**MEMORANDUM**

**Charging Order Issues In The Harmonized Acts**

TO: Lisa R. Jacobs, Chair, JEB

FROM: Jay D. Adkisson

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New sections F.2, H.2, and L.3 are in blue.

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This Memorandum addresses issues that have arisen under the charging order provisions of the so-called Harmonized Acts (UPA, ULPA, ULLCA and their revisions), and which are amenable to being addressed within the text of these Acts or in expanded Comments as appropriate. For brevity, I have referred to the text of ULLCA § 503 below, although nearly all the comments would apply with equal fervor to UPA § 504 and ULPA § 703.

## I. OVERVIEW

The charging order procedure found in the Harmonized Acts is an anachronism and the result of a mistake made when the charging order remedy was imported into the first UPA of 1914, and which later infected the UPA's progeny (the ULPA and ULLCA). The mistake has a historical underpinning in that American law diverged from English law at about the time of the Declaration of Independence, with American law adopting the lien of civil law to create a security interest in property, while English law continued for many years to use charging order which charged the property with payment of a debt.

Under American law, the correct remedy (then and now) would have been to simply expand the law of attachment, *i.e.*, an involuntary judicial lien, to encompass a debtor's distributive interest in a partnership, and to slightly modify the attachment so that distributions were directed to the creditor. This would allow the litigants and the courts to take advantage of the very substantially fleshed-out existing law of attachments, and not instead be confounded by an atypical remedy that is unique to a particular asset.

Note that many of the following problems would be fixed in substantial part simply by striking out the word "charging" and inserting instead "attachment", which is how these provisions should have been drafted in the first place.

## II. ISSUES

The use of "D/M" below refers to the Debtor/Member whose interest is being charged.

### A. NATURE OF REMEDY

#### 1. Distributions/Economic Rights: Creditors rights to distributive interests/economic rights

Courts frequently struggle with three issues:

1. What constitutes the D/M's rights that are subject to the charging order.

2. The effect of a charging order on the D/M's rights.

3. The effect of a foreclosure on the D/M's rights.

**What constitutes the D/M's rights that are subject to the charging order?** The confusion here arises from the general structure of the Harmonized Acts, which require a court to look outside the creditor's rights Article to other parts of the particular Act to make the determination that only the D/M's distributional rights are implicated. This can be fixed by a better explanatory Comment.

**The effect of a charging order on the D/M's rights?** The current language of § 503(a) states that "a charging order constitutes a lien on a judgment debtor's transferable interest . . .." The phrase "transferable interest" requires the court to then determine what that means, an eventually ends up a lien being placed on the "distributional interest". That the lien is on the "distributional interest" should be better spelled out in the Comment.

**The effect of a foreclosure on the D/M's rights?** Similarly, § 503(c) talks about "transferable interest" when "distributional interest" would be more clear.

### B. PRE-JUDGMENT

#### 1. Prejudgment Relief: Freezing the interest and distributions pending judgment

There is no provision for a pre-judgment attachment of the D/M's interest, although other assets of a putative debtor are usually fair game for such relief. The exclusivity provision, § 503(h), would seem to prohibit such pre-judgment relief.

Pre-judgment attachment of the putative D/M's interest should be allowed under the same circumstances that such attachment would be allowed against other assets of such a debtor. The court should also have the

discretion to allow either the entity to retain pre-judgment distributions or have them paid into a court fund pending resolution of the merits of the case. However, the diversion of such distributions should be subject to § 503(g) which provides for exemptions.

## C. MOTION MECHANICS

### 1. Procedure: The procedure for obtaining a charging order and ancillary provisions

One of the biggest flaws with the charging orders is that, except for California, the states have not enacting coordinating procedures in their Enforcement of Judgments Laws. This has forced courts nationwide to consider motions for charging orders on an *ad hoc* basis — quite literally, making up the procedure as they go.

The simple California procedure follows:

> CCP § 708.310.
>
> If a money judgment is rendered against a partner or member but not against the partnership or limited liability company, the judgment debtor's interest in the partnership or limited liability company may be applied toward the satisfaction of the judgment by an order charging the judgment debtor's interest pursuant to Section 15907.3, 16504, or 17705.03 of the Corporations Code.
>
> CCP § 708.320.
>
> (a) A lien on a judgment debtor's interest in a partnership or limited liability company is created by service of a notice of motion for a charging order on the judgment debtor and on either of the following:
>
> (1) All partners or the partnership.
>
> (2) All members or the limited liability company.
>
> (b) If a charging order is issued, the lien created pursuant to subdivision (a) continues under the terms of the order. If issuance of the charging order is denied, the lien is extinguished.

While simple, the California procedure thus provides for the following:

1. A noticed motion for charging order;

2. Service both upon the D/M and the target entity;

3. A temporary lien created upon service of the motion (analogous to a lien being created on an asset that is the subject of a levy); and

4. The lien becomes permanent if the motion for charging order is granted, or the lien is extinguished if not.

At least these provisions should be incorporated into the Harmonized Acts. Arguably, there should also be a provision allowing a creditor to obtain a charging order on an *ex parte* basis, without notice to the D/M or the entity, where there is a showing that the D/M may attempt to transfer the interest before service is made.

Some of the opinions discussing charging order motion procedure (or the lack thereof) include:

- *Open Road Trucking, LLC v. Swanson*, 2019 WL 6768443 (N.D., Dec. 12, 2009).
- *Ilani v. Abraham*, D.Nev. Case No. 2:17-CV-692 (Aug. 21, 2018).
- *Brown v. Sperber-Porter*, 2018 WL 4184372 (D.Ariz., Aug. 24, 2018).
- *Textron Financial Corp. v. Gallegos*, C.D.Cal. Case No. 15cv1678 (Oct. 7, 2015).
- *Kearney Construction Co., LLC v. Bank of America, N.A.*, 2015 WL 1499155 (M.D. Fla., 2015).
- *SE Property Holdings, LLC v. Unified Recovery Group, LLC*, 2014 WL 5846388 (S.D.Ala., 2014).
- *Regions Bank v. Stewart*, 2011 WL 1827453 (S.D.Ala., 2011).

**2. Unknown Interest: Where the debtor's interest, if any, has not been ascertained**

What if it is unknown what interest the D/M holds in the entity, if indeed the D/M holds any interest at all? This is an issue that has frequently befuddled the courts and has led to disparate results on similar facts.

With other assets, the judgment enforcement mechanisms allow a creditor to place a lien without having to ascertain whether the debtor has any interest, or exactly what that interest may be. Thus, for example, the filing of an abstract of judgment with the county recorder will pick up any real

property that the debtor owns in the county, if at all, without the creditor having to make prior identification of it. If the debtor has not real property in the county, then the lien will simply have no effect: No harm, no foul. Allowing a creditor to place liens without knowing if they will attach to any property is completely consistent with the protective effect of liens.

Notably, this is also true with levies: A creditor may obtain a writ of levy directed to Chase Bank without knowing whether the creditor has any accounts there at all, but if the creditor does have accounts they are picked up by the levy.

Thus, the Harmonized Acts should be amended to provide that it is not necessary for a creditor to establish that the debtor has any interest in the entity, or the amount of the interest, prior to bringing the motion for charging order. If the debtor has no interest in the entity: No harm, no foul.

Opinions discussion this problem include:

- *Perez v. Dhillon*, 2020 WL 1900447 (E.D.Cal., April 17, 2020).
- *435 Elm Investment, LLC v. CBD Investments LP I*, 2020 Ohio 943, 2020 WL 1230320 (Ohio App., March 13, 2020).
- *Regions Bank v. Hyman*, 2015 WL 1056302 (M.D.Fla., Mar. 10, 2015).
- *Arvest Bank v. Byrd*, Case No.10-02004 (W.D.Tenn., Aug, 19, 2014).
- *Safeco Ins. Co. v. Raisch*, Case No. C 11-05332 PSG (N.D.Cal., March 20, 2013).

A final problem is that § 503(a) is couched in the discretionary "may enter a charging order" which frequently leads to confusion as to what circumstances may or may not exists that would cause the court to deny the charging order. This "may" should probably be replaced by the mandatory "shall", which would be consistent with other judgment enforcement remedies which are automatically issued by the clerk, *i.e.*, levies and garnishments, etc.

Indeed, there is a question of whether the motion itself should be required. With other judgment enforcement remedies, the clerk simply issues the appropriate Writ, and then there is a hearing only if either the debtor or a third-party has a problem with the relief sought, *i.e.*, the debtor asserts a claim of exemption, or a bank asserts a priority lien on funds of the debtor.

### 3. Order Form Generally: Most issues to the form of the charging order

Many of the judgment enforcement remedies have statutory forms, *e.g.*, garnishment summons. Again, the charging order procedure is *ad hoc*, and there is nothing like a standard form to be utilized by creditors. It would be helpful for the Comment to include an exemplar form charging order.

There is likewise considerable confusion about the extent of the application of § 503(b)(2) ("make all other orders necessary to give effect to the charging order"). *See, e.g.*, *Law v. Zemp*, 362 Or. 302 (Jan. 11, 2018) (creditor must make evidentiary showing to obtain ancillary supporting terms in a charging order).

It is suggested that § 503 should be amended such that all consideration of any kind passing to a D/M should be considered to be in the nature of of a distribution and thus subject to the charging order, without regard to how it is characterized by either the D/M or the entity, *i.e.*, loans, salary, payment of the D/M's credit cards and other expenses, use of vehicle, etc.

**4. Order Form Future Interests: How the charging order affects subsequently-acquired interests**

Assume that at the time the charging order is entered, the D/M owns a 20% interest in the entity, as one of five members. Later, another member withdraws and the D/M's interest increases to 25%. Is the additional 5% interest subject to the charging order?

It is suggested that § 503 be amended to provide that future interests, a/k/a after-acquired interests, be subject to the prior charging order. This is again consistent with other judgment enforcement liens which likewise pick up after-acquired property, *i.e.*, an abstract of judgment will pick up and apply to a new parcel that the debtor takes title to in the county, such as from an inheritance.

Opinions on this subject include:

- *Meyer v. Christie*, 2011 WL 4857905 (D.Kan., Slip Copy, Oct. 13, 2011).
- *Presidential Facility, LLC v. Debbas*, Case No. 09-12346 (E.D.Mich., April 12, 2013).

**5. Exemptions: Available state and federal protections that may apply to charging orders**

While § 503(g) provides that the D/M may take advantage of any exemption, there is no guidance on how or when the D/M may assert the exemption. This should be corrected; presumably, the D/M must assert or lose the exemption at the hearing on the charging order.

Note that most judgment enforcement remedies that take something from the debtor are accompanied by statutory warnings that the debtor must assert any exemption within X days or lose the exemption.

An unsettled issue is whether a D/M may assert the Federal Wage Garnishment Law, 15 U.S.C. §§ 1671, *et seq.*, should apply to limit the charging order to 25% of the D/M's net disposable income, where the D/M can demonstrate that the distribution, or a part of the distribution, derives from the D/M's labors. For an analogous situation, *see U.S. v. Alexander*, 2016 WL 2893406 (D.Ariz., 2016).

Opinions on exemptions include:

- *U.S. v. Alexander*, 2016 WL 2893406 (D.Ariz., 2016).
- *In re Holt*, Bk.D.S.C. No. 13-02506-dd (Sept. 12, 2013).
- *In re Singh*, Case No. 11-15433 (N.D.Ohio, Sept. 19, 2012).

**6. Intra-Member Disputes: Where one member obtains a charging order against another**

The Harmonized Acts provide little guidance in the area of intra-member disputes, *i.e.*, where one member obtains a judgment and charging order against the interest of another member. In that circumstance, there is an issue whether charging order exclusivity should apply to limit the creditor/member's remedy to a charging order against the D/M's interest, since "Pick Your Partner" is not being violated.

Resolution of this issue may have significant effects upon the dynamics of the partnership, however, since it may or may not alter the voting powers of the members and also impact other members who are not party to the dispute.

This is an issue that the members should be empowered to address in the operating agreement, but it is also suggested that § 503 be amended to provide a default setting in the absence of resolution in the operating agreement (and almost no operating agreements address this subject).

Some of the opinions on intra-member disputes include:

- *Gillet v. ZUPT, LLC*, 2017 WL 716633 (Tex.App. 14th Distr., Feb. 23, 2017).
- *Young v. Levy*, 2014 WL 2741060 (Fla.App., June 18, 2014).
- *Voll v. Dunn*, 2014 WL 7461644 (Conn.Super., Nov. 10, 2014).

## D. INTERSTATE

### 1. Conflicts Of Law: Determining which state's laws apply to a charging order dispute

The Harmonized Acts do not offer direct guidance on which state's laws should govern such a dispute, which has frequently led to confusion.

Implicitly, § 501 states that "[a] transferable interest is personal property", and for personal property the conflict of law pointer is usually to the state of the debtor's residence. The D/M's frequently attempt to apply the law of the entity's jurisdiction formation on some ground or another, almost always unsuccessfully, but these attempts waste the resources of the court and the parties. Thus, it would be preferable to amend § 503 to expressly state a clear and unequivocal conflict of law rule.

Opinions addressing conflict of law issues in relation to charging orders include the following:

- *Wells Fargo Equip. Fin. v. Retterath*, 2019 WL 1574686 (Iowa, April 12, 2019).
- *Peach REO, LLC v. Rice*, 2017 WL 2963511 (W.D.Tenn., July 11, 2017).
- *Earthgrains Baking Co. v. Sycamore Family Bakery, Inc*., D.Utah Case No. 09CV523 (Aug. 21, 2015).
- *Mahalo Investments III, LLC v. First Citizens Bank and Trust Co., Inc*., 2015 WL 687922 (Ga.App., Feb. 19, 2015).
- *Capital Trans Int'l, LLC v. Int'l Petroleum Investment Co*., 2013 WL 557236 (M.D.Fl., 2013).
- *American Nat'l Bank v. Medved*, 281 Neb. 799, 2011 WL 2586341 (2011).
- *American Institutional Partners, LLC v. Fairstar Resources, Ltd*., 2011 WL 1230074 (D.Del., Mar. 31, 2011).
- *Koh v. Inno-Pacific Holdings, Ltd*., 114 Wash.App. 268, 54 P.3d 1270 (2002).

### 2. Jurisdiction: Issues relating to the court's authority over out-of-state LLCs

The courts have frequently struggled the issue of whether there must be personal jurisdiction over the entity for the charging order to be issued. In my opinion, the correct rule would be that that the court does not need

jurisdiction *in personam* to place the lien on the D/M's entity (any more than a creditor would need jurisdiction over Intel to place a lien on the debtor's Intel stock shares), but that personal jurisdiction would be required to enforce the charging order against the entity, *i.e.*, if the court of judgment does not have personal jurisdiction over the entity, then to enforce the charging order against the entity as to distributions the creditor would need to domesticate the judgment in the jurisdiction where the entity is found. However, even as to distributions, the court of judgment would be able to enforce the charging order against the D/M, *i.e.*, compel the D/M to pay over distributions to the creditor, since personal jurisdiction over the D/M has already been established.

At the very least, this issue needs to be fully addressed in the Comment to § 503, but because jurisdiction is a critically important threshold issue, perhaps it would warrant a statutory change.

Opinions that have discussed the issue include:

- *German American Capital Corp. v. Morehouse*, 2017 WL 3411941 (D.Md., 2017).
- *Arayos, LLC v. Jimmie Ellis*, 2016 WL 1642676 (S.D.Ala., 2016).
- *Spates v. Office of the Attorney General*, 2016 WL 354417 (Tex.App.14th Dist., Jan. 28, 2016).
- *Merrill Ranch Properties, LLC v. Austell*, 2016 WL 1176823 (Ga.App., 2016).
- *Vision Marketing Resources, Inc. v. McMillin Group, LLC*, 2015 WL 4390071 (D.Kan., July 15, 2015).
- *Wells Fargo Bank v. Barber*, 2015 WL 470589 (M.D.Fla., Feb. 4, 2015).
- *Shanghai Real Estate Ltd. v. Greenberg*, 2014 WL 660624 (Conn.Super., Jan. 28, 2014).
- *Rockstone Capital, LLC v. Marketing Horizons, Ltd*., 2013 WL 4046597 (Conn.Super., Unpublished, July 17, 2013).
- *Bank of America, N.A. v. Freed*, ___ N.E.2d ____, 2012 IL App (1st) 110749, 2012 WL 6725894 (Ill.App. 1 Dist., 2012).

### 3. Foreign Entities: Charging orders against out-of-state entities

The single most obvious and notorious flaw in the ULLCA relates to the unintended exclusion of foreign LLCs from the application of Article V, such that the charging order provisions have been held not to apply to LLCs not formed within the state. This was of course not the intended result, utterly makes no sense within the statutory scheme of the ULLCA, and it requires a statutory fix.

Opinions considering the issue include:

- *Peninsula Advisors, LLC v. Fairstar Resources Ltd*., Case No. 10-CV-489 (D.Del., Feb. 5, 2014).

- *Fannie Mae v. Heather Apartments LP*, 2013 WL 6223564 (Minn.App., Unpublished, 2013).

## E. CREDITOR RESTRICTIONS

### 1. Information Rights: Creditors' ability to access information about the LLC

The courts have struggled to determine what information that a creditor holding a charging order is entitled to, though usually end up with the correct decision.

This can be fixed by an expanded Comment noting that a creditor as a mere lienholder (or even as a involuntary assignee after foreclosure) has no rights *in that capacity* against the entity.

However, a creditor normally in judgment enforcement proceedings is entitled to whatever information the debtor receives about the debtor's investment, which would mean information that the debtor receives from the entity, *i.e.*, if the debtor can obtain information from the entity, the debtor must do so and then turn that information over to the creditor pursuant to the creditor's appropriate discovery request or at a debtor's examination. If this information requires extraordinary confidentiality for the entity — say, the D/M is the CFO of the company — then protective orders or the appointment of a receiver would be appropriate.

Opinions discussing this issue include:

- *Succession of McCalmont*, 2018 WL 6521176 (La.App., Cir. 3, Dec. 12, 2018).

- *GenX Processors Mauritius Ltd. v. Jackson*, 2018 WL 5777485 (D.Nev., Nov. 2, 2018).

- *Dream Games v. PC Onsite LLC*, 2016 WL 1554978 (D. Ariz., 2016).

- *Mack Film Development, LLC v. Benevolent Partners, L.P.*, 2014 WL 929702 (Conn.Super., Fairfield, Feb. 6, 2014).

- *In re Boone County Utilities, LLC*, Adv.Proc. No. 12-50128 (Bk.S.D.In., Sept. 17, 2014).

- *Rock Bay, LLC v. Eighth Judicial District Court*, 129 Nev. Adv. Op. 21, 2013 WL 1349284 (Nev., April 4, 2013).

### 2. Management & Voting Rights: Rights of creditor after charging order issued

Courts continue to face arguments by creditors that as holders of charging orders they should have the right to participate in the management of the entity and vote the D/M's interests. While the courts have so far rejected these challenges (at least outside the SMLLC context), it would be preferable to amend the statute to make this clear.

Opinions addressing this issue include:

- *Southlake Equipment Co., Inc. v. Henson Gravel & Sand, LLC*, 213 Okla.Civ.App. 87 ( 2013).

- *Green v. Bellerive Condominiums LP.*, 135 Md.App. 563, 763 A.2d 252 (Md.Sp.App., 2000).

## F. LIEN EFFECT AND PRIORITY

### 1. Lien: The lien effect of a charging order and priority issues

One of the hottest areas of litigation involving charging orders is that of lien priority, both of charging order liens against other types of liens and competing charging orders. The issue exists, in part, because there is substantial uncertainty regarding the following:

1. How and when is a charging order lien perfected?

2. What is the effect of the perfection of a charging order lien in one state on other states?

3. Where must a charging order be perfected?

The answers to these questions are not found in § 503, and that section should be amended to attempt to address these issues. Merely expanding the Comment will likely not be effective, since lien perfection and priority

questions are often determined by other statutes, and the charging order lien perfection and priority fix requires statutory equivalency.

Some illustrative opinions on this issue include:

- *MDQ, LLC v. Gilbert, Kelly*, 2019 WL 948726 (Cal.App., Distr. 2, Feb. 27, 2019).
- *Capstone Bank v. Perry-Clifton Enterprises, LLC*, 2017 WL 5894915 (Fla.App., Nov. 30, 2017).
- *JPMorgan Chase Bank v. McClure*, 2017 CO 22, 2017 WL 1321334 (Colo., April 10, 2017).
- *SEC v. Detroit Memorial Partners, LLC*, 2016 WL 6595942 (N.D.Ga., Nov. 8, 2016).
- *Delaware Acceptance Corp. v. Estate of Metzner*, 2016 WL 632893 (Del.Ch., Unpublished, Feb. 17, 2016).
- *In re Dzierzawski*, 2015 WL 1612092 (Bk.E.D.Mich., 2015).
- *Lefkowitz v. Quality Labor Mgt., LLC*, 2014 WL 5877850 (Fla.App., Distr. 5, 2014).
- *Renteria v. Canepa*, Case No. 3:11-cv-00534-RCJ-CWH (D.Nev., 2013).
- *P.B. Surf, Ltd. v. San Paloma Partners, L.P.*, 2012 WL 5511019 (N.D.Ala., 2012).

### 2. Lien: Lien effect generally

The acts are unclear as to the effect of a lien on a member's interest. For example, assume that A, B, C and D each own 25% of XYZ LLC, and each of their interests are subject to a lien (whether voluntary or involuntary). Does this mean that XYZ LLC itself could not issue new interests in violation of the liens? Or, viewed from a different angle, could a creditor complain because the creditor had a lien on 100% of the interests but is now being diluted?

## G. COMPLIANCE

### 1. Compliance: Issues for the LLC and non-debtor members in complying with a charging order

The Harmonized Acts make no provisions for a court to enforce a charging order, thus leaving the presumption that the appropriate remedy sounds in contempt.

Acts of non-compliance with a charging order typically fit into the following categories:

1. Non-compliance by the entity, by decision of the D/M;

2. Non-compliance by the entity, by decision another member;

3. Non-compliance by the D/M; and

4. Collusive non-compliance by the D/M, the entity, and/or other members.

There is also a distinction to be drawn between willful non-compliance (what contempt requires) and non-willful non-compliance (*i.e.*, negligence) for which contempt is not available and the creditor's remedy would sound in damages.

The contempt remedy requires the creditor to obtain an Order to Show Cause (OSC) re Contempt (still known in some states as a Writ of *Fieri Facias*), and go through a lengthy evidentiary hearing process. Conversely, damages for a negligent distribution are usually remedied through a creditor's suit or similar device, similar to where a bank allows a debtor to withdraw money pending a levy. It is probably satisfactory for an expanded Comment to explain this difference.

The non-compliance may also be divided between the making of a distribution to the D/M in violation of the charging order, and the making of so-called "imputed income" to the D/M by paying the D/M's expenses, such as credit cards, car leases, etc. This issue probably requires a change to § 503 to make it clear that all consideration of any kind passing to a D/M is subject to the charging order, and that the entity is directly liable to the creditor for a like amount of the consideration given by the entity but not distributed to the creditor.

Opinion addressing the issue of compliance with a charging order include:

- *Earthgrains Baking Companies, Inc. v. Sycamore Family Bakery, Inc.*, 2019 WL 6001940 (D.Utah, Nov. 14, 2019).

- *Golfwood Square LLC v. O'Malley*, 2018 IL App (1st) 172220-U, 2018 WL 4370875 (Ill.App., Unpublished, Sept. 11, 2018).

- *Garcia v. Garcia*, 2018 WL 2316522 (Cal.App. Distr. 5, Unpublished, May 22, 2018).

- *SE Property Holdings, LLC v. The Rookery, LLC*, S.D.Ala. Civil No. 11-0014-WS-C (April 13, 2018).

- *Joshlin Bros. Irrigation v. Sunbelt Rental, Inc*., 2014 WL 248104, 2014 Ark. App. 65 (Ark.App., Unpublished, Jan. 22, 2014).

- *Seven Arts Pictures, Inc. v. Jonesfilm*, 2013 WL 599661 (5th Cir., Feb. 18, 2013).

- *In re Cowstone*, LLC, 2012 WL 2205565 (Bkrtcy.E.D.N.C., Slip Copy, June 14, 2012).

- *Buckeye Retirement Co. v. Buffa*, 2011 WL 6299681 (D.Conn., Dec. 16 2011).

**2. Receiver: The role of the receiver in charging order proceedings**

The courts have sometimes struggled with the issue of a receiver appointed pursuant to a charging order. Section 503(b)(1) states that the court may "appoint a receiver of the distributions subject to the charging order, with the power to make all inquiries the judgment debtor might have made . . .." Frequently, creditors attempt to have the receiver appointed for the entity itself, and take over the control and operations of the entity.

Thus, the receiver has essentially two powers: (1) receive distributions, and (2) obtain information from the entity.

The first power (receive distributions) is an oddity, because the distributions should be going from the entity directly to creditor anyway, and it is difficult to image situations where it would be beneficial to interpose the receiver in the middle.

The second power (obtain information from the entity) is the more practical purpose of the receiver, since the creditor is entitled to whatever information about the entity that the D/M is entitled, but the D/M may be less than cooperative in seeking that information or in providing it to the creditor.

The proper workings of the receiver could be better spelled out in an expanded Comment.

Opinions considering a receiver appointed in relation to a charging order include:

- *Morgan Stanley Smith Barney LLC v. Johnson*, 2020 WL 1222684 (March 13, 2020).
- *Morgan Stanley Smith Barney LLC v. Johnson*, 2018 WL 4654711 (D.Minn., Sept. 27, 2018).
- *Pajooh v. Royal West Investments LLC, Series E*, 2017 WL 1173892 (Tex.App., 2017).
- *Jonas v. Waterman*, 2013 WL 6231619 (D.Mont., 2013).
- *Limbright v. Hofmeister*, 2012 WL 5605437 (E.D.Ky., 2012).
- *U.S. v. Zabka*, 900 F.Supp.2d 864 (C.D.Ill., 2012).
- *Deutsch v. Wolff*, 7 S.W.3d 460 (Mo.App.W.D.,1999).
- *91st Street Joint Venture v. Goldstein*, 691 A.2d 272, 114 Md.App. 561 (Md.Sp.App., 1997).

## H. SINGLE MEMBER LLC

### 1. Single-Member LLCs: Enforcing the judgment against an LLC with a sole member

Since the *sine qua* non of charging order exclusivity is to protect the interest of non-debtor partners pursuant to the "pick you partnership" doctrine, the charging order remedy should not apply to a single-member LLC (SMLLC).

The ULLCA establishes a two-part procedure for dealing with SMLLCs: First, the creditor obtains a charging order lien under § 503(a); and, second, the creditor forecloses on the lien under § 503(f), which makes the creditor the new single member of the LLC, which then is presumably wound up so that its assets may be distributed to creditors.

It is suggested that this procedure is wasteful and somewhat duplicative, and that a creditor should simply be allowed to levy on the single interest in the same fashion as any general intangible. Consideration should also be given to simply allowing the creditor to levy directly upon the LLC's assets.

Note that there is an issue as to when the single member status of the entity is to be tested, considering that a wily debtor will attempt to have a strawman buy a 1% or other small interest in the LLC for value so as to destroy the single-member status. Whether the existing provisions are retained or new provisions are adopted, this issue should be addressed.

### 2. Expansion of SMLLC rules to situations where there are multiple members but the creditor holds a charging order against all the members

Assume that there are two 50% members in an LLC and the same creditor holds a charging order against both members, i.e., there are no non-debtor members to the LLC. If the creditor forecloses, then the creditor would be the involuntary assignee of 100% of the economic interests in the LLC, but presumably would still have no other rights. Fundamentally, there is no reason why the situation of where all the outstanding interests have been subject to a charging order lien and/or foreclosure should be treated any differently than in the SMLLC context.

## I. FORECLOSURE

### 1. Foreclosure: Liquidation by judicial sale of the debtor's right to distributions

While foreclosures of charging order liens are very rare (because it rarely improves the creditor's position, and may in fact worsen it), when a creditor does move to foreclose there is often confusion about what happens.

The confusion manifests itself in the creditor (and sometimes the court) thinking that foreclosure is of the entity itself, and not merely the charging order lien. This confusion can be substantially negated by an expanded Comment on the issue that the foreclosing creditor becomes no more than an involuntary assignee of the interest and with no greater rights. No statutory change is suggested.

Opinions addressing the foreclosure of charged interests include:

- *Preservation Holdings, LLC v. Norberg*, 2019 IL App (1st) 181136 (June 14, 2019).
- *In re Talbut*, 2016 WL 937373 (N.D.Ohio, Slip Copy, 2016).
- *Disalvo Properties, LLC v. Bluff View Commercial, LLC*, 2015 WL 3759402 (Mo.App., 2015).
- *Levy v. Carolinian, LLC*, 2014 WL 4347503 (S.C., 2014).
- *Kriti Ripley, LLC v. Emerald Investments, LLC*, 2013 WL 3200596 (S.C., June 26, 2013).

## J. REPURCHASE/REDEMPTION RIGHTS

### 1. Repurchase/Redemption Rights: Third-parties' ability to purchase the charged interest

Because under § 503(e) the predicate of repurchase or redemption rights is the initiation of proceedings to foreclose the charged interest, and foreclosures are very rare as it is, instances of such repurchase or redemption of the D/M's interest are almost non-existent. They are then pushed to the very brink of extinction by the requirement that the creditor then be paid the full amount of the judgment to effectuate such repurchase or redemption.

Nonetheless, there are two issues that could be addressed:

1. Whether such repurchase or redemption should be allowed to occur if the creditor and the LLC or non-debtor members agree to a price.

2. What happens if there are competing attempts to repurchase or redeem the D/M's interest.

Note that if there is a power-struggle going on with the entity. Currently this seems to be addressed by the language of § 503(f) which gives the repurchasing or redeeming party only the rights *as to the extent of the D/M's former interest* only the rights that the creditor would have had, being that of an involuntary assignee.

The opinions which have addressed repurchase or redemption rights include:

- *Leasing Innovations, Inc. v. R&D Mainman Family Limited Partnership,* 2016 NY Slip Op 31330(U) (N.Y. County Super., 2016).

- *Eights & Jackson Investment Group v. Kaw Valley Bank*, 2013 WL 183753 (D.Kan., Jan. 17, 2013).

## K. APPEAL

### 1. Appeal: Issues relating to the appeal of a charging order

How appeals of charging orders (and foreclosures thereof) are taken provide a myriad of issues that litigants and the courts have struggled with, including:

1. Whether a charging order is a final appealable order.

2. What is the correct appellate procedure.

3. Whether the entity as a non-party to the case has standing to appeal the order.

The courts have reached conflicting results on whether the charging order is an immediate appealable order. Some courts treat charging orders as final appealable orders. Other courts disagree, and typically rationalize something to the effect that the "final order" will be that which results in the final satisfaction of the judgment, or at least something like that. These courts treat charging orders as in the nature of interlocutory orders, which makes little sense because the judgment has already been entered in the case. Where the courts do not treat charging orders as a final order, any effective appeal of the charging order must be made by an extraordinary writ.

It is suggested that § 503 be amended to provide that a charging order is a final appealable order, and that the parties to the charging order have an immediate appeal as of right. An expanded Comment to this effect will likely be of dubious effect.

Where the charging order affects the entity in some incorrect way, *e.g.*, the court gives the creditor management rights, the entity itself may need to appeal the charging order and this issue should also be considered.

The opinions addressing appellate issues in the charging order context include:

- *Rand v. Steinberg*, 2018 WL 4183449 (Md.Spec.App., Unreported, Aug. 31, 2018).
- *Rogers Grp., Inc. v. Gilbert*, 2016 WL 2605651 (Tenn.App., 2016).
- *Jack M. Sanders Family Limited Partnership v. Roger T. Fridholm Revocable Living Trust*, 2014 WL 1603546 (Tex.App.Distr. 1, 2014).

## L. RELATION TO OTHER REMEDIES

### 1. Exclusivity: The charging order as the sole remedy available to creditors and exceptions

The phrase "exclusive remedy" as found in § 503(h) has caused considerable confusion. This is largely because the term "remedy" is a statutory term-of-art that normally refers to a list of enumerated remedies in a particular state's judgment enforcement laws, but is misinterpreted to mean something like "exclusive outcome" — which isn't the same thing.

A problem is that what constitutes a "remedy" varies from state to state, and there are other avenues of a creditor to obtain relief (such as reverse veil piercing or fraudulent transfer actions) that may or may not considered to be a "remedy". Thus, there may avenues of relief that are desired for

creditors to access, but which may be off-limits because of the phrase, and there may be avenues of relief that are undesirable for creditors to access that are available to creditors because they are not technically "remedies".

Thus, it is suggested that consideration be given to using some other phrase than "exclusive remedy" in the text of § 503(h).

Opinions considering the issue of charging order exclusivity include:

- *U.S. v. Wilhite*, 2017 WL 5517410 (D.Colo., Nov. 17, 2017).
- *Devoll v. Demonbreun*, 2016 WL 4538805 (Tex.App., Aug. 31, 2016).
- *Leonard v. Leonard*, (N.J.Super.A.D., 2012).
- *Robert Christensen v. John Oedekoven*, 95 Wy. 3 (Wyo.App., 1995).

**2. Voidable Transactions/Fraudulent Transfers: Issues relating to avoidable transfers of interests**

There has been some litigation over whether a transfer made by a financially-distressed debtor to an entity could be avoided as a fraudulent transfer, or whether the "exclusive remedy" phrase operates to eliminate such fraudulent transfer claims as well. It is suggested that an expanded Comment to the effect that such fraudulent transfer claims are not barred by the "exclusive remedy" phrase be included.

Some of the opinions on this subject include:

- *Wilson v. Pauling*, 2020 WL 2197931 (D.Colo., May 6, 2020).
- *Fannie Mae v. Grossman*, 2014 WL 4055371 (D.Minn., 2014).
- *Scottsdale Ins. Co. v. Tolliver*, 2012 WL 524414 (N.D.Okla., 2012).

**3. Alter Ego/Veil Piercing and Choice of Law**

In egregious cases involving (mostly) single-member LLCs, an alternative remedy for a creditor is to add the LLC to the judgment on a so-called "reverse piercing" theory. However, the choice of law pointer for alter ego is typically to that of the state of formation, which may have "race to the bottom" laws that are so creditor-unfriendly that they violate public policy in the forum state. Thus, it is suggested that in certain circumstances the

forum state may instead choose its law in determining whether the alter ego remedy should be employed, as opposed to the of the state of formation which may have little or nothing to actually do with the LLC other than it was created there.

END