

April 27, 2017
**Drafting Committee on the
Uniform Protected Series Act**
Where We Are and Where We Are Going
Agenda for Next (and Final) Internet Meeting

Where We Are and Where We Are Going

We have almost finished the substantive decision making for the act. Only six substantive issues remain, none of which is earth shaking. We will discuss and decide these issues at our next and final internet meeting, Thursday, May 4, 2017, from 3:00-4:30 PM Central Time (agenda below).

The drafting of both the text and comments is very advanced. With one exception, discussed below, the draft to be issued early next week is consonant with the most recent comments provided by John Stieff, our Style liaison.

The Chair appointed a Fine Tooth Comb Subcommittee (“FTCS”) to do a line-by-line review of the statutory text, proofreading, flyspecking, and identifying and resolving any other drafting problems. The FTCS consists of Allan Donn, Harry Haynsworth, Lisa Jacobs, Ed Smith, the Reporter, and *ex officio* the Chair.

The annual meeting draft is due at the ULC office by June 2, 2017.

At the annual meeting, we read the morning of July 15, 2017, from 8:15 AM to noon. We will have a meeting on July 14th, beginning at 4 PM, room to be determined, to discuss any last minute issues and make reading assignments. If history is a reliable guide, the meeting will last 15-20 minutes.

The Pivotal Issue with the Committee on Style

The Committee on Style wants to replace “solely by reason of” with “solely because” throughout the act. For several very substantial reasons, the Chair rejects this idea (and the Reporter concurs). Also, the Chair and Vice Chair of the Standing Committee on the Harmonization of Business Entity Acts vehemently oppose Style’s position. Discussions continue.

Agenda for Next (and Last) Internet Meeting – Remaining Substantive Issues

We will discuss the remaining six issues in the following order:

1. LLC statutes that provide constructive notice for publicly filed records¹

¹ A few jurisdictions, e.g. Pennsylvania, have adopted the hub and spoke approach of the Uniform Business Organizations Code (“UBOC”). In these jurisdictions, a constructive notice provision will likely be in the hub rather than in the LLC statute. The same is true for name requirements, registered agents, entity transactions, etc. For convenience’s sake, this email

- a. Should the act provide analogously (by extrapolation) for constructive notice for records filed under the act?
 - b. If so, should the act also authorize a statement of protected series dissolution?
2. Restrictions in the operating agreement on power or purpose of a limited liability company – applicability at the protected series level
 - a. In the current draft:
 - i. the default rule is that a protected series:
 - has whatever powers the limited liability statute grants a limited liability company; and
 - may have any purpose that the statute permits a limited liability company to have; and
 - ii. an operating agreement's limitation on a company's power or purpose does not automatically "flow through" to the protected series level and *vice versa*.
 - b. The issue – should the act provide as a default rule that a restriction on power or purpose at the company level flows through to the protected series level?
3. Foreign registration and certificates of good standing
 - a. The situation:
 - i. The act applies foreign registration provisions to a foreign protected series as if the foreign protected series were a foreign limited liability company.
 - ii. Some LLC statutes require a certificate of good standing when a foreign limited liability company seeks to register to do business in the state.
 - iii. However, most LLC statutes do not require a public filing to establish a protected series, which precludes a certificate of good standing at the protected series level.
 - b. The issue – how should the act apply the certificate requirement at the foreign protected series level when no certificate is available at that level? Two possibilities:
 - i. Require a statement of good standing re: the foreign series limited liability company and re: the foreign protected series an affidavit of "all is well" from a person with governance authority over the foreign protected series.
or
 - ii. Same approach except require that the affidavit be from an individual authorized by the foreign series limited liability company.
4. Section 705(a) and the inclusion of criminal proceedings

refers only to LLC statutes. In the act, a legislative note will explain the situation and, where appropriate, bracketed instructions to "cite" will read as follows: [cite limited liability company statute or other statute pertaining to].

- a. Section 705(a) currently states:
SECTION 705. DISCLOSURE REQUIRED WHEN FOREIGN SERIES LIMITED LIABILITY COMPANY OR FOREIGN PROTECTED SERIES PARTY TO PROCEEDING.
(a) Not later than [30] days after becoming a party to a proceeding before a civil, criminal, administrative, or other adjudicative tribunal of this state or a tribunal of the United States located in this state: ...
 - b. Should this section omit criminal proceedings?
 - i. The question of discovery in a criminal matter is beyond the Committee's competence.
 - ii. On information and belief, requiring a criminal defendant to volunteer information to the prosecutor is at least unusual, probably rare, and possibly unprecedented.
 - c. Should this section include arbitration proceedings, and, if so, expressly? E.g.: –
 - i. “or other adjudicative tribunal ~~of~~ located in this state or”
or
 - ii. “other adjudicative tribunal of this state, including an arbitration located in this state, or”
5. Access of a series limited liability company to information maintained by its protected series; access of protected series to information maintained by the company and other protected series
- a. Records pertaining to associated property
 - i. The situation:
 - A protected series' apparently adequate Section 301 recordkeeping could be rendered ambiguous in light of records maintained by the company or other protected series of the company. The company faces a comparable problem.
 - Access to associated property records of other “family members” allows the company and each protected series to guard against such ambiguity.
 - The operating agreement could address this problem delegating recordkeeping responsibility for all family members to one person – the company, one of the protected series, or a third party (e.g., a management company).
 - ii. The issues:
 - whether to have a default rule providing access or merely a comment noting the trap for the unwary; and
 - if a default rule is to be provided, what should it be?
 - b. A default right to access other information seems unnecessary (members have access rights, see Section 305) and imprudent (conflation/piercing/affiliate liability concerns).

6. Formalities and vertical piercing

- a. The current comment to Section 401 explains the committee's current position, which might rest on an incorrect premise.

In the context of non-series limited liability companies, some limited liability company statutes modify the traditional grounds for piercing (i.e., overcoming the shield) to the following effect: "The failure of a limited liability company to observe formalities relating to the exercise of its powers or management of its activities and affairs is not a ground for imposing liability on a member or manager for a debt, obligation, or other liability of the company." Uniform Limited Liability Company Act (2006) (Last Amended 2013), Section 304(b). This act contains no such language, because such language might be read as undercutting the strict formalities required to associate an asset with a protected series or series limited liability company.

- b. The underlined language is accurate as far as it goes but does not take into account a possible effect of Section 401(c), which provides

(c) A claim seeking to disregard a limitation in subsections (a) or (b) is governed by the principles of law and equity, including a principle providing rights to creditors or holding a person liable for a debt, obligation, or other liability of another person, which would apply if each protected series of the series limited liability company were a limited liability company:

(1) organized separately from the company that established the protected series; and;

(2) distinct from the company and any other protected series of the company.

If an enacting state's LLC statute contains Uniform Limited Liability Company Act (2006) (Last Amended 2013), Section 304(b) or comparable "formalities don't matter" language, a court might apply the "formalities don't matter" concept to the horizontal shields. For example, a court might analogize an effort to pierce a horizontal shield to an effort to hold one wholly-owned subsidiary of a company liable for the debts of another wholly-owned subsidiary of the company. For example:

"Granted, Section 304(b) applies by its terms only to an attempt to hold a parent liable for the debts of a subsidiary. However, this court sees no valid policy reason against extending analogous protection as to plaintiff's attempt to hold one sibling of the parent liable for the debt of another

sibling of the parent. Piercing having begun as a claim in equity, the court's equitable power is sufficient to so hold."

- c. If the Committee wants to preclude such an extension, the should address the matter, in the statute (the Reporter's preference) or in a comment. The former approach might read as follows:

Section 401

(a) A person is not liable, directly or indirectly, by way of contribution or otherwise, for a debt, obligation, or other liability of:
[vertical shield]

(b) Subject to subsection (c) and Section 403: [horizontal shields]

Alternative #1 [(c) The failure of a limited liability company or a protected series to observe formalities relating to the exercise of its powers or management of its activities and affairs is not a ground to disregard a limitation in subsection (a) but may be a ground to disregard a limitation in subsection (b).

Alternative #2 [(c) Subject to Sections 301 and 403, the failure of a limited liability company or a protected series to observe formalities relating to the exercise of its powers or management of its activities and affairs is not a ground to disregard a limitation in subsection (a) or (b).

(d) Subject to subsection (c), aA] [(c) A] claim seeking to disregard a limitation in subsections (a) or (b) is governed by the principles of law and equity, including a principle providing rights to creditors or holding a person liable for a debt, obligation, or other liability of another person, which would apply if each protected series of the series limited liability company were a limited liability company:

(1) organized separately from the company that established the protected series; and;

(2) distinct from the company and any other protected series of the company.