



M E M O R A N D U M

TO: Series LLC Drafting Committee
FROM: Thomas E. Rutledge
DATE: January 6, 2017
RE: Possibility of Incorporating into Series Act Provisions Addressing the Merger of Either or Both of a Series Organization or a Series Thereof

With the hope of better articulating concerns I have raised in our various phone calls, I wanted to reduce to writing my initial thoughts with respect to the possibility of mergers of involving series LLCs, a category that itself includes either the merger of the series LLC or the merger of an individual series.

An Individual Series Should Not Be Permitted To Engage In a Merger.

From early on in this process, extensive time and energy has been devoted to making sure that an individual series is not classified as a legal entity separate and distinct from the series LLC that caused it to be formed. I submit that, at this late date, allowing an individual series to engage in the merger transaction is inconsistent with that protocol. A merger is a transaction engaged in by and between business entities. This analytic path is consistent with the rule that partnerships organized under the Uniform Partnership Act (1914) were not endowed with the ability to engage in a merger. Of course, it is not news to anybody in this audience that, under the Uniform Partnership Act (1914), with minimal exceptions, a partnership was viewed not as a legal entity but simply an aggregate of the partners.

If Harmonized META Allows for Series Mergers, the Fact That the Cart Was Put Before the Horse Should Be of No Import.

As Dan Kleinberger has pointed out, Harmonized META allows individual series to engage in organic transactions. Accepting that to be the case, this drafting project should in no manner be bound by that determination. From my perspective, if Harmonized META did that, it put the cart before the horse, determining the rights and characteristics of an organizational form (the series) before this drafting committee had determined those answers. If and to the extent Harmonized

META allows an individual series to engage in organic transaction, the correct answer at this juncture is to revise Harmonized META to delete that capacity¹.

The Complexity of a Comprehensive Answer is Beyond the Available Time

Enclosed herewith is a series of PowerPoint slides penultimate diagramming the various merger transactions that could take place. As indicated by the slide, there is also the possibility of a series LLC engaging in a merger with a business organization other than an LLC (all the possible permutations thereof are not set forth in separate diagrams). At minimum, I submit that these diagrams illustrate the multitude of potential transactions that would need to be considered before we would enable series to engage in merger transaction. Admittedly, the number of permutations is reduced if we do not allow an individual series, on its own account, to engage in a merger. Still, there remain a multitude of issues to be considered. For example, assume that ABC, LLC is organized in State One, while XYZ, LLC is organized in State Two. Both ABC and XYZ are series organizations. I believe we need to examine the degree to which we are exacerbating the punt with respect to assessing the validity of association. Assume ABC is merged with and into XYZ. It could ultimately be the law of XYZ that the validity of association is assessed as of the time of the operative facts giving rise to the claim (e.g., the time of the automobile accident). Conversely, under the law of ABC, it could be that the validity of association is determined at the time the judgment on the claim is rendered.

Set forth as the last slide is not a well-organized listing of additional questions I have with respect to implementation of any merger provisions involving series LLCs.

Conversions?

Please note that I am not completely dismissing the concerns of individuals including Leigh Griffith and John Williams that allowing series (and I understand their concern to be at that level rather than at the level of the series LLC) to engage in organic transactions. I previously suggested that many and maybe even most of those issues can be addressed by an alternative mechanism, namely allowing an individual series to convert into a freestanding LLC. Once converted, that organization could engage in the range of organic transactions otherwise allowed LLCs. Second, allowing the conversion of a non-entity into an entity did not do violence to our “a series is not an entity” paradigm. While a particular “effect of the conversion” statute would undoubtedly need to be crafted, I believe that is something we could accomplish in the available time.

All that said, in a subsequent discussion with Steve Frost, a significant problem was identified in this paradigm. Going back to the fact that we have not specified when a claim arises for determining whether or not association of property has properly taken place, a conversion could provide a mechanism for a “shell game”. Essentially, aware that a claim might arise, the individual series that is directly responsible thereon could convert into its own freestanding LLC. To the extent of the assets associated with the series, and as will property titled to but not associated with

¹ This is a topic which could be discussed at the March, 2017 meeting of the JEB.

the converted series, there is no change in the creditor's position. However, if the ultimate judgment cannot be satisfied out of the assets of the now converted series, there will be significant questions as to whether there can be recourse against unassociated assets of the former "mothership"² or the other series thereof. For that reason, my conversion idea has, at best, a significant hole, and should at this juncture be set aside.

Intra-Series LLC "Mergers"

In the course that same phone call with Steve Frost, we considered a limited proposal, one focused upon Leigh's issue of allowing transfer by operation of law of assets between series of a series LLC or between the series and the "mothership." Under this mechanism, we would allow "mergers" between the series of a series LLC and as well allow "mergers" of a series into its mothership LLC. While we would need to craft both procedural and effect of the transaction provisions, they can largely be based upon existing language with respect to mergers. In addition, we should not refer to this transaction as a merger, you will need to create a new label therefore (I am not sure Steve was entirely enamored with my recommendation that it be called a "wombat"). Questions requiring further consideration are whether a wombat affords the opportunity for shell games or otherwise causes problems.

Enclosure

² Apologies, but it's really the only term that works in this sentence.