textsuperscript{74} Id. §§ 251(b) (merger between Delaware stock corporations), 255(b) (merger between Delaware nonstock corporations).

\textsuperscript{75} Id. §§ 252 (merger between Delaware and foreign stock corporations), 254 (merger between corporation and joint-stock association), 256 (merger between Delaware and foreign nonstock corporations), 257 (merger between Delaware stock and nonstock corporations), 258 (merger between Delaware and foreign stock and nonstock corporations), 263 (merger between corporation and partnership), 264 (merger between corporation and LLC).

\textsuperscript{76} 8 Del. C. § 141(f).

\textsuperscript{77} Id. (director consent); Id. § 228(c) (stockholder consent).

\textsuperscript{78} Id. § 108(c).

\textsuperscript{79} Id.

\textsuperscript{80} Id. § 313(a).
Wisconsin District Court Finds LLC Minority Owners Owe No Common Law Duties to Majority Members

By:  Jeff Storch  
Boardman & Clark LLP  
Madison, Wisconsin

In April 2019, the Wisconsin Supreme Court held in Marx v. Morris that Chapter 183 of the Wisconsin Statutes, governing limited liability companies (the “Act”), did not abrogate common law duties between the members of an LLC. See our articles on Marx here and here. However, the Wisconsin Supreme Court did not define the scope of the applicable common law duties. A U.S. District Court started to define that scope in a July 2019 case.

In Raab v. Wendel, the U.S. District Court for the Eastern District of Wisconsin, in reconsidering its earlier decision issued the month before Marx, held that even after Marx, a majority member of an LLC does not have a common law breach of fiduciary duty claim against a minority member. In other words, minority owners of an LLC do not owe a common law fiduciary duty to LLC majority owners.

In Raab, the court indicated that the Wisconsin Supreme Court concluded that common law breach of fiduciary duty claims are not categorically precluded by Section 183.0402 of the Act. However, the Raab court continued that merely because those claims are not categorically precluded does not mean that such a claim exists in all cases, and the Wisconsin Supreme Court left it to lower courts to sort out whether the facts of any particular case supported a breach of fiduciary duty claim.

The court then analogized LLC member claims to corporation shareholder claims, where minority shareholders do not owe fiduciary duties to majority shareholders. The court consequently held that an LLC majority member does not have a common law breach of fiduciary duty claim against an LLC minority member.

Although as a federal case Raab is not binding on Wisconsin courts, it provides a prediction for how the Wisconsin Supreme Court may rule on this matter in the future. If LLC members want more certainty, they should state in the LLC’s operating agreement what, if any, duties apply to LLC members. While Section 183.0402 of the Act provides default rules (which under Marx include common law fiduciary claims), that section also states that those rules apply only “[u]nless provided in an operating agreement.” So, for example, if members do want minority members to have fiduciary duties to majority members, they can so specify in the operating agreement. In light of Raab, those LLCs who want minority members to have fiduciary duties to majority members should consider amending their operating agreements.

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1 386 Wisc. 2d 122, 925 N.W.2d 112 (Wisc. 2019).
2 Case No. 16-CV-1396, 2019 WL 1060856 (E.D. Wisc. March 6, 2019).
Wisconsin Supreme Court Concludes Wisconsin’s LLC Act Does Not Preempt Common Law Claims

By: Jeff Storch
Boardman & Clark LLP
Madison, Wisconsin

In April of 2019, the Wisconsin Supreme Court held that Chapter 183 of the Wisconsin Statutes, governing limited liability companies (the “Act”), did not abrogate common law duties for LLCs. In Marx v. Morris, on certification from the Wisconsin Court of Appeals from a denial of defendant’s summary judgment motion in the circuit court, the Court responded to the question, “Does [the Act] preempt common law claims by one member of an LLC against another member based on the second member’s alleged self-dealing?” In answering, the Court stated that the Act does not state or imply that Wis. Stat. § 183.0402 constitutes the entirety of an LLC member’s or manager’s obligations to other members and to the LLC and consequently held that the plaintiffs’ common law claims survived, at least at the current stage of the proceedings. The Court remanded to the circuit court for further proceedings.

While the Court’s decision provides the first definitive guidance on whether Wisconsin recognizes common law duties for LLC members and managers, the issue is far from resolved. First, due to the procedural status of the case, the nature of the plaintiffs’ common law claims was not fully explored. Next, the Court did not define the scope of the common law duties that apply to LLCs; it merely found that LLC common law claims are not preempted by the Act. A strong dissent claimed that there could not be any such claims to preempt because, prior to the adoption of the Act, there was no such thing as an LLC member. The dissent’s logic suggests yet another argument that, at most, the “common law” of LLCs can only date back to the relatively recent enactment of the Act.

For now, LLCs that want more certainty on what duties apply to their members and managers should document those duties in the LLC’s operating agreement. Members and managers may wish to review and amend their current operating agreements.

1 386 Wisc. 2d 122, 925 N.W.2d 112 (Wisc. 2019).

RIP

THE JOURNAL OF PASSTHROUGH ENTITIES

Regrettably, THE JOURNAL OF PASSTHROUGH ENTITIES to which many of our Committee members including Kelley Bender, Allan Donn, Bruce Ely, Steve Frost and Tom Rutledge have served as regular contributors, has ceased operations effective with its November/December 2019 issue.

Following on the demise several years ago the journal BUSINESS ENTITIES, there are fewer and fewer places to turn for information and analysis.
What If There The Parties Cannot Agree On An Operating Agreement - Why Not Claim A General Partnership Was Formed Instead - Did Not Work This Time

By: Edward Wender
Potomac Law Group PLLC


In this case, the principals were engaged in the mortgage origination and servicing business and when hard times hit sought to combine their respective businesses. Mas Associates, LLC was an existing limited liability company engaged in the mortgage origination and servicing business. Harry, Joel and Mark (their first names were used in both the lower court and appellate opinions) were the principals although Mark had no interest in Mas Associates, LLC of which his wife owned a 91% interest. Mark operated as if he was the non-member manager of the business.

Negotiations started in 2009 and involved counsel for each of the principals and regulatory counsel to all three entities. The discussions and structure of the arrangements were documented contemporaneously through notes of regulatory counsel and unsigned drafts of agreements. The intent of the parties was for Joel and Harry to ultimately become members of Mas Associates, LLC. The structure contemplated an "Interim Period" during which Harry and Joel would be employees entitled to receive "W-2 compensation equal to 1/3 of the profits of the origination division of the Company". The Interim Period was intended to be a time during which licensing and operations would be ironed out. The Interim Agreement was apparently signed and extended before it was set to expire in November 2012. There was no documentation or agreement as to what would happen if the Interim Period never ended.

The businesses were combined and licenses were surrendered except for a license in the name of Equity Mortgage Lending (a trade name of MAS Associates, LLC). Harry and the other principals characterized themselves as partners and took part of management of the operations. Harry and Joel worked for Equity Mortgage Lending under a salary and commission basis. Drafts of documents continued to be circulated. Harry refused to be personally liable for more than a one third share of a warehouse loan which would fund mortgage origination and his refusal was one of the reasons that delayed having documents executed.

Harry provided $275,000 of working capital to the operation through loans to Mark's wife who then made a capital contribution to Mas Associates. Needless to say, no promissory notes were executed.

As is often the case in litigation involving limited liability companies, litigation was precipitated by Harry's resignation (some two years after the initial discussions) and Harry's request for the return of his "capital contribution" and a share of the proceeds from a possible sale of the business.

Since Harry was clearly not a member of MAS, his counsel argued that the negotiations resulted in a general partnership among Harry, Joel, Mark and Mas Associates.

The trial court found that there was evidence of partnership among Harry, Joel, Mark and MAS Associates and the Court of Special Appeals upheld the trial court. The Court of Appeals granted certiorari and reviewed the evidence as to the intent to form a general partnership, as a limited liability company could only be formed by filing Articles of Organization with the Maryland State Department of Assessments and Taxation and no such filing occurred.

Joel and Mark cited Ramone v. Lang, 2006 WL 905347 (Del Ch., 2006), for the proposition that parties should not be considered to have formed a partnership because of negotiations to form an LLC. In Ramone, the parties sought to form an LLC but could not agree on its terms. The Ramone Court said it would be inequitable to conclude that a partnership was formed as a result of the failure of negotiations to form an LLC. The result of Ramone makes sense in that how can a Court claim that an agreement was reached to form a partnership, in light of the fact that no agreement was ever reached to form the intended limited liability company.

In MAS, a number of drafts of Operating Agreements were prepared. While there as an agreement on how to operate in the Interim Period and apparently the agreement was honored, the parties continuously sought to finalized documents whereby Harry and Joel
would become members of Mas Associates.

The Court applying the rational of Ramone held that no partnership was formed. The fact that Joel and Harry participated in management was not remarkable in that they could be non-member managers or simply part of a hired management team to operate the business. The use of the term “partner” was similarly dismissed as the term is used colloquially.

The principal problems with Harry’s contention were (a) that the trade name (Equity Mortgage Lending) and all licenses for the business were held by MAS Associates, (b) that all funds provided by Harry were through checks payable to Mark’s wife and were not direct contributions to MAS Associates, (c) all payments to Harry were characterized and reported as W-2 wages, and (d) Harry refused to be liable for more than 1/3rd of the warehouse loan (whereas a general partner would presumably be liable for the entire loan). The Court relied on Section 9A-202(c) of the Maryland Revised Uniform Partnership Act that provides “An unincorporated association or entity created under a law other than the laws described in subsection (b) of this section is not a partnership.”

Harry’s lawyers did a very good job convincing the trial court and an appellate court to hold a partnership was created in order to give Harry an equitable shot at obtaining his money back. In this instance the heavy involvement of lawyers undid this contention by creating documentary evidence that the intent was to create an LLC.

Interim arrangements should provide for provisions for the termination of discussions. Had a new company been formed to hold the licenses and employ Harry and Joel, rather than MAS whose ownership was well documented and for which there was a signed operating agreement, the result might have been different.

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1 The laws cited in subsection (b) are the Maryland Revised Uniform Partnership Act or a statute of another jurisdiction comparable to this title or the Maryland Uniform Partnership Act and their respective subsequent amendments.
Chicken Sh*t Bingo Fans Rejoice: The Dragpipe Saloon Survives a Dissolution Scare

By:  Peter Mahler
    Farrell Fritz, P.C.
    New York, New York

In a moment I’ll explain why you’re looking at a picture of “chicken shit bingo,” but first…

The nationwide landscape of statutes and case law governing judicial dissolution of limited liability companies exhibits more state-to-state similarity than dissimilarity.

On the statutory side, this is due in large part to the use of the same model acts in the initial wave of LLC enabling legislation that swept the country in the late 1980s and early 1990s and, of course, the more recent adoption by many states of the Revised Uniform LLC Act.

On the case law side, because all LLC laws share a fundamental deference to the members’ contractual preferences as expressed in the operating agreement, and because the LLC statutes almost invariably include as ground for dissolution the impracticability of the LLC’s continued operation in conformity with the members’ agreement, to a very large extent court decisions in LLC dissolution cases turn on common-law principles of contract interpretation which also tend to uniformity among the states.

All of which is to make the point that, while a steadily increasing focus in my practice and of this blog is New York’s experience with judicial dissolution of LLCs as the newly dominant form of closely held business entity, business divorce practitioners in all states can benefit greatly from staying abreast with LLC case law developments from across the country — and not just Delaware!

Along those lines, two weeks ago I wrote about a recent Kentucky appellate ruling affirming the dismissal of a minority member’s petition to dissolve a single-asset realty holding LLC. That case turned wholly on the court’s reading of the operating agreement’s purpose clause.

In this post, we look at a South Dakota Supreme Court decision issued earlier this month in another LLC dissolution case also involving a single-asset realty holding company with the fanciful name, Dragpipe Saloon, LLC, in which the court reversed the lower court’s order granting a dissolution petition alleging deadlock. In that case, the operating agreement’s purpose clause was one of several interesting issues addressed in the court’s opinion.

The Sturgis Motorcycle Rally

Sturgis, South Dakota is the setting for the Sturgis Motorcycle Rally founded by the Jackpine Gypsies motorcycle club and held every year since 1938 over ten days in August. According to its Wikipedia entry, the Rally’s original focus was racing and stunts, but has since expanded into a huge, festival-like event featuring top-name entertainers and attendance of a half-million or more people.

Among the more colorful facts mentioned in the entry, there were 405 individuals jailed at the 2004 Rally, approximately $250,000 worth of motorcycles are stolen annually, and there have been a number of mysterious, unsolved deaths at the Rally.

Dragpipe Saloon, LLC

In 2003, four friends formed Dragpipe Saloon, LLC to purchase 74 acres of land near Sturgis. On 18 acres they built a bar and camping facilities that are open only during the Rally; the remaining acreage is leased to a farmer. During the Rally Dragpipe also sells t-shirts, hosts food vendors, and provides live entertainment including, you guessed it, “chicken shit bingo” which, I’ve reluctantly learned, is a “real thing” supposedly inspired...
The four members each invested $80,000 in the venture. Under Dragpipe’s operating agreement, the four members each received a 25% membership interest and voting rights. The agreement states that Dragpipe’s purpose is to engage in all lawful activities, including, but not limited to, owning, purchasing, taking, leasing, or otherwise holding or acquiring real property and any interest or right in real property and any improvements thereon, and to hold, own, operate, control, maintain, manage and develop such property and interests in any manner that may be necessary, useful or advantageous . . . [to the] company.

The operating agreement authorizes any member to voluntarily resign their membership and obtain the “fair market value of [the member’s] Ownership Interest, adjusted for profits and losses to the date of resignation.” Fair market value is determined by unanimous vote of the members or, failing that, by an independent appraiser.

In 2005, one of the founding members sold her membership interest to a new investor.

Dragpipe had its first profitable year in 2015 and posted modest profits in 2016 and 2017. The members provide labor during the Rally without compensation and have never received income distributions. Profits in 2015 covered mortgage expense previously contributed pro rata by the members and allowed reimbursement of the members’ out-of-pocket expenses.

Two Members Initially Obtain Judicial Dissolution

After the 2015 Rally, two members of Dragpipe found buyers for their membership interests. The other two members had no objection but the proposed sales fell through. In 2017, the two who wanted to sell plus a third member agreed to list the Dragpipe property for sale for $950,000, but the fourth member refused to go along with it.

The two members who had tried to sell their membership interests did not invoke their right under the operating agreement to resign and receive fair market value. Instead, they filed suit requesting judicial dissolution of Dragpipe and the sale of its assets.

The circuit court granted the request. In a post-trial ruling, the court found that the profit made in 2015-2017 was insufficient to begin repaying the capital contributions made by the members and that the parties were “at a standstill” on whether to sell the property. The court determined that the only way for Dragpipe to make money was to sell its real estate. The court concluded that judicial dissolution was authorized under South Dakota’s LLC Act because Dragpipe’s economic purpose was unreasonably frustrated and because it was not reasonably practicable to carry on its business in conformity with the operating agreement.

Supreme Court’s Reversal

The two members who opposed dissolution appealed to the South Dakota Supreme Court which, in its decision earlier this month, agreed with the appellants and reversed the circuit court’s dissolution order. Dysart v Dragpipe Saloon, LLC, 2019 S.D. 52 [Sup. Ct. S. Dak. Sept. 4, 2019].

The court’s summary of the governing legal principles characterized involuntary judicial dissolution as “an exceptional level of intervention into the otherwise private agreement of an LLC’s members” which should be unavailable merely to resolve disagreements among owners or relieve an owner of an investment decision later regarded as improvident. Rather, judicial dissolution is permitted only in those instances where it is expressly authorized under our statutes.

Turning to the facts of the case, the Supreme Court cited five factors undermining the lower court’s dissolution order.

First, the panel determined that the lower court’s findings did not “support the legal conclusion that it is no longer practicable for Dragpipe to continue to operate in accordance with its operating agreement.” Initially focusing on Dragpipe’s purpose as stated in its operating agreement, the court found that:

The operating agreement broadly states Dragpipe’s purpose as “owning, purchasing, taking, leasing, or otherwise holding or acquiring real property” and to “hold, own, operate, control, maintain, manage and develop such property and interests in any manner that may be necessary, useful or advantageous[.]” Here, Dragpipe did, in fact, “purchas[e] . . . real property” that it now “hold[s], own[s], operate[s],
maintain[s] and manages[s].” Continuing to do so is no less practicable now than it has been throughout Dragpipe’s history of operation.

Second, the appellees’ dissatisfaction with the return on their investment in Dragpipe was not enough to establish frustration of purpose, prompting the court to comment:

The fact that the Appellees believe it to be a prudent time to sell Dragpipe’s real property and realize the gain from their investments does not mean Dragpipe is unable to continue to operate in accordance with its stated purposes. Nor do the historic losses or Dragpipe’s failure to return income distributions to its members render its operation impracticable. In more recent years, Dragpipe’s performance has improved and yielded profitable results, if not large cash returns, for its members. It may well be that the Appellees have grown weary of Dragpipe’s lukewarm revenue outcomes over the years, but that does not, itself, mean that Dragpipe is not “carrying on the company’s business in conformity with . . . the operating agreement[.]”

Third, the Supreme Court also disagreed with the circuit court’s finding that Dragpipe’s economic purpose was likely to be unreasonably frustrated. Here’s what it said on that score:

In the absence of an order directing judicial dissolution, Dragpipe will continue to operate more or less as it has since its inception. Even if, as the circuit court found, the principal means of making money for Dragpipe’s members will ultimately be through the sale of the real property, that does not mean that the members’ failure to reach a consensus about a proposed sale here is likely to frustrate Dragpipe’s economic purpose.

Fourth, the operating agreement provided the appellees with the option to resign and receive fair market value for their membership interests as determined either by agreement or independent appraisal, in lieu of dissolution. The appellees “have not availed themselves of this option,” the court wrote, “nor does it appear they have continued in their efforts to sell their interests outright” despite the lack of any objection by the appellants to their doing so.

Fifth, the court found “no ‘impenetrable deadlock’ and no indication that a member or member-faction is benefitting from the disagreement regarding the proposed sale of Dragpipe’s real estate to the prejudice of the other members.” The lower court’s finding that the members were “at a standstill,” the panel wrote, is attached to the implicit legal conclusion that Dragpipe must sell its real estate now. However, we do not perceive the same degree of urgency when we interpret the text of Dragpipe’s operating agreement and consider the legal standards for judicial dissolution.

For all of these reasons, and upon its conclusion that Dragpipe was operating within its contractually articulated purpose, that it was economically feasible, and that the members “are not effectively deadlocked and have multiple options for resolving their disagreement about the sale of Dragpipe’s real estate,” the court held that “the ‘drastic remedy’ of judicial dissolution is not supported and that the circuit court’s judgment of dissolution must be reversed.”

The Takeaway. The South Dakota Supreme Court’s analysis and the outcome in Dysart likely would be the same had the case arisen under the LLC statutes and case law of any other state. Dysart also underscores the challenges inherent in formulating the operating agreement for a multi-member, single-asset realty holding LLC in which, quite often, non-control members eventually seek to cash out their membership interests without a ready public market for their interests and without ready financing at the company or member level.

But, you ask, didn’t the petitioning members in Dysart have a readily available exit by means of resigning and receiving fair market value for their interests? Yes, they did, but one must assume that they did not exercise that option, and instead went to the trouble and expense of suing for dissolution, because they believed that a forced sale on the open market of Dragpipe’s property and operations would generate a fatter payout on a pro rata basis than an appraisal of fair market value which likely would include marketability and minority discounts.

Finally, Dysart presents a nice contrast with the above-mentioned Kentucky case that I recently wrote about, also involving a single-asset realty holding LLC. In that case, where the court found that the continued operation of the property as a parking lot was consistent with the operating agreement’s purpose clause, I
commented that the unsuccessful petitioner’s real problem was the absence of any provision in the operating agreement either requiring the property to be developed and sold within a defined period or, if not, giving him a buyout option. In Dysart, the operating agreement gave the unsuccessful petitioners a buyout option which they declined to employ for whatever reasons.
Case Law Summaries

At the 2019 LLC Institute, there will be a pair of case law update programs, one focused on Delaware and one focused on non-Delaware cases, including cases in bankruptcy. Those outlines will be posted to the Committee website and distributed to the Committee membership through the listserv.
WORTH READING

Emma Cueto, Sedgwick Strikes Clawback Deal With Former Equity Partners, Law360 (June 7, 2019)


Thomas E. Rutledge, Judicial Expulsion of a Member: What Have We Learned From All Saints University of Medicine Aruba, I.E., Test and Kenny v. Fulton Associates, J. Passthrough Entities (July-August 2019) 33


Karen C. Burke, Section 199A and Choice of Passsthrough Entity, The Tax Lawyer (Spring 2019)


### 2019 Business Entity Enactments

#### Uniform Protected Series Act

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#### Uniform Limited Cooperative Association Act

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#### Revised Uniform Partnership Act

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#### Revised Uniform Limited Liability Company Act

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#### Revised Uniform Unincorporated Nonprofit Association Act

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PLANNING AHEAD

The Committee on LLCs, Partnerships and Unincorporated Entities will meet three times in 2020: at the Spring Meeting of the Section on Business Law, at the Annual Meeting of the Section of Business Law, and at the 2020 LLC Institute. Looking forward:

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<td>2020 ABA BLS Spring Meeting</td>
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<td>2020 ABA BLS Annual Meeting</td>
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The detailed schedules for Committee meetings and programs at these meetings will be announced in future issues of the LLC & Partnership Reporter.