700 NORTH STREET
POST OFFICE BOX 136
JACKSON, MISSISSIPPI 39205-1036

STATE OF MISSISSIPPI
SECRETARY OF STATE
DELBERT HOSEMANN
DIVISION OF POLICY AND RESEARCH

TELEPHONE (601) 359-3101
FACSIMILE (601) 359-1499
www.sos.state.ms.us/policy_research

2008 BUSINESS REFORM COMMITTEES
MEETING OF THE LLCS AND PARTNERSHIPS COMMITTEE

July 10, 2008
11:30 A.M.

Secretary of State's Office
700 North Street
Jackson, Mississippi

AGENDA

1. Welcome – Cheryn Baker

2. Roll Call of Persons Attending by Teleconference

3. Approval of minutes of June 12, 2008 Meeting

4. Introduction of Panelists – Cheryn Baker

5. Presentations by Panelists –

    a. Thomas E. Rutledge
    b. Elizabeth S. Miller
    c. Scott E. Ludwig
    d. Robert R. Keatinge

6. Formation of Sub-Groups

    a. Model registered Agent Act Group
    b. Other Groups

7. Other Business

8. Reminder of Upcoming Meetings: Dates and Future Programs – Cheryn Baker

9. Adjourn 1:00 P.M.

Upcoming Meeting Dates

July 31

August 14

August 28

September 8, No Meeting -- Recommendations Due

Materials for this Meeting:

1. Minutes of June 12, 2008 Meeting
2. Biographical Sketch of Thomas E. Rutledge
3. Biographical Sketch of Elizabeth S. Miller
4. Biographical Sketch of Scott E. Ludwig
5. Biographical Sketch of Robert R. Keatinge
6. LLCs Act Comparison Chart MS, DE, and RULLCA
7. MORAA Committee Roster
8. MS Partnership Act Statute
9. Summary of Articles
10. The Miller and Rutledge Article – "The Duty of Finest Loyalty and Reasonable Decisions: The Business Judgment Rule in Unincorporated Business Organizations?"
11. The Sandra Miller Article – " The Role of the Court in Balancing Contractual Freedom with the need for Mandatory Constraints on Opportunistic and Abusive Conduct in the LLC"
12. The Series LLC Article – "The Loaves and Fishes of Subchapter K"
13. Sample LLC Forms and Filing Fees from other States

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Robert R. Keatinge

Robert Keatinge has been a Visiting Associate Professor at Suffolk University School of Law for the 2007-2008 academic year and is Of Counsel to the Denver law firm of Holland & Hart LLP. He practices in the areas of business organizations, taxation, and professional responsibility. Mr. Keatinge has represented a wide variety of business organizations and their owners from small start-up companies to publicly traded corporations. He has written and spoken nationally in the areas of business law, taxation and professional responsibility. He is the co-author of Keatinge and Conaway on Choice of Business Entity (2008) and Ribstein and Keatinge on Limited Liability Companies Second Edition (2004) (both Thomson/West) as well as author of law review and other articles on business, tax, and professional responsibility. He has been an adjunct professor at the University of Denver, College of Law and the University of Miami, School of Law. He is a fellow of the American College of Tax Counsel, a member of the American Law Institute, and is listed in the current Best Lawyers in America in three specialties (Corporate Governance and Compliance Law, Corporate Law and Tax Law), Who's Who in America, and other publications. He is a current member of the ABA Business Law Section/National Conference of Commissioners on Uniform State Laws (NCCUSL) Joint Editorial Board on Unincorporated Business Organizations and the Association of Professional Responsibility Lawyers. He has been ABA Advisor to the NCCUSL Drafting Committees on Revisions to Uniform Limited Liability Company Act; the Revision to the Uniform Limited Partnership Act (2001) and the Uniform Limited Liability Company Act (1996) and an ABA Section of Real Property Probate and Trust Law adviser on the Model Entity Transactions Act and the Model Statutory Trust Entity Act and was a member of the Ad Hoc Subcommittee to Comment on the Revised Uniform Partnership Act. He is former Chair of the Colorado Bar Association Business Law and Taxation Sections. He is former chair of the Committees on Taxation and on Partnerships and Unincorporated Business Organizations of the ABA Business Law Section and of the Joint Editorial Board for the ABA/BNA Lawyer's Manual on Professional Conduct and a former Member of the American Bar Association House of Delegates.

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Scott E. Ludwig

Scott E. Ludwig is a member of the regional law firm of Bradley Arant Rose & White LLP (Huntsville, Alabama office), where his practice is devoted to business law (incorporated and unincorporated entities) and tax law. Scott is a member of the American College of Tax Counsel; listed in *The Best Lawyers in America* (Biotechnology, Corporate, Non-Profit/Charities, Tax, and Trust and Estates) and *Who's Who in American Law*. He is actively involved in the ABA's Business Law Section where he is the Vice-Chair of the Committee on LLCs, Partnerships and Unincorporated Entities, immediate past chair of the subcommittee on Limited Liability Companies, co-chair of the Revised Prototype Limited Liability Company Act Revision Task Force, co-chair of the Prototype Limited Liability Partnership Agreement subcommittee, and a member of the Limited Partnership subcommittee, General Partnership subcommittee, Negotiated Acquisitions Committee, Task Force on Model Joint Venture Agreement, and Taxation Committee. Scott is also chair of the Section's Publications Board, where he serves as a member of the Ad Hoc Committee on Content Distribution and is an incoming member of the ABA's Standing Committee on Publication Oversight. He is an ABA Section of Business Law advisor to the National Conference of Commissions of Uniform State Laws' Revised Uniform Limited Liability Company Act and Omnibus Business Organizations Code Study Committee. Scott is also a member of the ABA's Section of Real Property, Trust & Estate Law (Committees: Asset Protection Planning, Business Investment Entities, Partnerships, LLCs and Corporations, Estate and Gift Tax, Organizational and Operational Issues of Exempt Organizations, and State and Local Law Concerns of Exempt Organizations), and Section of Taxation (Committees: Corporate Tax (Subcommittee: Taxable Acquisitions), Partnerships and LLCs (including being a member of the Comment Committees in response to Notice 2000-29 and Notice 2005-43), Disregarded Entities, Estate Planning, State Tax Issues, Tax-Free Distribution, and State and Local Taxes). He has spoken at the ABA regarding surveys on Limited Liability Company State Taxation and Professional Unincorporated Entities. Scott is a member of the Alabama State Bar having been the Chair of the Tax Section and the Alabama LLP Act Committee and a member of the Alabama LLC Act and Alabama LP Act Revision Committees. Scott chairs the Task Force on Bar Governance for the Huntsville-Madison County Bar Association. He has been President of the Alabama Federal Tax Clinic and President of the Huntsville Financial and Estate Planning Council. He co-authored, *Second Circuit Affirms McNamee: Validity of Check- the-Box Regulations Again Confirmed*, Journal of Taxation (July, 2007); and *The Sixth Circuit Affirms Littriello: Check-the-Box Regulations Are Upheld*, Journal of Taxation (June, 2007). Scott is an editor of the *State Limited Partnership Laws* and the *State Limited Liability Company Laws* treatise by Aspen Publishers. He was a contributor to the *Model Real Estate LLC Operating Agreement*, The Business Lawyer (March 2008), *Model Joint Venture Agreement with commentary*, (ABA, 2006); and *The Model LLC Membership Interest Redemption Agreement*, The Business Lawyer (May, 2006). He was a co-reporter for the *Prototype Partnership Agreement for a Limited Liability Partnership Formed Under the Uniform Partnership Act(1997)*, The Business Lawyer (February, 2003) and *Prototype Limited Liability Partnership Agreement,* American Bar Association (2003). He co-authored *Selected Pitfalls Arising From the Use of Hybrid Entities, Part 2, Business Entities,* V. 4 (November/December 2002), as well as two editions of the *Alabama Limited Liability Company Handboo*k.

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Elizabeth S. Miller

Elizabeth S. Miller is a Professor of Law at Baylor University School of Law where she teaches Business Organizations, Business Planning, and related courses. Professor Miller speaks and writes extensively on business organizations topics, particularly partnerships and limited liability companies. She frequently appears on continuing legal education programs and is co-author of a three-volume treatise on *Business Organizations* published by Thomson/West as part of its Texas Practice Series. Professor Miller has just completed a term as Chair of the Partnerships and Unincorporated Business Organizations Committee of the Business Law Section of the American Bar Association. She is Chair Elect of the Council of the Business Law Section of the State Bar of Texas and is the immediate past Chair of the Partnership and Limited Liability Company Law Committee of the Business Law Section of the State Bar of Texas. Professor Miller has been involved in the drafting of legislation affecting Texas business organizations for many years and has served in an advisory or membership capacity on the drafting committees for numerous prototype, model, and uniform statutes and agreements relating to unincorporated business organizations. She currently serves on the drafting committee for the Omnibus Business Organizations Code, a joint project of the National Conference of Commissioners on Uniform State Laws and the American Bar Association. She also serves on the drafting committee that is revising the ABA Prototype Limited Liability Company Act. Professor Miller is an elected member of the American Law Institute and a Fellow of the American Bar Foundation and the Texas Bar Foundation.

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Thomas E. Rutledge

Thomas E. Rutledge is a member of Stoll Keenon Ogden PLLC (Louisville, Kentucky), where his practice is devoted to business and securities law with a specialized focus on the law of business organizations. He was a member of the committees that drafted the Kentucky Limited Liability Company Act and the Limited Liability Partnership amendments to the Kentucky Uniform Partnership Act and the 1994 and 2002 amendments to the Kentucky Business Corporation Act. He was the principal drafter of the Kentucky Revised Uniform Partnership Act (2006) and the Kentucky Uniform Limited Partnership Act (2006) and as well the 2007 amendments made among all the Kentucky business entity laws. Tom is actively involved in the LLCs, Partnerships and Unincorporated Entities Committee of the Section of Business Law, American Bar Association where he serves as editor of the PUBOGRAM (the committee newsletter), chair of the Subcommittee on Limited Liability Companies, and as co-chair of both the Model Limited Liability Company Act and Model LLC Transactional Documents subcommittees. He served as co-chair of the subcommittee that drafted the *Prototype Limited Liability Partnership Agreement*, and served as co-chair and reporter for the subcommittee that drafted the *Model Limited Liability Company Membership Interest Redemption Agreement*. He is also active with the Ad-Hoc Committee on Entity Rationalization and is an ABA Section of Business Law advisor to the National Conference of Commissioners of Uniform State Laws project to update the Uniform Limited Liability Company Act as well as to the drafting committees for the Uniform Entity Transactions Act and the Uniform Statutory [Business] Trust Act. Tom is a Fellow at the University of Louisville, School of Law and an Adjunct Professor at the University of Kentucky, College of Law. A frequent speaker and writer on business entity law, he has published in the *Kentucky Law Journal*, *Northern Kentucky Law Review*, *Baylor Law Review*, *South Dakota Law Review*, *St. Louis University Law Journal*, the *LLC Reporter*, the *LLC Advisor*, *Bench & Bar*, *Business Entities*, *Corporate Counsel Weekly*, *The Delaware Journal of Corporate Law*, *The Business Lawyer*, the *Brandeis Law Journal* and *Probate and Property*, and has articles forthcoming for *The Business Lawyer*, *Suffolk Law Review* and the *American Business Law Journal*. Tom is an editor of STATE LIMITED LIABILITY COMPANY AND PARTNERSHIP LAWS and of STATE LIMITED PARTNERSHIP LAWS, is a regular columnist to the *Journal of Passthrough Entities*, is named in both CHAMBER’S USA - AMERICA’S LEADING BUSINESS LAWYERS and BEST LAWYERS IN AMERICA, and is a member of the American Law Institute.

West's Annotated Mississippi Code Currentness
Title 79. Corporations, Associations, and Partnerships
Chapter 13. Uniform Partnership Act (1997) [Effective January 1, 2005] (Refs & Annos)
Article 1. General Provisions

§ 79-13-103. Effect of partnership agreement; nonwaivable provisions

(a) Except as otherwise provided in subsection (b), relations among the partners and between the partners and the partnership are governed by the partnership agreement. To the extent the partnership agreement does not otherwise provide, this chapter governs relations among the partners and between the partners and the partnership.

(b) The partnership agreement may not:

(1) Vary the rights and duties under Section 79-13-105 except to eliminate the duty to provide copies of statements to all of the partners;

(2) Unreasonably restrict the right of access to books and records under Section 79-13-403(b);

(3) Eliminate the duty of loyalty under Section 79-13-404(b) or 79-13- 603(b)(3), but:

(i) The partnership agreement may identify specific types or categories of activities that do not violate the duty of loyalty, if not manifestly unreasonable; or

(ii) All of the partners or a number or percentage specified in the partnership agreement may authorize or ratify, after full disclosure of all material facts, a specific act or transaction that otherwise would violate the duty of loyalty;

(4) Unreasonably reduce the duty of care under Section 79-13-404(c) or 79-13-603(b)(3);

(5) Eliminate the obligation of good faith and fair dealing under Section 79-13-404(d), but the partnership agreement may prescribe the standards by which the performance of the obligation is to be measured, if the standards are not manifestly unreasonable;

(6) Vary the power to dissociate as a partner under Section 79-13-602(a), except to require the notice under Section 79-13-601(1) to be in writing;

(7) Vary the right of a court to expel a partner in the events specified in Section 79-13-601(5);

(8) Vary the requirement to wind up the partnership business in cases specified in Section 79-13-801(4), (5), or (6);

(9) Vary the law applicable to a limited liability partnership under Section 79-13-106(b); or

(10) Restrict rights of third parties under this chapter.

CREDIT(S)

Added by Laws 2004, Ch. 458, § 103, eff. January 1, 2005.

HISTORICAL AND STATUTORY NOTES

Pursuant to its authority under Section 1-1-109, the Joint Legislative Committee on Compilation, Revision and Publication of Legislation ratified the correction of a typographical error in subsec. (a) of this section. The words "this act" were changed to "this chapter".

Uniform Laws:

This section is based upon § 103 of the Uniform Partnership Act (1997). See 6, Part I, Uniform Laws Annotated, Master Edition.

Miss. Code Ann. § 79-13-103, **MS ST** § **79-13-103**

Current through all 2007 Sessions and Chs. 302, 309, 312, 373 and 376 of the 2008 Reg. Sess.

END OF DOCUMENT

State of Tennessee
Department of State
Corporate Filings
312 Eighth Avenue North
6th Floor, William R. Snodgrass Tower
Nashville, TN 37243

CERTIFICATE OF CONVERSION
(Another Business Entity into LLC)

For Office Use Only

Pursuant to the provisions of §48-249-703 of the Tennessee Revised Limited Liability Company Act, the undersigned Limited Liability Company hereby submits this certificate of conversion:

1. The name of the domestic limited liability company as set forth in its articles of organization is:

____.

2. The name of the converting other business entity immediately prior to the filing of the certificate of conversion is:

____.

3. The jurisdiction in which the converting other business entity was formed is _______________ , its date of formation is ________________________ (month/day/year), and its business type is a ________________________________ .

4. All required approvals of the conversion have been obtained by the other business entity.

5. If the conversion is not to be effective upon the filing of the certificate of conversion and articles of organization, then the future effective date or time of the conversion to a domestic LLC is:

Date:______________________ , _______________Time ___________________

______________________________ ______________________________
Signature date **Signature**

______________________________ ______________________________
Signer's capacity **Name (typed or printed)**

State of Tennessee

Department of State
Corporate Filings
312 Eighth Avenue North
6th Floor, William R. Snodgrass Tower
Nashville, TN 37243

CERTIFICATE OF CONVERSION
(LLC into another Business Entity)

For Office Use Only

Pursuant to the provisions of §48-249-704 of the Tennessee Revised Limited Liability Company Act, the undersigned Limited Liability Company submits this certificate of conversion:

1. The current name of the of the domestic limited liability company (hereinafter referred to as the domestic LLC) is: ______________________________ .

   If different, the name of the domestic LLC under which its articles of organization were originally filed is:
   ______________________________ .

2. The date of filing of the original articles of organization of the domestic LLC was:
   ______________________ (month/day/year).

3. The name of the other business entity into which the domestic LLC is to be converted is ______________________, its jurisdiction of formation is ______________________, and its business type is a ______________________ .

4. All required approvals of the conversion have been obtained by the domestic limited liability company.

5. If the conversion is not to be effective upon the filing of the certificate of conversion, then the future effective date or time of the conversion is:
   Date: ______________ , ____________ Time ______________

6. The following box must be checked and the mailing address provided if the domestic LLC is converting to a foreign entity:

❑The foreign entity agrees that it may be served with process in this State in any proceeding for the enforcement of any obligation of the domestic LLC arising prior to the date of the conversion, irrevocably appointing the Secretary of State as its agent to accept service of process in any such proceeding. The address (including zip code) to which a copy of such process shall be mailed to it by the Secretary of State is:

______________________________ .

______________________ ______________________
Signature date Signature

______________________ ______________________
Signer's capacity Name (typed or printed)

State of Tennessee

Department of State
Corporate Filings
312 Eighth Avenue North
6th Floor, William R. Snodgrass Tower
Nashville, TN 37243

ARTICLES OF ORGANIZATION (LIMITED LIABILITY COMPANY)

(For use on or after 7/1/2006)

Reset Form

For Office Use Only

The Articles of Organization presented herein are adopted in accordance with the provisions of the Tennessee Revised Limited Liability Company Act.

1. The name of the Limited Liability Company is: ______________________________

____

(NOTE: Pursuant to the provisions of TCA §48-249-106, each limited Liability Company name must contain the words "Limited Liability Company" or the abbreviation "LLC" or "L.L.C.")

2. The name and complete address of the Limited Liability Company's initial registered agent and office located in the state of Tennessee is:

____
(Name)

____
(Street address) *(City)* *(State/Zip Code)*

____
(County)

3. The Limited Liability Company will be: *(NOTE: PLEASE MARK APPLICABLE BOX)*

☐ Member Managed ☐ Manager Managed ☐ Director Managed

4. Number of Members at the date of filing, if more than six (6): ______________ .

5. If the document is not to be effective upon filing by the Secretary of State, the delayed effective date and time is: (Not to exceed 90 days)
Date: ______________ , ______________ Time: ______________

6. The complete address of the Limited Liability Company's principal executive office is:

____
(Street Address) *(City)* *(State/County/Zip Code)*

7. Period of Duration if not perpetual: ______________________________

8. Other Provisions:

9. THIS COMPANY IS A NONPROFIT LIMITED LIABILITY COMPANY (Check if applicable) ☐

____
Signature Date

____
Signature

____
Signer's Capacity (if other than individual capacity)

____
Name (printed or typed)

State of Tennessee
Department of State
Corporate Filings
312 Eighth Avenue North
6th Floor, William R. Snodgrass Tower
Nashville, TN 37243

APPLICATION FOR REINSTATEMENT FOLLOWING ADMINISTRATIVE DISSOLUTION/REVOCATION (LLC)

For Office Use Only

Pursuant to the provisions of §48-245-303 or §48-246-503 of the Tennessee Limited Liability Company Act or §48-259-606 or §48-249-910 of the Tennessee Revised Limited Liability Company Act, this application is submitted to the Tennessee Secretary of State for reinstatement.

1. The name of the Limited Liability Company is ______________________________

   (Name change if applicable) ______________________________

   ____

2. The effective date of its administrative dissolution/revocation is ______________________________
   (must be month, day and year)

3. The ground(s) for the administrative dissolution/revocation

   ☐ did not exist.

   ☐ has/have been eliminated.

   [NOTE: Please mark the applicable box]

4. The Limited Liability Company name as listed in number one (1) satisfies the name requirements of Tennessee Limited Liability Company Act or Tennessee Revised Limited Liability Company Act, as applicable.

5. The Limited Liability Company control number assigned by the Secretary of State, if known is ______________________________.

____
Signature Date

____
Name of Limited Liability Company

____
Signer's Capacity

____
Signature

____
Name (typed or printed)

ROSS MILLER
Secretary of State
206 North Carson Street
Carson City, Nevada 89701-4299
(775) 684 5708
Website: secretaryofstate.biz

Articles of Organization Limited-Liability Company

(PURSUANT TO NRS 86)

USE BLACK INK ONLY - DO NOT HIGHLIGHT

ABOVE SPACE IS FOR OFFICE USE ONLY

1. ***Name of Limited-Liability Company:*** *(must contain approved limited-liability company wording; see instructions)*	Check box if a Series Limited-Liability Company ☐
2. ***Resident Agent Name and Street Address:*** *(must be a Nevada address where process may be served)*	Name **(MANDATORY)** Physical Street Address — City — Nevada — Zip Code **(OPTIONAL)** Mailing Address — City — State — Zip Code
3. ***Dissolution Date:*** *(OPTIONAL; see instructions)*	Latest date upon which the company is to dissolve (if existence is not perpetual):
4. ***Management:***	Company shall be managed by ☐ Manager(s) **OR** ☐ Members *(check only one box)*
5. ***Name and Address of each Manager or Managing Member:*** *(attach additional page if more than 3)*	Name Address — City — State — Zip Code Name Address — City — State — Zip Code Name Address — City — State — Zip Code
6. ***Name, Address and Signature of Organizer:*** *(attach additional page if more than 1)*	Name — **X** **Signature** Address — City — State — Zip Code
7. ***Certificate of Acceptance of Appointment of Resident Agent:***	I hereby accept appointment as Resident Agent for the above named limited-liability company. **X** **Authorized Signature of R.A. or On Behalf of R.A. Company** — Date

This form must be accompanied by appropriate fees.

Reset

ROSS MILLER
Secretary of State
206 North Carson Street
Carson City, Nevada 89701-4299
(775) 684 5708
Website: secretaryofstate.biz

Instructions for Limited-Liability Company Articles of Organization
(PURSUANT TO NRS 86)

IMPORTANT: READ ALL INSTRUCTIONS CAREFULLY BEFORE COMPLETING FORM.

1. *Name of the Limited-Liability Company:* The name must contain the words Limited-Liability Company, Limited Company or Limited or the abbreviations Ltd., L.L.C., LLC or LC . The word "company" may also be abbreviated. The name must be distinguishable from the name of a limited-liability company, limited partnership, limited-liability limited partnership, limited-liability partnership, business trust or corporation already on file in this office. A name may be reserved, if available, for 90 days by submitting a name reservation form with a $25.00 filing fee to the office of the Secretary of State. For details you may call (775) 684-5708, visit www.secretaryofstate.biz, or write to the Secretary of State, 206 North Carson Street, Carson City NV. 89701-4201. If it appears from the name and/or purpose of the entity being formed that it is to be regulated by the Financial Institutions Division, Insurance Division, State Board of Professional Engineers and Land Surveyors, State Board of Accountancy or Real Estate Division, the application will need to be approved by the regulating agency before it is filed with the Office of the Secretary of State.

2. *Resident Agent:* Persons wishing to file articles of organization in the State of Nevada must designate a person as a resident agent who resides or is located in this state. Every resident agent must have a street address in the state of Nevada for the service of process, and may have a separate mailing address such as a post office box, which may be different from the street address

3. *Dissolution Date:* State the latest date upon which the company is to dissolve. This provision is optional.

4. Limited-liability companies may be managed by one or more manager(s) or one or more members. Please state whether the company is managed by members or managers. If the company is to be managed by one or more managers, the name and post office or street address, either resident or business, of each manager must be set forth. If the company is to be managed by the members, the name and post office or street address, either residence or business, of each member must be set forth.

5. One or more persons may organize a limited-liability company. Indicate the names and addresses of the organizers executing the articles.

6. Resident agent must complete and sign certificate of acceptance at bottom of form or attach a separate signed certificate of acceptance.

7. On a separate 8 ½" x 11" sheet, state any other provisions which the members elect to set out in the articles of organization for the regulation of the internal affairs of the company, including any provisions which under NRS Chapter 86 are required or permitted to be set out in the operating agreement of the company.

IMPORTANT

INITIAL LIST OF MANAGERS OR MEMBERS: Pursuant to NRS 86.263, each limited-liability company organized under the laws of this state shall, on or before the last day of the first month after the filing of its articles of organization, and annually thereafter, file its list of officers, directors and resident agent. The initial list fee is $125.00. Forms will be mailed to you upon the filing of your limited-liability company and annually thereafter to the entity's resident agent.

COPIES: One file stamped copy of the articles will be returned at no additional charge. To receive a certified copy, enclose an additional $30.00 per certification. A copy fee of $2.00 per page is required for each additional copy generated when ordering 2 or more file stamped or certified copies. Appropriate instructions must accompany your order. NRS 86.241 requires that a limited liability company have at least one certified copy to be kept in the office of the resident agent. The Secretary of State keeps the original filing.

FILING FEE: $75.00 Filing fee is required. Filing may be expedited for an additional $125.00 expedite fee.

Filing may be submitted at the office of the Secretary of State or by mail at the following addresses:

Secretary of State
New Filings Division
206 N. Carson Street
Carson City, NV 89701-4299
775-684-5708 Fax 775-684-7138

(This Office Accepts Expedited Filings Only)
Secretary of State-Satellite Office
Commercial Recordings Division
555 E. Washington Avenue, Suite 4000
Las Vegas, NV 89101
702-486-2880 Fax 702-486-2888

ROSS MILLER
Secretary of State
202 North Carson Street
Carson City, Nevada 89701-4201
(775) 684 5708
Website: nvsos.gov

Customer Order Instructions

Service Requested: ☐ Regular ☐ 24-Hour Expedite (additional fee included)

SUBMIT THIS COMPLETED FORM WITH YOUR FILING

USE BLACK INK ONLY - DO NOT HIGHLIGHT

Name of Entity: ____________________ Date: __________

Return to: ____________________

Contact Name: ____________________ Phone: __________

Return Delivery (mark one): ☐ FedEx: Account # __________

☐ Hold for Pick Up ☐ Mail to Address Above ☐ Other (explain below)

Order Description (include items being ordered and fee breakdown)*:

* **PLEASE NOTE:** this office keeps the original paperwork. The first file stamped copy ordered at the time of filing is at no charge. Each additional copy is **$2.00** per page (plus **$30.00** for each certification.)

Total Amount: __________

Method of Payment:

☐ Check/Money Order ☐ eCheck/Credit Card (attach checklist) ☐ Trust Account __________

☐ Use balance remaining in job # __________

Reset

ROSS MILLER
Secretary of State
206 North Carson Street
Carson City, Nevada 89701-4299
(775) 684 5708
Website: nvsos.gov

2-Hour Expedite
Customer Order Instructions

SUBMIT THIS COMPLETED FORM WITH YOUR FILING **USE BLACK INK ONLY - DO NOT HIGHLIGHT**

Date:

2-Hour Expedite Service Requested: **$500.00** Fee Included

Return to:

Address:

Phone:

Contact Person:

Return Delivery **(mark one):** ☐ FedEx: Account #

☐ Hold for Pick Up ☐ Mail to Address Above ☐ Other

Confirmation Fax Number: Confirmation E-mail Address:

Name of Entity:

Order Description (include items being ordered and fee breakdown)*****:

*** PLEASE NOTE:** this office keeps the original paperwork. The first file stamped copy ordered at the time of filing is at no charge. *Each additional copy is **$2.00** per page (plus **$30.00** for each certification.)*

Total Amount:

Method of Payment:

☐ Check/Money Order ☐ eCheck/Credit Card (attach checklist) ☐ Trust Account

☐ Use balance remaining in job #

Reset

ROSS MILLER
Secretary of State
206 North Carson Street
Carson City, Nevada 89701-4299
(775) 684 5708
Website: nvsos.gov

1-Hour Expedite
Customer Order Instructions

SUBMIT THIS COMPLETED FORM WITH YOUR FILING

USE BLACK INK ONLY - DO NOT HIGHLIGHT

Date:

1-Hour Expedite Service Requested: **$1000.00** Fee Included

Return to:

Address:

Phone:

Contact Person:

Return Delivery (mark one): ☐ FedEx: Account #

☐ Hold for Pick Up ☐ Mail to Address Above ☐ Other (explain below)

Confirmation Fax Number:

Confirmation E-mail Address:

Name of Entity:

Order Description (include items being ordered and fee breakdown)*:

* **PLEASE NOTE:** this office keeps the original paperwork. The first file stamped copy ordered at the time of filing is at no charge. *Each additional copy is **$2.00** per page (plus **$30.00** for each certification.)*

Total Amount:

Method of Payment:

☐ Check/Money Order ☐ eCheck/Credit Card (attach checklist) ☐ Trust Account

☐ Use balance remaining in job #

Reset

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202 North Carson Street
Carson City, Nevada 89701-4201
Phone: (775) 684 5708
Website: secretaryofstate.biz

24-hour, 2-hour and 1-hour Expedite Service Guidelines

IMPORTANT: To ensure expedited service, please mark "Expedite" in a conspicuous place at the top of the service request. Please indicate method of delivery.

24-HOUR EXPEDITE SERVICE

The Secretary of State offers a 24-hour expedite service on most filings processed by this office. If you choose to utilize this service, please enclose with your filing the additional expedite fee. Please note that this expedite fee is in addition to the standard fee charged on each filing and/or order. Check the 24-hour expedite box on your customer order instruction form. If not using our order form, state clearly in your cover letter that you are requesting 24-hour expedited service, include your telephone number and return information. Attach the order form or cover sheet to the *top* of your filing and submit to this office. Each filing will be returned by U.S.P.S. regular mail unless other arrangements are made. This office *does not* fax confirmation of a 24-hour expedite.

The fee for 24-hour handling ranges from $25.00 to $125.00. Please consult our fee schedules for the appropriate 24-hour expedite fee. If you require assistance, please contact this office.

Time Constraints: Each filing submitted receives same day filing date and may be picked up within 24-hours. Filings to be mailed the next business day if received by 2:00 pm of receipt date and no later than the 2nd business day if received after 2:00 pm. Expedite period begins when filing or service request is received in this office in fileable form.

2-HOUR EXPEDITE SERVICE

The Secretary of State offers a 2-hour expedite service on most filings processed by this office. If you choose to utilize the 2-hour expedite service, please enclose with your filing an additional $500.00 per filing and/or order. Please note that this expedite fee is in addition to the standard fee charged on each filing and/or order. Complete and submit the 2-hour customer order instruction form. If not using our order form, state clearly in your cover letter that you are requesting 2-hour expedited service and include your telephone number and return information. Attach the order form or cover sheet to the *top* of your filing and submit to this office. Each filing will be returned by U.S.P.S. regular mail unless other arrangements are made.

1-HOUR EXPEDITE SERVICE

The Secretary of State offers a 1-hour expedite service on most filings processed by this office. If you choose to utilize the 1-hour expedite service, please enclose with your filing an additional $1000.00 per filing and/or order. Please note that this expedite fee is in addition to the standard fee charged on each filing and/or order. Complete and submit the 1-hour customer order instruction form. If not using our order form, state clearly in your cover letter that you are requesting 1-hour expedited service and include your telephone number and return information. Attach the order form or cover sheet to the *top* of your filing and submit to this office. Each filing will be returned by U.S.P.S. regular mail unless other arrangements are made.

1-Hour and 2-Hour Time Constraints: Each filing submitted for either 1-hour or 2-hour expedite receives same day filing date and will be acknowledged by fax or e-mail within expedite service time. Failure to indicate method of acknowledgement (fax or e-mail) or to provide a correct fax number or e-mail address may prevent the Secretary of State from acknowledging the filing of such documents. Filings may be picked up within the expedite service period. Filings to be mailed will be mailed out no later than the next business day following receipt. Expedite period begins when filing or service request is received in this office in fileable form.

The Secretary of State reserves the right to extend the expedite period in times of extreme volume, staff shortages or equipment malfunction. These extensions are few and will rarely extend more than a few hours.

ROSS MILLER
Secretary of State
202 North Carson Street
Carson City, Nevada 89701-4201
(775) 684 5708
Website: nvsos.gov

ePayment Checklist
(For Counter, Telephone, Fax and Mail Requests)

USE BLACK INK ONLY - DO NOT HIGHLIGHT

Service Type: Counter ☐ Telephone ☐ Mail ☐ Fax ☐

Order Processing Requested: **(Expedite Processing *Requires* Additional Fees)**

Regular Processing ☐ **24-HOUR** Expedite ☐ **2-HOUR** Expedite ☐ **1-HOUR** Expedite ☐

Payment by Electronic Check *(account holder name and address required below)*

Account Type;
☐ Checking
☐ Savings

Routing Number:

Account Number:

eCheck

Amount of Electronic Check: **USD $**

Payment by Card *(card holder name and billing address required below)*

Payment Type: Credit: ☐

Card Type: VISA ☐ MasterCard ☐ Discover ☐ American Express ☐

Customer Credit Card Number:

V CODE*

***** 3-digit number found on the far right of the backside of VISA, MasterCard and Discover cards
4-digit number found on the front right side of American Express card.

NOTICE: *For security and verification purposes, all credit card payments must include the 3 or 4-digit CVV2 code (V Code) number located on the credit card. Failure to include this code will result in the rejection of your filing or service request.*

Credit Card Expiration Date: Month Year

Amount to Charge Card: **USD $**

Order Information *(required)*

Entity Name/Order Reference:

Account/Card Holder Information:

Name as it Appears on the Account

Billing Address

City, State, Zip

Telephone

Payment Authorization

I authorize the Secretary of State to bill an amount not to exceed the following to be charged to the above listed account(s):

X ____________________________________

Authorized Signature

Not to Exceed Amount: **USD $**

Reset

ROSS MILLER
Secretary of State
202 North Carson Street
Carson City, Nevada 89701-4201
(775) 684 5708
Website: secretaryofstate.biz

Resident Agent Acceptance

General instructions for this form:

ABOVE SPACE IS FOR OFFICE USE ONLY

1. Please print legibly or type; Black Ink Only
2. Complete all fields. Do not highlight.
3. Ensure that document is signed in signature field.

In the matter of ______________________
(Name of business entity)

I, ______________________
(Name of resident agent)

hereby state that on __________ I accepted the appointment as resident agent
(Date)

for the above named business entity. The street address of the resident agent in this state is as follows:

(MANDATORY) Physical Street Address

Suite number

City

NEVADA

Zip Code

Optional: (address where mail will be sent)

(OPTIONAL) Additional Mailing Address

Suite number

City

State

Zip Code

Signature:

X ______________________
Authorized Signature of R.A. or On Behalf of R.A. Company

Date

Reset

ROSS MILLER
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202 North Carson Street
Carson City, Nevada 89701-4201
Phone: (775) 684 5708
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Copies and Certification Services Fee Schedule 10-1-05

The following is a list of copies and certification services and the associated fees. Fees are per document unless otherwise noted.

SERVICE REQUESTED:

Copies	$2.00 per page
Certification of Document	$30.00
Search	$50.00
Certificates:	
Certificate of Existence (evidence of good standing – short form)	$50.00
Certificate of Existence (listing amendments – long form)	$50.00
Certificate Evidencing Name Change, Certificate of Fact of Merger, Certificate of Default, Certificate of Revocation, Certificate of Dissolution, Certificate of Withdrawal, Certificate of Cancellation, Certificate of Non-Existence	$50.00
Corporate Charter	$50.00
Miscellaneous Certificates	$50.00
Apostille (Hague Treaty Nations)/Certification (Non-Hague Treaty Nations)	$20.00
Exemplification	$50.00

EXPEDITE SERVICE:

Expedite service is available for copies, certificate and certification services. Fees for expedite service are in addition to the fees as listed above.

<u>24 Hour Expedite Service:</u> Order may be picked up or mailed out within 24-hours.

Copies: (per entity name)	
1 to 10 pages	$75.00
11 or more pages	$125.00
Certificates (per entity name & and certificate type):	
1 to 10 certificates	$75.00
11 or more certificates	$125.00
Search: Expedite fee on search only; additional expedite fee required for copies	$25.00

<u>4-Hour Expedite Service:</u> Order may be picked up or mailed within 4-hours.

<u>CERTIFICATES ONLY (per entity name & certificate type):</u>

1 or more certificates	$125.00

<u>2-Hour Expedite Service:</u> Order may be picked up or mailed within 2-hours.

1 or more certificates (per entity name & and certificate type)	$500.00
1 or more copies (per entity name)	$500.00

<u>1-Hour Expedite Service:</u> Order may be picked up or mailed within 1-hour.

1 or more certificates (per entity name & and certificate type)	$1000.00
1 or more copies (per entity name)	$1000.00

BASIC INSTRUCTIONS:

1. All orders may be submitted in writing, with fees enclosed, to the above address. Telephone orders with payment by VISA, Mastercard, Discover or American Express may be called into our Customer Service Department at (775) 684-5708. Trust account and credit card customers may fax *<u>expedite orders only</u>* to (775) 684-5645. Trust account orders must be received on company letterhead.
2. All orders not specified as a pick-up are mailed out via first-class mail, unless a Federal Express number is provided or other major courier pickup arrangement is made.
3. Fax back service is *only available* on 1-hour and 2-hour expedite orders for certificates or copies of 50 pages or less. This service must be requested at time of order with complete fax information provided.
4. Each order will be returned to one address only.

ROSS MILLER
Secretary of State
202 North Carson Street
Carson City, Nevada 89701-4201
Phone: (775) 684 5708
Website: secretaryofstate.biz

Limited-Liability Company Fee Schedule Effective 10-1-05

LIMITED-LIABILITY COMPANY FEES: Pursuant to NRS 86 for both Domestic and Foreign Limited-Liability Companies.

Articles of Organization	$75.00
Registration of Foreign Limited-Liability Company	$75.00
Reinstatement Fee	$300.00
Certificate of Amendment	$175.00
Restated Articles	$175.00
Certificate of Correction	$175.00
Certificate of Termination (pursuant to NRS 86.226)	$175.00
Merger	$350.00
Termination Pursuant to NRS 92A	$350.00
Dissolution of Domestic Limited-Liability Company	$75.00
Dissolution of Foreign Limited-Liability Company	$75.00
Preclearance of any Document	$125.00
Articles of Conversion – contact office for fee information	
Articles of Domestication – contact office for fee information	
Revival of Limited-Liability Company – contact office for fee information	
24-Hour Expedite fee for above filings	**$125.00**
Change of Resident Agent/Address	$60.00
Resident Agent Name Change	$100.00
Resignation of Manager or Managing Member	$75.00
Resignation of Resident Agent (plus $1.00 for each additional entity listed)	$100.00
Name Reservation	$25.00
24-Hour Expedite fee for above filings	**$25.00**
Apostille	$20.00
Certificate of Good Standing	$50.00
Initial List of Managers or Members	$125.00
Annual or Amended List of Managers or Members	$125.00
24-Hour Expedite fee for above filings	**$75.00**
Certification of Documents – per certification	$30.00
Copies – per page	$2.00
Late Fee for List of Managers or Members	$75.00

2-Hour Expedite is available on all of the above filings at the fee of $500.00 per item.

1-Hour Expedite is available on all of the above filings at the fee of $1000.00 per item.

PLEASE NOTE: the expedite fee is in addition to the standard filing fee charged on each filing and/or order.

24-HOUR EXPEDITE TIME CONSTRAINTS:

Each filing submitted receives same day filing date and may be picked up within 24 hours. Filings to be mailed the next business day if received by 2:00 pm of receipt date and no later than the 2nd business day if received after 2:00 pm. Expedite period begins when filing or service request is received in this office in fileable form. The Secretary of State reserves the right to extend the expedite period in times of extreme volume, staff shortages, or equipment malfunction. These extensions are few and will rarely extend more than a few hours.

ROSS MILLER
Secretary of State
204 North Carson Street, Ste 1
Carson City, Nevada 89701-4299
(775) 684 5708
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Articles of Conversion

(PURSUANT TO NRS 92A.205)

Page 1

USE BLACK INK ONLY - DO NOT HIGHLIGHT **ABOVE SPACE IS FOR OFFICE USE ONLY**

Articles of Conversion
(Pursuant to NRS 92A.205)

1. Name and jurisdiction of organization of constituent entity and resulting entity:

Name of constituent entity

Jurisdiction

Entity type *

and,

Name of resulting entity

Jurisdiction

Entity type *

2. A plan of conversion has been adopted by the constituent entity in compliance with the law of the jurisdiction governing the constituent entity.

3. Location of plan of conversion: (check one)

☐ **The entire plan of conversion is attached to these articles.**

☐ **The complete executed plan of conversion is on file at the registered office or principal place of business of the resulting entity.**

☐ **The complete executed plan of conversion for the resulting domestic limited *partnership is* on file at the records office required by NRS 88.330.**

* corporation, limited partnership, limited-liability limited partnership, limited-liability company or business trust .

This form must be accompanied by appropriate fees.

ROSS MILLER
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Articles of Conversion

(PURSUANT TO NRS 92A.205)

Page 2

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ABOVE SPACE IS FOR OFFICE USE ONLY

4. Forwarding address where copies of process may be sent by the Secretary of State of Nevada (if a foreign entity is the resulting entity in the conversion):

Attn:

c/o:

5. Effective date of conversion (optional) (not to exceed 90 days after the articles are filed pursuant to NRS 92A.240) * :

6. Signatures - must be signed by:

1. If constituent entity is a Nevada entity: an officer of each Nevada corporation; all general partners of each Nevada limited partnership or limited-liability limited partnership; a manager of each Nevada limited-liability company with managers or all the members if there are no managers; a trustee of each Nevada business trust; a managing partner of a Nevada limited-liability partnership (a.k.a.; general partnership governed by NRS chapter 87).
2. If constituent entity is a foreign entity: must be signed by the constituent entity in the manner provided by the law governing it.

Name of *constituent* entity

X ________________________________

Signature	Title	Date

* Pursuant to NRS 92A.205(4) if the conversion takes effect on a later date specified in the articles of conversion pursuant to NRS 92A.240, the constituent document filed with the Secretary of State pursuant to paragraph (b) subsection 1 must state the name and the jurisdiction of the constituent entity and that the existence of the resulting entity does not begin until the later date. **This statement must be included within the resulting entity's' articles.**

Filing Fee $350.00

This form must be accompanied by appropriate fees.

Reset

ROSS MILLER
Secretary of State
204 North Carson Street, Suite 1
Carson City, Nevada 89701-4299
(775) 684 5708
Website: secretaryofstate.biz

Filing Instructions for the Amendments Division

<u>IMPORTANT: READ ALL INSTRUCTIONS CAREFULLY BEFORE COMPLETING FORM.</u>

Dear Customer: We value your patronage and desire to provide you the best service possible. In an effort to facilitate your filing we would appreciate your taking a moment to read the following before submitting your document. Failure to include any of the information required on the form may cause the filing to be rejected.

-Thank you-

1.) One file stamped copy of the filing will be returned at no additional charge. To receive a certified copy, enclose an additional $30.00 per certification. A <u>copy fee</u> of $2.00 per page is required for each additional copy generated when ordering 2 or more file stamped or certified copies. Appropriate instructions must accompany your order.

2.) If paying for expedite service, include and highlight the word <u>"EXPEDITE"</u> in your correspondence.

3.) Verify filing is submitted on the correct form prescribed by the Secretary of State.

4.) Forms must include appropriate signatures as required.

5.) If applicable, include the appropriate names and addresses as requested on the form.

6.) If adding new managers or general partners, their names and addresses must be set forth.

7.) Documents must reflect the complete name of the entity as registered with the Secretary of State.

8.) Attach all pages that are referenced as attachments.

9.) All documents must be legible for filming and/or scanning.

10.) If filing restated articles (containing newly amended articles, deletions or additions), provide a form prescribed by the Secretary of State indicating which articles have been amended, deleted or added. Furthermore, ***<u>the articles must contain the necessary amendment language as required by the statutes</u>*** governing amendments for that type of business entity.

11.) Verify that the status of the entity is not revoked. Verification may be made by visiting our Web site at www.secretaryofstate.biz or calling this office.

12.) The correct filing date must be provided when required.

13.) All required information must be completed and appropriate boxes checked or filing will be rejected.

14.) Please contact this office for assistance if you are unsure of the filing fee for your document.

All forms may be downloaded from our Web site www.secretaryofstate.biz . The Nevada Revised Statutes may be obtained at http://www.leg.state.nv.us/NRS.

Filing may be submitted at the office of the Secretary of State or by mail at the following addresses:

Secretary of State
Amendments Division
204 N. Carson Street, Suite 1
Carson City, NV 89701-4299
775-684-5708 Fax 775-684-5731

(This Office Accepts Expedited Filings Only)
Secretary of State-Satellite Office
Commercial Recordings Division
555 E. Washington Avenue, Suite 4000
Las Vegas, NV 89101
702-486-2880 Fax 702-486-2888

ROSS MILLER
Secretary of State
202 North Carson Street
Carson City, Nevada 89701-4201
(775) 684 5708
Website: nvsos.gov

Customer Order Instructions

Service Requested: ☐ Regular ☐ 24-Hour Expedite (additional fee included)

SUBMIT THIS COMPLETED FORM WITH YOUR FILING

USE BLACK INK ONLY - DO NOT HIGHLIGHT

Name of Entity: Date:

Return to:

Contact Name: Phone:

Return Delivery (mark one): ☐ FedEx: Account #

☐ Hold for Pick Up ☐ Mail to Address Above ☐ Other (explain below)

Order Description (include items being ordered and fee breakdown)*****:

* **PLEASE NOTE:** this office keeps the original paperwork. The first file stamped copy ordered at the time of filing is at no charge. Each additional copy is **$2.00** per page (plus **$30.00** for each certification.)

Total Amount:

Method of Payment:

☐ Check/Money Order ☐ eCheck/Credit Card (attach checklist) ☐ Trust Account

☐ Use balance remaining in job #

Reset

ROSS MILLER
Secretary of State
206 North Carson Street
Carson City, Nevada 89701-4299
(775) 684 5708
Website: nvsos.gov

2-Hour Expedite
Customer Order Instructions

SUBMIT THIS COMPLETED FORM WITH YOUR FILING **USE BLACK INK ONLY - DO NOT HIGHLIGHT**

Date:

2-Hour Expedite Service Requested: **$500.00** Fee Included

Return to:

Address:

Phone:

Contact Person:

Return Delivery **(mark one):** ☐ FedEx: Account #

☐ Hold for Pick Up ☐ Mail to Address Above ☐ Other

Confirmation Fax Number: Confirmation E-mail Address:

Name of Entity:

Order Description (include items being ordered and fee breakdown)*****:

* **PLEASE NOTE:** this office keeps the original paperwork. The first file stamped copy ordered at the time of filing is at no charge. *Each additional copy is **$2.00** per page (plus **$30.00** for each certification.)*

Total Amount:

Method of Payment:

☐ Check/Money Order ☐ eCheck/Credit Card (attach checklist) ☐ Trust Account

☐ Use balance remaining in job #

Reset

ROSS MILLER
Secretary of State
206 North Carson Street
Carson City, Nevada 89701-4299
(775) 684 5708
Website: nvsos.gov

1-Hour Expedite
Customer Order Instructions

SUBMIT THIS COMPLETED FORM WITH YOUR FILING | **USE BLACK INK ONLY - DO NOT HIGHLIGHT**

Date: ______

1-Hour Expedite Service Requested: **$1000.00** Fee Included

Return to: ______

Address: ______

Phone: ______

Contact Person: ______

Return Delivery (mark one)**:** ☐ FedEx: Account # ______

☐ Hold for Pick Up ☐ Mail to Address Above ☐ Other (explain below)

Confirmation Fax Number: ______ Confirmation E-mail Address: ______

Name of Entity:

Order Description (include items being ordered and fee breakdown)*:

*** PLEASE NOTE:** this office keeps the original paperwork. The first file stamped copy ordered at the time of filing is at no charge. *Each additional copy is **$2.00** per page (plus **$30.00** for each certification.)*

Total Amount: ______

Method of Payment:

☐ Check/Money Order ☐ eCheck/Credit Card (attach checklist) ☐ Trust Account ______

☐ Use balance remaining in job # ______

Reset

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24-hour, 2-hour and 1-hour Expedite Service Guidelines

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1-HOUR EXPEDITE SERVICE

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1-Hour and 2-Hour Time Constraints: Each filing submitted for either 1-hour or 2-hour expedite receives same day filing date and will be acknowledged by fax or e-mail within expedite service time. Failure to indicate method of acknowledgement (fax or e-mail) or to provide a correct fax number or e-mail address may prevent the Secretary of State from acknowledging the filing of such documents. Filings may be picked up within the expedite service period. Filings to be mailed will be mailed out no later than the next business day following receipt. Expedite period begins when filing or service request is received in this office in fileable form.

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ePayment Checklist
(For Counter, Telephone, Fax and Mail Requests)

USE BLACK INK ONLY - DO NOT HIGHLIGHT

Service Type: Counter ☐ Telephone ☐ Mail ☐ Fax ☐

Order Processing Requested: **(Expedite Processing *Requires* Additional Fees)**

Regular Processing ☐ **24-HOUR** Expedite ☐ **2-HOUR** Expedite ☐ **1-HOUR** Expedite ☐

Payment by Electronic Check *(account holder name and address required below)*

Account Type:
☐ Checking
☐ Savings

Routing Number: ____________

Account Number: ____________

eCheck

Amount of Electronic Check: USD $ ____

Payment by Card *(card holder name and billing address required below)*

Payment Type: Credit: ☐

Card Type: VISA ☐ MasterCard ☐ Discover ☐ American Express ☐

Customer Credit Card Number: ____________ V CODE*

* 3-digit number found on the far right of the backside of VISA, MasterCard and Discover cards
4-digit number found on the front right side of American Express card.

NOTICE: *For security and verification purposes, all credit card payments must include the 3 or 4-digit CVV2 code (V Code) number located on the credit card. Failure to include this code will result in the rejection of your filing or service request.*

Credit Card Expiration Date: Month ____ Year ____

Amount to Charge Card: USD $ ____

Order Information *(required)*

Entity Name/Order Reference: ____

Account/Card Holder Information:

Name as it Appears on the Account ____

Billing Address ____

City, State, Zip ____

Telephone ____

Payment Authorization

I authorize the Secretary of State to bill an amount not to exceed the following to be charged to the above listed account(s):

X ____________________

Authorized Signature

Not to Exceed Amount: USD $ ____

Reset

COMPARISON OF THE MISSISSIPPI, DELAWARE, AND REVISED UNIFORM LLC ACTS

General Provisions	**MISSISSIPPI**	**DELAWARE**	**Revised UNIFORM LLC ACT**
Definitions	§ 79-29-103	§ 18-101	§ 102
Name	§ 79-29-104 Name must be distinguishable from other entities and must be reserved with the Secretary of State.	§18-102, 103 Name must be distinguishable from other entities and must be reserved with the Secretary of State.	§ 108 Same, section for reserving names, transfer of reservation to another.
Registered Office/Agent	§ 79-29-106 (1) LLC must maintain in this state: (a) Registered office (b) Registered agent for service of process (2) LLC may change registered office/agent by filing a certificate with the appropriate information with the Secretary of State. (3) Registered agent may change its address by filing a certificate with the appropriate information with the Secretary of State. (4) Registered agent may resign by delivering certificate with appropriate information to the Secretary of State. Effective 90 days after filing.	§ 18-104 (domestic LLCs) (a) LLC shall maintain in this state: (1) Registered office (2) Registered agent for service of process (b) A registered agent may change the address of the registered office of the LLC for which it is registered agent by paying a fee and filing a certificate with the appropriate information. (c) The registered agent of one or more LLCs may resign and appoint a successor by paying a fee and filing a certificate with the Secretary of State. (d) The registered agent of one or more LLCs may resign without appointing a successor by paying a fee and filing a certificate with the Secretary of State. § 18-904 (foreign LLCs) (Same as above)	§ 113 (a) LLC shall designate and continuously maintain in this state: (1) an office, which need not be a place of its activity; and (2) an agent for service of process (b) A foreign LLC that has a certificate of authority under section 802 shall designate and continuously maintain in this state an agent for service of process. (c) An agent must be an individual who is a resident of this state or other person with authority to transact business in this state. § 114 (a) A LLC or foreign LLC may change its designated office, its agent for service of process, or the address of the agents by filing a statement of change with the appropriate information with the Secretary of State. § 115 (a) To resign as an agent for service of process, the agent must deliver to the Secretary of State for filing a statement of resignation with the appropriate information.
Service of Process on LLCs	§ 79-29-111 (1) LLC's registered agent is the LLC's agent for service of process. (2) If LLC has no registered agent or registered agent can not be found then service of process shall be upon Secretary of State's office.	§ 18-105 (domestic) (a) Service of legal process upon any domestic LLC shall be made by delivering a copy personally to any manager of the LLC, or the registered agent, or leaving it at the dwelling house of a manager or registered agent, or at the registered office or principal place of business. (b) If LLC can not be served by manner provided, it shall be lawful to serve process against the LLC upon the Secretary of State. § 18-910 (registered foreign LLCs); (same as above)	§ 116 (a) An agent appointed to a LLC is an agent of the company for service of process, notice or demand required or permitted by to be served on the company. (b) If no agent appointed or cannot find agent with reasonable diligence, the Secretary of State is an agent of the company. (c) Service may be made by delivering duplicate copies of the process, notice, or demand.

	MISSISSIPPI	DELAWARE	Revised UNIFORM LLC ACT
		§ 18-911 (unregistered foreign LLCs) (a) Any foreign LLC which shall do business in the state without having registered shall be deemed to have appointed the Secretary of State as its agent for service of process. (b) Business definition for this section (c) In the event of service upon the Secretary of State, the Secretary of State shall notify the LLC by letter, certified mail, return receipt requested, directed to the foreign LLC company at the address furnished.	
Nature of Business Permitted, Purpose & Powers	§ 79-29-108 Any lawful purpose permitted, subject to other laws. MS LLC Act does not preclude banks or insurance companies as LLCs.	§ 18-106 Any business, purpose, activity permitted, except insurance & banking.	**§§** 104,105 Capacity to sue and be sued in its own name and the power to do all things necessary or convenient to carry on its activities
Indemnification	§ 79-29-110 Indemnification may be provided for any member, manager or other person made a party to a proceeding because he is or was a member, manager or agent of the LLC against which such liability incurred.	§ 18-108 A LLC may, and shall have the power to, indemnify and hold harmless any member or manager or other person from and against any an all claims and demands whatsoever.	§ 408(a) Provides for indemnification; but: The members may agree to alter or eliminate the foregoing indemnification obligation.
Formation			
Document for Organization	§ 79-29-201: Certificate of Formation Requires at least 1 member to form LLC.	§ 18-201: Certificate of Formation Requires at least 1 member to form LLC.	§ 201: Certificate of Organization Allows “shelf” (no-member) registration for 90 days.
Amendment to Document	§ 79-29-202 (1) Certificate of formation is amended by delivering a certificate of amendment thereto to the office of the Secretary of State with appropriate information. (2) A manager or member (if no manager) who becomes aware that any statement in a certificate is false shall promptly amend the certificate. (3) Certificate of formation may be amended at any time for any proper purpose. (4) Unless otherwise provided, all	§ 18-202 (Identical to MS Act)	§ 202 Identical to MS and Delaware Act except no mention of all members agreeing on certificate of amendment.

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	members must agree on certificate of amendment.		
Execution	§ 79-29-205 (1) Unless otherwise specified, any document required by this chapter to be filed with the Secretary of States office shall be signed.	§ 18-204 (domestic) (a) Each certificate shall be executed by one or more authorized persons. (b) Unless otherwise provided, any person may sign any certificate or amendment thereof or enter into a LLC agreement or amendment thereof by an agent. (c) The execution of a certificate by an authorized person constitutes an oath or affirmation, under the penalties of perjury in the third degree. § 18-205 (a) If a person required to execute a certificate required by this subchapter fails or refuses to do so, any other person who is adversely affected by the failure or refusal may petition the Court of Chancery to direct the execution of the certificate. (b) If a person required to execute a LLC agreement or amendment thereof fails or refuses to do so any other person who is adversely affected by the failure or refusal may petition the Court of Chancery to direct the execution of the certificate. § 18-909 (foreign) Section 12-204(c) shall be applicable to foreign LLCs as if they were domestic LLCs	**§** 203 (a) A record delivered to the Secretary of State for filing pursuant to this act must be signed in a certain way pursuant to this section.
Annual Report	N/A	N/A	**§** 209 Foreign and domestic LLCs required to give annual report (same info as filing)
LLC Operating Agreement/Writing Requirement	§ 79-29-306 Operating Agreement may be oral. The LLC Agreement **may limit** or eliminate any and all **fiduciary duties** except for bad faith violations of the implied contractual covenant of good faith and fair dealing.	§ 18-101(7) Operating Agreement may be oral. The LLC Agreement **may limit** or eliminate any and all **fiduciary duties** except for bad faith violations of the implied contractual covenant of good faith and fair dealing.	**§** 110 Operating agreement may be oral. The restrictions on the operating agreement under the ULLC are much more detailed. It limits the agreements power to contract around provisions of the Act. Items the Members Cannot Vary The members cannot vary any of the following:

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	ULLC stricter on duties…		1. The capacity of an LLC to sue or be sued in its own name 2. The principle that the law of formation governs the internal affairs of the LLC, and that each member and manager is afforded limited liability 3. The power of a court to act on a petition to compel a person to file a certificate of organization 4. The power of a court to dissolve an LLC 5. The requirement that a dissolved LLC must wind up. Items Members Cannot Eliminate But May Vary The members cannot eliminate, but may vary, in a manner consistent with the RULLCA any of the following: 1. The duty of loyalty 2. The duty of care 3. Any other fiduciary duty 4. The contractual obligation of good faith and fair dealing Items Members Cannot Restrict The members cannot restrict any of the following: 1. The right to approve a merger, conversion, or domestication of the LLC to a member who would have personal liability in the resultant entity. 2. The rights of any person other than a member or manager, except the rights of a judgment creditor. Items Members Cannot Unreasonably Restrict The members cannot unreasonably restrict either of the following: 1. The right to LLC information and inspection of LLC records 2. The right of a member to maintain a derivative action.
Merger & Consolidation	§ 79-29-209 (1) Unless otherwise provided, one or more domestic LLCs may merge with a domestic or foreign entity pursuant to a plan of merger. §79-29-210 Unless otherwise provided: (a) Plan of merger must be adopted by the members.	§ 18-209 (b) Pursuant to an agreement of merger or consolidation, one or more domestic LLCs may merge or consolidate with or into one or more domestic LLCs or one or more business entities. Unless otherwise provided, the merger or consolidation must be approved by the members. (c) Upon a merger or consolidation, the	**§** 1002 (a) A LLC may merge with one or more other constituent organizations pursuant to this section, Sections 1003 through 1005 and a plan of merger, if: (1) The governing statute of each authorizes the merger. (2) The merger is not prohibited by law. (3) Each organization complies with its governing statute. (b) A plan of merger must be in a record and must

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	(b) LLC must notify each member of the meeting the plan will be submitted. (c) Approval of merger requires majority approval. (d) Separate voting by voting groups is required. §79-29-211 After approval, a certificate of merger shall be executed on behalf of each party to the merger by any manager. §79-29-212 (1) When a merger becomes effective: (a) The entity designated as the survivor continues or comes into existence. (b) Separate existence of every entity that is merged ceases. (c) All property owned and every contract possessed vests in the survivor. (d) All liabilities vest in the survivor. (e) Name of survivor may be substituted for any entity that ceased to exist b/c merger. (f) Organizational documents of a survivor are amended to the extent provided in the merger. (g) Organization documents created by merger become effective. (h) Interests in an entity this is a party to a merger that are to be converted under the plan of merger. (2) Any party to the merger that was liable before merger remains liable after merger. (3) Upon merger becoming effective, a foreign entity is deemed to: (a) Appoint the Secretary of State as its agent for service of process. (b) Agree to promptly pay the amount, if any, entitled to the members and owners.	LLC or entity surviving shall file a certificate of merger or consolidation executed by one or more authorized persons on behalf of the LLC or entity with the Secretary of State containing the appropriate information. (d) Unless a future effective date or time is provided in a certificate or merger or consolidation, in which event a merger or consolidation shall be effective at any such future effective date or time, a merger or consolidation shall be effective upon the filing in the office of the Secretary of State. (e) A certificate of merger or consolidation shall act as a certificate of cancellation for a domestic LLC which is not the surviving or resulting entity in the merger or consolidation. (f) An agreement of merger or consolidation approved in accordance with subsection (b) of this section may: (1) Effect any amendment to the LLC agreement. (2) Effect the adoption of a new LLC agreement. (g) When a merger becomes effective all rights, privileges, powers, property, debts, causes of action, and etc. shall vest in the surviving or resulting LLC or entity. (h) A LLC agreement may provide that a domestic LLC shall not have the power to merge or consolidate as set forth in this section.	include the appropriate information.

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Conversion/Domestication	N/A NEED! DE is good model, allows for easy conversion.	§ 18-214 (Other types of entities may convert to an LLC by complying with this section & filing);	**§** 1006 (a) An organization other than a LLC or foreign LLC may convert to a LLC, and a LLC may convert to an organization other an a foreign LLC pursuant to this section, Section 1007 through 1009, and a plan of conversion, if: (1) The governing statute of each authorizes the conversion. (2) The conversion is not prohibited by law. (3) Each organization complies with its governing statute. (b) A plan of conversion must be in a record and contain the appropriate information.
	MS does not address	§ 18-216 (An LLC may convert to another type of entity by complying with this section & filing); § 18-212 (A non-U.S. entity may become domesticated as a Delaware LLC by complying with this section & filing).	ULLC allows conversion to LLC (by organization other than LLC or foreign LLC). The 2006 revision also allows for conversion of existing LLC to other entity (but not foreign LLC). Requires a plan of conversion. (**§** 1006(b)). Plan of conversion must be consented to by all members. ULLC does not address conversion of non-US entities into LLCs.
Contractual Appraisal Rights	§ 79-29-214 Default to statute if operating agreement does not grant. Notice required to beneficial holders if entity concludes they will be required, then beneficial holders must notice LLC with intent to exercise.	§ 18-210 The LLC Agreement may grant appraisal rights to its members.	N/A Must be addressed in operating agreement.
Series LLCs	N/A	§ 18-215 Series LLCs are permitted. Illinois, Iowa, Nevada, Oklahoma, Tennessee, and Utah are other states that have series provisions.	N/A The primary reason the drafters rejected the series concept is that it raises questions as to how a series will be treated under other laws. Since very few states have enacted series provisions, there is a substantial question as to how a series LLC will be treated in a state whose LLC statute does not contain a series provision. It is well settled that the internal affairs of any business entity, including an LLC, are governed by the laws under which the entity is formed. As long as the creation of series is deemed to be a matter of internal affairs, a court in a non-series LLC state should apply the law of series LLCs in effect in the state of formation, including the limited liability protection. If,

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			however, the court considers the LLC to be subject to the doctrine of limited liability that is in effect in the law of the forum state, then the court could find that the limited liability afforded to a series under the law of the state of formation does not apply in the forum state.
Members & Managers			
Access to and Confidentiality of Information; Records	§ 79-29-308 -requires some records to be kept in medium that can easily be provided (§ 107) Any books and records of the LLC are subject to inspection and copying for any proper purpose by any *member* or their agent. (MS does not explicitly say "managers;" just "members").	§ 18-305(c) DE provides access explicitly for both members and managers. A manager may keep LLC information confidential from members if the manager has a good faith belief that such is in the LLC's best interests.	§ 410 Does not require that any records be kept, but ensures members rights to inspect any records. -In manager-managed, the informational rights of § 410 apply only to managers and not members.
Agency Powers of Members and Managers	§ 79-29-303 Every member is an agent of the LLC. However, if the management of the LLC is vested in a manager or managers, then every manager is an agent of the LLC, and no member, acting solely in the capacity as member, is an agent of the LLC.	§ 18-402 Unless otherwise provided in the LLC Agreement, each member and manager is an agent of the LLC and has authority to bind the LLC.	§ 301 -Member is not agent of manager-managed LLC solely by being a member. -a person's status as a member does not prevent or restrict law other than this act from imposing liability on a limited liability company because of the member's conduct.
Fiduciary Duties if Member-Managed	N/A	§ 18-1101(c)-(e) The LLC Agreement **may limit** or eliminate any and all **fiduciary duties** except for bad faith violations of the implied contractual covenant of good faith and fair dealing.	§409 Members owe the LLC **and each other** a duty of loyalty and a duty of care. The LLC Agreement **may modify** the list of duties under this section, but **it may not** : (1) unreasonably restrict the right to information or access to records; (2) eliminate the duty of loyalty (but it may identify types of categories or activities that do not violate this duty); (3) unreasonably reduce the duty of care; or (4) eliminate the duty of good faith and fair dealing.

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			A member who is not also a manager in a manager-managed LLC only has the duty to refrain from disclosing or using information obtained from the articles of organization to the detriment of the LLC or other members.
Fiduciary Duties if Manager-Managed	§ 79-29-402 (limited to standards of conduct for mgr. "good faith, ordinarily prudent mgr" standard. Very limited like DE-dependent on agreement.	§ 18-1101(c)-(e) Dependent on operating agreement.	§409(h) Same duties imposed on managers. A manager in a manager-managed LLC is held to the same standards of conduct as a member in a member-managed LLC
Business Transactions of Members/Managers with the LLC	§ 79-29-109. Limited only by the agreement.	§ 18-107 May act as non-member except where bound by the agreement.	§ 409 Limited to the duties of loyalty and care as outlined in the section.
Liability of Members to Third Parties	§ 79-29-305 (1) A person who is a member of the LLC is not liable, by reason of being a member, for any act by another member, manager, agent or employee. (2) A member is not a proper party to a proceeding by or against a LLC except: (a) Where the object of the proceeding is to enforce a member's rights against the LLC. (b) In a derivative action pursuant to Article 11. (c) When it is agreed upon in an LLC agreement or other type of agreement.	§ 18-303 (a) Except as provided otherwise, the debts, obligations, and liabilities of a LLC shall be solely the responsibility of the LLC, and no member or manager shall be held personally liable. (b) Under a LLC agreement or another agreement, a member or manager may agree to be held liable.	§ 304 (a) The debts and obligations, or other liabilities of the LLC, whether arising in contract, tort, or otherwise: (1) are solely the debts, obligations, or other liabilities of the company; and (2) do not become the debts, obligations, or other liabilities of a member or manager solely by reason of the member acting as a member or manager acting as a manager. (b) The failure of a LLC to observe any particular formalities relating to the exercise of its powers or management of its activities is not a ground for imposing liability on the members or managers for the debts, obligations, or other liabilities of the company.
Reliance on Reports and Information	§ 79-29-402(2). Managers entitled to rely on info…members not included explicitly	§ 18-406 Members and managers will be protected if they act in reasonable, good faith reliance upon reports and information.	N/A
Management of the LLC	§ 79-29-401 (1) Certificate of formation of a LLC may delegate responsibility for managing an LLC to the extent it provides. (2) Managers need not me residents of the state or members of the LLC unless	§ 18-402 Unless otherwise provided, management of a LLC shall be vested in its members in proportion to the then current percentage or other interest of members in the profits of the LLC.	§ 407 The agreement under the ULLC also determines whether the LLC is member-managed or manager-managed and has default to member-managed if unspecified, and It allows for certificates of authority to be filed to provide notice that only certain members/managers of the LLC are

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	otherwise specified. (3) Number of managers shall be fixed by or in the manner provided for in the certificate of formation or LLC agreement. (4) Unless otherwise provided, managers will be elected by the members. (5) Unless otherwise provided, any vacancy in a manager's position will be filled by a vote of the members. (6) All managers may be removed in the manner provided for in the certificate of formation or LLC agreement. (7) Unless otherwise provided, any action required or permitted to be taken by the managers of a LLC may be taken upon majority vote of the members.	§18-403 A manager may make contributions to the LLC and share in the profits and losses of, and in distributions from the LLC as a member. §18-404 (a) LLC agreement may provide for classes or groups of managers having such relative rights as the LLC agreement provides. (b) A LLC agreement may grant to all or certain identified managers or a specified class or group of the managers the right to vote on any matter. (c) A LLC agreement may set forth provisions relating to notice of the time, place, or purpose of any meeting. (d) Unless otherwise provided, meetings of managers may be held by means of conference telephone or other communication equipment. §18-405 (a) A manager who fails to perform in accordance with the LLC agreement shall be subject to specified penalties or specified consequences. (b) At the time or upon the happening of specified events in the LLC agreement, a manager shall be subject to specified penalties or consequences. §18-406 A member, manager or liquidating trustee of a LLC shall be fully protected in relying in good faith upon the records of the LLC. §18-407 Unless otherwise provided, a member or manager has the power and authority to delegate one or more other persons the member's or manager's right and powers to manage and control the LLC.	entitled to do business on LLC's behalf.
Delegation of Rights & Powers to Manage	79-29-401 (1) Certificate of formation of a LLC may	§ 18-407 See above.	§ 407 (b)(2) In a member-managed LLC, the following rules

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	delegate responsibility for managing an LLC to the extent it provides		apply: (1) The management and conduct of the company are vested in the members. (2) Each member has equal rights in the management and conduct of the company's activities. (3) Differences may be decided by a majority of votes. (4) Act outside ordinary course of business may be undertaken only by consent of all members. (5) The operating agreement may only be amended with consent of all members. (c) In a manager-managed LLC, the following rules apply: (1) Any matter relating to the activities of the company is decided exclusively by the managers. (2) Each manager has equal rights. (3) A difference maybe decided by majority of the managers. (4) Consent of all managers is required for certain acts. (5) Manager may be chose at any time by majority of managers. (6) Person need not be a member to be a manager. (7) Person ceasing to be manager does not discharge debt, obligation, or other liability which the person incurred as a manager. (d) Action requiring consent may be taken with out meeting. (e) The dissolution of a LLC does not affect the applicability of this section. (f) This act does not entitle a member to remuneration for services performed.
Classes & Voting	§ 79-29-304 If not provided for in the articles of organization, operating agreement, MS provides default provision of 1 vote per member on each voting matter.	§ 18-302 (members); § 18-404 (managers) Must be provided for in the operating agreement.	N/A. There are no default provisions in ULLC. Voting will either be addressed in agreement or not at all.
Notice & Meetings	§ 79-29-305. certificate of formation or agreement provides notice requirements.	§ 18-302 (c) A LLC agreement may set forth provisions relating to notice of the time, place, or purpose of any meeting at which any matter is to be voted on by members. (d) Unless otherwise provided, meetings may be held by means of conference	N/A Operating agreement

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		telephone or other communications equipment. § 18-404 (See above in Management of LLC)	
Contested Matters Relating to Managers; Contested Votes	N/A	§ 18-110 (a) Upon application, the Court of Chancery may hear and determine the validity of any admission, election, appointment, removal, or resignation of a manager, and the right of any person to become or continue to be a manager. (b) Upon application, the Court of Chancery may hear and determine the result of any vote of member or managers upon matters as to which the members or managers have the right to vote on pursuant to the LLC agreement. (c) This section is an extension of and not a limitation upon the right otherwise existing of service of legal process upon nonresidents.	N/A
Admission of Additional Members	§ 79-29-301 (2) After filing by the Secretary of State, a person may be admitted as a member: (a) In the case of a person acquiring a LLC interest directly from the LLC, upon the compliance with the certificate of formation or the LLC agreement. (b) In the case of an assignee of a LLC interest, upon the compliance of subsection (1) of 79-29-304.	§ 18-301 (b) After formation, a person is admitted as a member: (1) If a person is not an assignee upon the consent of all members and the members admission is reflected in the records. (2) If the person is an assignee, at the time provided and in compliance with the LLC agreement. If the LLC agreement does not provide a time then when it is reflected in the records. (3) A person being admitted as a member of a surviving or resulting LLC, as provided in the LLC agreement or merger/consolidation agreement.	§ 401(d) Person who becomes new member is deemed to have assented to the operating agreement
Remedies for Breach of LLC Agreement by Member	N/A	§ 18-306. DE only authorizes that the agreement may control remedies (akin to liquidated damages?) Penalties, consequences may be specified in agreement.	N/A
Remedies for Breach of	N/A	§ 18-405	N/A

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LLC Agreement by Manager		Likewise, penalties and consequences may be specified in agreement.	
Removal/Withdrawal	§ 79-29-307. Agreement provides, but MS has default § 79-29-307(3). If operating agreement does not preclude appraisal rights, then members have appraisal rights.	§ 18-304 A person ceases to be a member of a LLC upon the happening of any of the events in this section. (1) Unless otherwise provided, or with written consent of all members, a member: (a) Makes an assignment for the benefit of creditors. (b) Files a voluntary petition in bankruptcy. (c) Is adjudged a bankrupt or insolvent. (d) Files a petition or answer seeking reorganization, etc. (e) Files an answer or other pleading admitting or not contesting the material allegations pleaded against the member. (f) Seeks, consents to or acquiesces in the appointment of a trustee, receiver, or liquidator of the member.	§ 601 (a) A person has the power to dissociate as a member at any time, rightfully or wrongfully, by withdrawing as a member by express will under § 602(1).
Contributions, Distributions, & Resignation			
Form of Contribution	§ 79-29-501 May be in cash, property, services rendered, or a promissory note or other obligation to contribute cash or property or to perform services.	§ 18-501 The contribution may be in cash, property, or service rendered, or a promissory note or other obligation to contribute the cash or property or to perform services.	§ 402 The contribution may consist of tangible or intangible property or other benefit to a LLC, including money, services performed, promissory notes, other agreements to contribute money or property, and contracts for service to be performed.
Liability for Contribution	§ 79-29-502 (1) Only enforceable if set out in a writing signed by the member. (2) Obligated to the LLC to perform an enforceable promise to contribute case or property or to perform services, even if he is unable to perform due to death, disability, or any other reason.	§ 18-502 (a) Except as provided under a LLC agreement, a member is obligated to a LLC to perform any promise to contribute cash or property or to perform services, even if the member is unable to perform because of death, disability, or any reason.	§ 403 (a) A person's obligation to make a contribution to a LLC is not excused by a person's death, disability, or other inability to perform personally if a person does not make a required contribution. The person's estate is obligated to contribute money equal to the value of the part of the contribution, at the option of the company. (b) A creditor of a LLC which extends credit or otherwise

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	(3) Obligation of a member to make a contribution or return money or other property paid or distributed in violation of the chapter may be compromised only by specific consent of all members. (4) Certificate of formation or LLC agreement may provide that the interest of any member who fails to meet his obligations shall be subject to specified penalties.	(b) Unless otherwise provided, the obligation of a member to make a contribution or return money or other property paid or distributed in violation of this chapter may be compromised only by consent of all the members. (c) A LLC agreement may provide that the interest of any member who fails to make any contribution that the member is obligate to make shall be subject to specified penalties of such failure.	acts in reliance on an obligation described in subsection may enforce the obligation.
Allocation of Profits & Losses	§ 79-29-503 The profits and losses of a LLC shall be allocated among the members, and among classes of members, in the manner provide by the certificate of formation or LLC agreement.	§ 18-503 (Identical to MS Act)	N/A
Allocation of Distributions	§ 79-29-504 Distribution of cash or other assets must be allocated in the manner provided for in the certificate of formation or the LLC agreement.	§ 18-504 (Identical to MS Act)	§ 404 (a) Any distributions made by a LLC before its dissolution and winding up must be in equal shares among members and dissociated members. (b) A person has a right to a distribution before the dissolution and winding up of a LLC only if the company decides to make an interim distribution. (c) A person does not have a right to demand or receive a distribution from a LLC in any form other than money. (d) If a member or transferee becomes entitled to receive a distribution, the member or transferee has the status of, and is entitle to all remedies available to, a creditor of the LLC with respect to the distribution.
Interim Distributions	§ 79-29-601 Member is entitled to receive distributions from a LLC before his dissociation and before dissolution to the extent and at the times or upon the occurrence of the events specified in the certificate of formation or LLC agreement.	§ 18-601 Except as otherwise provided, a member is entitled to receive from a LLC distributions before the member's resignation form the LLC and before the dissolution and winding up thereof.	N/A
Distribution in Kind	§ 79-29-603 Except as provided in the certificate of formation or LLC agreement, a member, has no right to demand any distribution	§ 18-605 (Identical to MS Act)	N/A

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	form a LLC in any form other than cash.		
Limitations on Distribution	§ 79-29-605 (1) No distribution may be made if, after giving effect to the distribution: (a) LLC would not be able to pay its debts due in the usual course of business. (b) LLC total assets would be less than the sum of its total liabilities plus the amount that would be needed if the LLC were to be dissolved at time of distribution. (2) LLC may base a determination that a distribution is not prohibited under subsection (1) of this section either on: (a) Financial statements prepared under reasonable accounting practices. (b) Fair valuation that is reasonable. (3) The effect of distribution is measured as of: (a) The date the distribution is authorized if payment occurs 120 days after date of authorization. (b) The date of payment is made if it occurs more than 120 days after the date of authorization. (4) If terms of any indebtedness of the LLC provide that any payment thereon is to be made only if, and to the extent that, payment of a distribution to members could then be made under this section, such indebtedness of a LLC, and any indebtedness issued as a distribution, is not a liability for purposes of distributions made under this section.	§ 18-607 (a) A LLC shall not make a distribution to a member to the extent that at the time of the distribution, after giving effect to the distribution, all liabilities of the LLC, other than the liabilities to members on account of their LLC interests and liabilities for which the recourse of creditors is limited to specified property of the LLC, exceed the fair value of the assets of the LLC, except that the fair value of property that is subject to a liability for which the recourse of creditors is limited shall be included in the assets of the LLC only to the extent that the fair value of that property exceeds the liability. (b) A member who receives a distribution in violation of subsection (a) and knew of the violation shall be liable to a LLC for the amount of the distribution. (c) Unless otherwise agreed, a member who receives a distribution from a LLC shall have no liability under this chapter or other applicable law for the amount of the distribution after the expiration of three years from the date of distribution unless an action to recover the distribution from such member is commenced prior to the expiration and an adjudication of liability against such member is made in said action.	§ 405 (a) A LLC may not make a distribution if after the distribution: (1) The company would not be able to pay its debts. (2) The company's total assets would be less than the sum of its total liabilities plus the amount that would be needed, if the company were to be dissolved or wound up, to satisfy the preferential rights upon dissolution, winding up, and termination of members whose preferential rights are superior to those of persons receiving under the circumstances. (b) A LLC may base a determination that a distribution is not prohibited under subsection (a) on financial statements prepared on the basis of accounting practices that are reasonable. (c) Distribution is measured pursuant to this section. (d) A LLC indebtedness to a member incurred by reason of a distribution made in accordance with this section is at parity with the company's indebtedness to its general, unsecured creditors. (e) A LLC indebtedness is not a liability for purposes of subsection (a) if the terms of the indebtedness provide that payment of principal and interest are made only to the extent that a distribution could be made to members under this section. (f) If indebtedness is issued as a distribution, each payment of principal or interest on the indebtedness is treated as a distribution, the effect of which is measure on the date the payment is made.
Resignation & Withdrawal	§ 79-29-307 (3) Unless provided against, the member may withdraw from a LLC by giving 30 days written notice to the other members, or such notice as provided for in the certificate of formation or LLC agreement.	§ 18-602 A manager may resign as a manager at the time or upon the happening of events specified in the LLC agreement. § 18-603 A member may resign from a LLC only at the time or upon the happening of	§ 601 (a) A person has the power to dissociate as a member at any time, rightfully or wrongfully, by withdrawing as a member by express will under § 602(1).

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		events specified in the LLC agreement. § 18-604 Except as otherwise provided, upon resignation of any resigning member is entitled to receive any distribution to which such member is entitled under the LLC agreement.	
Transfer of Membership Interests			
Nature of LLC Interest	§ 79-29-701 LLC is personal property. A member has no interest in specific LLC property.	§ 18-701 Same as MS	§ 501 A transferable interest is personal property.
Assignment of LLC Interest	§ 79-29-702 A member who assigns all of the member's interest in the LLC ceases to be a member upon assignment. The granting of a security interest, lien or other encumbrance will not cause the member to cease to be a member.	§ 18-702 A member who assigns all of the member's interest in the LLC ceases to be a member upon assignment. The granting of a security interest, lien or other encumbrance will not cause the member to cease to be a member.	§ 502 ULLC broader, “transfers” instead of specifically “assignments.” Language is similar to assignment sections of MS, DE
Right of Assignee to Become a Member	§ 79-29-704 Assignee “may” become member if agreement provides and all other member’s consent.	§ 18-704 (Identical to MS Act)	§ 502 (g) Except as otherwise provided in § 602(4)(B), when a member transfers a transferable interest, the transferor retains the rights of a member other than the interest in distributions transferred and retains all duties and obligations of a member.
Member's Interest Subject to Charging Order	§ 79-29-703 (Creditor’s Rights) Court may charge the LLC interest of the member with payment of the unsatisfied amount of the judgment, with interest. The judgment creditor has only the rights of an assignee of the LLC interest.	§ 18-703 (Identical to MS Act)	§ 503 Rights of Creditor A proper charging order requires the LLC to pay the judgment creditor any distribution that would otherwise be payable to the member. The charging order acts essentially in the same manner as does a garnishment. Neither a judgment creditor nor a receiver appointed to administer the assets of a member acquires any right to manage or govern the LLC.
Powers of Estate of Deceased or Incompetent Member	§ 79-29-705 If a member dies or is judged to be incompetent, the member’s executor administrator, guardian, conservator, or other legal representative may exercise all of the member’s rights.	§ 18-705 If a member dies or is judged to be incompetent, the member’s personal representative may exercise all of the member’s rights.	§ 602 A person is dissociated as a member of the LLC when: (6) In the case of a person who is an individual: (A) the person dies; or (B) in a member-managed LLC: (i) a guardian or general conservator for the person is

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			appointed; or (ii) there is a judicial order that the person has otherwise become incapable of performing the person's duties as a member under the operating agreement.
Dissolution			
Events Triggering Dissolution	§ 79-29-801 A LLC is dissolved upon the first of the following to occur: (a) At the time specified in the certificate of formation. (b) Upon the occurrence of the event specified in the certificate of formation or LLC agreement. (c) Upon consent of the members. (d) Upon an event of dissociation of a member, if a majority of the remaining members consent to do so. (e) Upon the entry of a decree of judicial dissolution.	§ 18-801 (Identical to MS Act)	§ 701 A LLC is dissolved upon the first of the following to occur: (1) An event or circumstances that the operating agreement states causes dissolution. (2) The consent of all members. (3) The passage of 90 consecutive days during which the company has no members; (4) On application by a member, the entry by an appropriate court of an order dissolving the company. (5) On application by a member, the entry by an appropriate court of an order dissolving the company on the grounds that the managers or those member in control of the company: (A) have acted, are acting. Or will act in a manner that is illegal or fraudulent. (B) have acted in a manner that is oppressive and was, is, or will be directly harmful to the applicant.
Dissociation Not Triggering Dissolution	N/A	§ 18-801(b) A member is admitted to the LLC in the manner provided in the LLC agreement, effective as of the occurrence of the event that terminated the continued membership of the last member.	N/A
Judicial Dissolution	§ 79-29-802 The chancery court in the county where the regular office of the LLC is located is the proper court in which to apply for judicial dissolution.	§ 18-802 The Court of Chancery is the proper court in which to apply for judicial dissolution.	§ 701 See above
Administrative Dissolution	N/A	N/A	§705 Secretary of State may commence proceeding to dissolve LLC administratively if LLC does not:

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			-pay fees, taxes, penalties imposed by Act or other law within 60 days; or -deliver the required annual report
Winding Up	§ 79-29-803 (1) Unless otherwise provided, the manager or managers, or, if management of the LLC is not vest in a manager or managers, the member who have not wrongfully dissolved a LLC, may wind up the LLC company's affairs. (2) Upon dissolution of the LLC and until the filing of a certificate of cancellation, the persons winding up the LLC's affairs may prosecute and defends suits. (3) Unless otherwise provided, the persons winding up the LLC's affairs are entitled to reasonable compensation.	§ 18-803 (a) Unless otherwise provided, a manger that has not wrongfully dissolved a LLC, the members or a person approved by the members , or by each class or group of members may wind up the LLC's affairs. (b) Upon dissolution of a LLC and until the filing of a certificate of cancellation, the persons winding up the LLC's affairs may prosecute and defend suits.	§ 702 (a) A dissolved LLC shall wind up its activities, and the company continues after dissolution only for the purpose of winding up.
Distribution of Assets	§ 79-29-805 Upon winding up of the LLC, the assets must be distributed as follows: (a) To creditors in satisfaction of liabilities of the LLC. (b) Except as provided by the certificate of formation and the LLC agreement, to members and former members in satisfaction of liabilities. (c) Except as provided by the certificate of formation and the LLC agreement, to member first for the return of their contributions and secondly respecting their LLC interests, in the proportions in which the members share in distribution.	§ 18-804 (Identical to MS Act)	§ 702 (b) In winding up its activities, a LLC: (1) Shall discharge the company's debts, obligations, or other liabilities, settle and close the company's activities, and marshal and distribute the assets of the company.
Filing	§ 79-29-204 Following dissolution, articles of dissolution filed with the SOS commences winding up.	§ 18-203 Following dissolution, a certificate of cancellation must be filed in the office of the Secretary of State.	§ 702(b)(2)(F) Articles of termination filed with Secretary of State.
Known Claims against the LLC	§ 79-29-806 The dissolved LLC must give written notice to its known claimants after the filing of the articles of dissolution.	§ 18-804(b)(1)-(2) The LLC must make reasonable provision for known claims, but there is no written notice requirement.	§ 703 Notice to known claimants required to be in writing. Detailed procedure- does not include contingent liabilities.

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Unknown Claims against the LLC	§ 79-29-807 If a dissolved LLC publishes notice of its dissolution in accordance with this section, claims against the dissolved LLC will be barred unless brought within 5 years after the publication of notice. (Some states say 2 years)	§ 18-804(b)(3) The LLC must make such provision as will be reasonably likely to be sufficient for unknown claims that are likely to arise or become known within 10 years after dissolution.	§ 704 If a dissolved LLC publishes notice of its dissolution in accordance with this section, claims against the dissolved LLC will be barred unless brought within 5 years after the publication of notice.
Trustees/Receivers for LLCs	§ 79-29-803 (1) Unless otherwise provided, the manager or managers, or, if management of the LLC is not vest in a manager or managers, the member who have not wrongfully dissolved a LLC, may wind up the LLC company's affairs.	§ 18-805 When the certificate of formation on any LLC formed under this chapter shall be cancelled by the filing of a certificate of cancellation, the Court of Chancery , on application of any creditor, member or manager, or any other person who shows good cause, may either appoint one or more persons to be receivers, to take charge of the LLC's property, and to collect the debts and property due to the LLC.	§ 602 (8) In the case of a person that is a trust or is acting as a member by virtue of being a trustee of a trust, the trust's entire transferable interest in the company is distributed.
Revocation of Dissolution	N/A	§ 18-806 LLC shall not be dissolved and its affairs not wound up if, prior to the filing of a certificate of cancellation in the office of the Secretary of State. The LLC is continued effective as of the occurrence of such event.	§ 706 (a) A LLC that has been administratively dissolved may apply to the Secretary of State for reinstatement within two years after the effective date of dissolution.
Foreign LLCs			
Law Governing	§ 79-29-1001 Subject to the Constitution of this state, the laws of the state or other jurisdiction under which a foreign LLC is organized govern its organization and internal affairs and the liability of its members, and a foreign LLC may not be denied registration by reason of any of any difference between those laws and the	§ 18-901 (Identical to MS Act)	§ 801 (a) The law of the state or other jurisdiction under which a foreign LLC is formed governs: (1) the internal affairs of the company; and (2) the liability of a member as a member and a manager as a manager for the debts, obligations, or other liabilities. (b) A foreign LLC may not be denied a certificate of authority by reason of any difference between the laws of the jurisdiction under which the company is formed and

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	laws of this state.		the law of this state. (c) A certificate of authority does not authorize a foreign LLC to engage in any business that a LLC may not engage in.
Registration	§ 79-29-1002 (1) Before transacting business in the state, a foreign LLC shall register with the Secretary of State. A foreign LLC shall file one original application signed with the appropriate information. (2) A foreign LLC properly registers with the Secretary of State before July 1, 1994 shall not be required to submit a new application.	§ 18-902 Before doing business in the state, a foreign LLC shall register with the Secretary of State. A foreign LLC shall submit: (1) A copy executed by an authorized person of an application for registration with the appropriate information. (2) A fee as set forth.	§ 802 (a) A foreign LLC may apply for a certificate of authority to transact business in this state by delivering an application to the Secretary of State for filing. (b) A foreign LLC shall deliver with a completed application a certificate of existence or a record of similar import signed by the Secretary of State or other official having custody of the company's filed records.
Issuance of Registration	§ 79-29-1003 If the Secretary of State finds that an application meets the requirements and all the fees paid, he shall: (a) Endorse on the original the word "Filed" with the month, day, and year. (b) File in his office the original (c) Return a copy to the filer.	§ 18-903 (Identical to MS Act)	§ 208 (like domestic; not covered specifically regarding foreign) (a) The Secretary of State, upon request and payment of fee, shall furnish to any person a certificate of existence for a LLC if the records filed show the company has been formed under § 2-1 and the Secretary of State has not filed a statement of termination.
Name	§ 79-29-1004 May register under any name, provided the name is a name that could be adopted by a domestic LLC.	§ 18-904 Name must be distinguishable from other entities and must be reserved with the Secretary of State; the name must be one that could be registered by a domestic LLC.	Name, like registration not covered specifically as to foreign entities, default must be domestic treatment.
Amendments	§ 79-29-1005 If any statement in the application for registration was false when made or any arrangements or other facts described have changed, the foreign LLC shall promptly deliver to the Secretary of State for the filing of a certificate, signed and acknowledged by a person authorized to do so, correcting such statement, together with a fee.	§ 18-905 (Identical to MS Act)	Same as domestic?
Cancellation of Registration	§ 79-29-1006 (1) A foreign LLC registered under this	§ 18-906 A foreign LLC may cancel its registration	§ 806 (a) A certificate of authority of a foreign LLC to transact

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	chapter shall cancel its registration upon completion of the winding up process. (2) A foreign LLC may cancel it registration whenever it ceases transacting business in this state. (3) Registration is cancelled by delivering a certificate of cancellation along with a fee to the Secretary of State. (4) A cancellation revokes the authority of the registered agent for service of process and acts as consent for the Secretary of State to accept service of process on behalf of the LLC.	by filing with the Secretary of State a certificate of cancellation together with a fee. A cancellation does not terminate the authority of the Secretary of State to accept service of process on the foreign LLC with respect to causes of action arising out of the doing business in the state of Delaware.	business in this state may be revoked by the Secretary of State in the manner provided in subsections (b) and (c) if the company does not meet certain requirements. (b) To revoke a certificate of authority, the Secretary of State must prepare, sign, and file a notice of revocation and send a copy to the company's agent for service of process. (c) The authority to transact business ceases on the effective date of the notice of revocation.
Action by Attorney General	§ 79-29-1009 The Attorney General may bring an action to restrain a foreign LLC from transacting business in this state in violation of this article.	§ 18-908 The Court of Chancery shall have jurisdiction to enjoin any foreign LLC from doing any business in the State of Delaware if such foreign LLC has failed to register or if the LLC has secured a certificate under false or misleading representations.	§ 809 The Attorney General may maintain an action to enjoin a foreign LLC from transacting business in this state in violation of this article.
Doing Business without Registration	§ 79-29-1007 A foreign LLC doing business in the state may not maintain any action, suit, or proceeding in any court of this state until it has registered in this state.	§ 18-907 A foreign LLC doing business in the state may not maintain any action, suit, or proceeding in the state until it has registered and has paid to this state all fees and penalties for the time during which it did business before registering.	§ 808 May not maintain any action, suit or proceeding unless it has a certificate of authority to transact business in the state.
Derivative Actions	§ 79-29-1101 through 1104 Proper plaintiff, requirement of demand before proceedings, stay of proceedings, dismissal… (no Right of action detailed as in other two statutes.)	§ 18-1001 through 1004 Right of action, Proper plaintiff, complaint and expenses.	§§ 902-906 Right of action, proper plaintiff, pleadings and expenses. Includes provision for a Special Litigation Committee for member-managed LLC disputes and manager-managed LLC disputes.
Activities Not Constituting Doing Business	§ 79-29-1008 (1) Following activities do not constitute transacting business: (a) Maintaining, defending, or settling any proceeding; (b) Holding meeting of it members or carrying on any other activities concerning internal affairs; (c) Maintaining bank accounts; (d) Maintaining office or agencies for	§ 18-912 (a)) Following activities do not constitute transacting business: (1) Maintaining, defending, or settling any proceeding; (2) Holding meeting of it members or carrying on any other activities concerning internal affairs; (3) Maintaining bank accounts; (4) Maintaining office or agencies for	§ 803 (a) Activities of a foreign LLC which do not constitute transacting business in this state within the meaning of this article include: (1) Maintaining, defending, or settling any proceeding; (2) Holding meeting of it members or carrying on any other activities concerning internal affairs; (3) Maintaining bank accounts;

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	the transfer, exchange, and registration of the company's own securities or interests; (e) Selling through independent contractors; (f) Soliciting or obtaining orders if the orders require acceptance outside this state before they become contracts; (g) Creating or acquiring indebtedness, mortgages, and security interests in real or personal property; (h) Securing or collecting debts or enforcing mortgages and security interests in property securing the debts; (i) Owning, without more, real or personal property; (j) Conducting an isolated transaction that is completed within thirty days and that is not one in the course of repeated transaction of a lie nature; or (k) Transacting business in interstate commerce. (2) Foreign LLC shall not be considered transacting business solely because it: (a) Owns a controlling interest in a corporation or a foreign corporation that transacts business in this state; (b) Is a limited partner of a LP or foreign LP that is transacting business in this state; or (c) Is a member or manager of a LLC that is transacting business in this state.	the transfer, exchange, and registration of the company's own securities or interests; (5) Selling through independent contractors; (6) Soliciting or obtaining orders if the orders require acceptance outside this state before they become contracts; (7) Selling and agreeing to deliver into the State, machinery, plants, or equipment, the construction, erection or installation of which within the state requires the supervision of technical engineers or skilled employees, and as a part of the contract of sale agreeing to furnish such services to the vendee at the time of construction; (8) Creating or acquiring indebtedness, mortgages, and security interests in real or personal property; (9) Securing or collecting debts or enforcing mortgages and security interests in property securing the debts; (10) Conducting an isolated transaction that is not one in the course of repeated transaction; (11) Doing business in interstate commerce; or (12) Doing business as an insurance company. (b) Person shall not be deemed to be doing business in the state solely by reason of being a member or manager of a LLC. (c) This section does not apply in determining whether a foreign LLC is subject to service of process, taxation, or regulation under any other law of this state.	(4) Maintaining office or agencies for the transfer, exchange, and registration of the company's own securities or interests; (5) Selling through independent contractors; (6) Soliciting or obtaining orders if the orders require acceptance outside this state before they become contracts; (7) Creating or acquiring indebtedness, mortgages, and security interests in real or personal property; (8) Securing or collecting debts or enforcing mortgages and security interests in property securing the debts; (9) Conducting an isolated transaction within thirty days that is not one in the course of repeated transaction; (10) Transacting business in interstate commerce. (b) For purposes of this article, the ownership in this state of income-producing real property or tangible property, other than property excluded under subsection (a), constitutes transacting business in this state. (c) This section does not apply in determining the contacts or activities that may subject a foreign LLC to service of process, taxation, or regulation under law of this state other than this act.

INTRODUCTION

The Committee has requested some additional research on fiduciary duties within the LLC and the series LLC.

I. CONTRACTUAL FREEDOM VS. STRONGER DEFAULT PROVISIONS

A key issue for the group is whether to leave the Mississippi LLC Act as a Delaware-styled, freedom-of-contract statute, allowing the operating agreement to govern the legal responsibilities of members, or to statutorily limit the operating agreement's ability to eliminate and modify fiduciary duties.

A. The Tennessee Revised Limited Liability Company Act (2005)

When Tennessee enacted its LLC Act in 1994, like most other states' LLC Acts, it was primarily designed to ensure that a properly-organized LLC would be treated as a partnership for federal tax purposes while maintaining a corporate-type liability shield. To achieve this goal, it contained numerous, complex technical requirements governing the organization and operation of LLCs.

Since 1994, however, federal tax laws have changed. Now, an LLC simply has to check a box on a tax form to be taxed as a partnership. Although Tennessee's LLC Act had been amended over the years to remove some of the tax-driven provisions, it continued to be a complex statute that was difficult to navigate and understand. The state desired a simpler, shorter, more flexible and more user-friendly statute, without unnecessary tax-driven provisions. This desire resulted in the Tennessee Revised Limited Liability Company Act of 2005 ("TRLLCA").

Section 401 of the TRLLCA allows for a "check-the-box" management choice. The Articles of Organization form, which can be filed online, requires the registrant to elect one of three (3) management choices (the former Act provided for only member-managed or governor (manager)-managed):

1. <u>Member-managed</u>: members have powers like those of general partners of a general partnership.
2. <u>Manager-managed</u>: members elect managers who have powers similar to those of general partners of a limited partnership.
3. <u>Director-managed</u>: LLC has a board of directors and officers like a corporation.

Under the former act, each LLC was required to have an individual acting as Chief Manager. That concept is absent in the TRLLCA. If there is to be a chief executive, that person may now be called "president" or have any other title desired by the LLC.

B. The Resulting Duties of Loyalty and Care in Choice of Management

Tennessee's former Act left open the possibility for a court to create fiduciary duties in addition to those set forth in the Act. TRLLCA makes it clear that the only fiduciary duties owed by a member of a member-managed LLC or by a manager of a manager-managed LLC are the statutory duties of loyalty and care.[1] The directors of a director-managed LLC and the officers of any LLC, however, are held to the same standards of conduct as directors and officers of corporations under the Tennessee Business Corporation Act. This is significant in that it indicates Tennessee's intention to treat the members and managers of member-managed and manager-managed LLCs like partners, defaulting to statutes limiting the traditionally high duty of loyalty in partnership law and echoing exactly the traditional duty of care in partnership law; and to treat the officers or directors of a director-managed LLC like corporate officers and directors.[2]

The implication for officers or directors of director-managed LLC could include application of the business judgment rule. The business judgment rule is well established in the corporate context of duty of care, but case law addressing the application or rejection of the business judgment rule in other business entities is limited. The following article explores the interplay of the business judgment rule and unincorporated business associations, such as LLCs.[3]

The Revised Uniform Limited Liability Company Act limits LLCs from eliminating certain fiduciary duties via the operating agreement. Tennessee Code §48-249-205 lists twenty-one (21) provisions that cannot be eliminated by the operating agreement. Included among these is a prohibition on eliminating the duty of loyalty or "unreasonably reducing" the duty of care.

II. A SUMMARY OF THE MILLER AND RUTLEDGE ARTICLE

The article reviews the business judgment rule in the corporate context and recent developments to unincorporated business entity laws that have altered the relationship of owners to each other and the entity. It also examines the degree to which the business judgment rule has been incorporated into the fiduciary provisions of the unincorporated business entities' acts. Finally the article reviews the limited case law addressing the business judgment rule applicability to unincorporated business associations.[4]

A. The Business Judgment Rule in the Corporate Context

Section II describes the business judgment rule as a judicial review standard rather than a standard of care. When a board of directors has exercised a minimum standard of care in making a decision, the courts will not second-guess the merits of the decision. If the process was proper, then the merits of the decision are not questioned.

In Delaware the plaintiff must show that the directors either made no decision or they were not disinterested or independent; or that the decision was uninformed or involved gross negligence.

Without the protection of the rule, directors must prove the entire fairness of a transaction. The plaintiff overcoming the presumption shifts the burden to the directors to prove entire fairness. The most obvious instances when the business judgment rule is unavailable to directors are when the directors are interested in the transaction or the directors cannot demonstrate that the proper process was followed.

Section II also offers five (5) justifications for employing the rule and notes that the provisions limiting personal liability of directors does not define the applicable fiduciary duties of directors.

B. The Evolving Structure of Unincorporated Business Organizations

Section III discusses the evolution of partnerships and the rise of the adoption of uniform partnership acts. While not summarized in this material, the evolution of partnerships is important for its part in shaping the relatively new entity, the LLC. It must be noted however, that the most recent uniform partnership laws define the fiduciary duties of both limited and general partners. The article notes that LLC statutes vary widely from state to state, particularly as the statutes regard fiduciary duties.

The article describes today's available business structures. Today, many LLCs are structured very similarly to corporations, even to the extent of being publicly-held. The article cautions that as unincorporated business organizations continue to assume aspects once reserved to the corporate form, there is a danger that corporate case law may be indiscriminately applied to the other business entities. The warning, in simple terms, is that while many states choose acts with more contractual governance—allowing the operating agreement rather than the statute to establish (or eliminate) fiduciary duties—there is always the possibility that courts will impose corporate standards on members or managers.

The final section notes the inconsistency in the application of the business judgment rule by courts in unincorporated organization litigation. Earlier, this paper reviewed Tennessee's changes to its LLC act, one being the implied incorporation of the business judgment rule protection for directors or officers of director-managed LLCs. Keep in mind that the business judgment rule is not a standard of care, but a standard of judicial review. Tennessee thus potentially invites courts to apply the business judgment rule. While this could offer predictability, the following section illustrates why it probably does not. As previously noted, the application of the business judgment rule in the LLC context is inconsistent at best.

C. The Mixed History of the Business Judgment Rule in Unincorporated Business Organization Law

The final section analyzes the use of the business judgment rule in the partnership context. The article notes that because no widely accepted approach to the duty of care has emerged from the varied statutes governing LLCs, and that because there is little case law focusing on the duty of care of members and managers of LLCs, there is little judicial guidance on whether liability for breach of the duty of care will be determined under a relaxed standard of culpability. Of note, in a Delaware case, the Delaware Chancery Court implied that the business judgment rule was applicable in LLC cases, but rejected the defendants' argument that the rule protected them, even though they conscientiously believed their actions were in the best interest of the LLC.[5] The Court found a breach of the duty of loyalty in the defendant's secretly orchestrated squeeze-down merger. Other cases referenced in the article note instances where the manager of an LLC sought business judgment rule protection but the court did not consider the rule at all.[6]

The article discusses the competition between the overlap of contract and fiduciary law, noting that the overlap presents a new challenge and demands a mechanism for assessing which frame of reference, a contract approach or a fiduciary duty approach, must be applied when considering an issue. Courts could apply a contract analysis, simply seeing if the agreement permits or prohibits the challenged action, or apply a fiduciary model imposing limitations to protect non-managerial investors from overreaching by the management. While the article notes that this problem persists regardless of entity form, it advises that a decision should be made deciding which frame of reference controls.

The article lists six (6) scenarios demonstrating the interplay of contract and fiduciary law. In the scenarios, the underlying statute:

1. expressly provides for a fiduciary duty of care and permits it to be waived or modified in the agreement, and the parties have waived or modified the duty by agreement.
2. expressly provides for a fiduciary duty of care, but is silent regarding waiver or modification, and the parties have waived or modified by agreement.
3. expressly provides a fiduciary duty of care and the agreement is otherwise silent.
4. is silent as to the fiduciary duty of care, but permits modification or waiver of duties and the parties have incorporated a standard into the agreement.
5. is silent as to the fiduciary duty of care and as to modification or waiver of duties and the parties have incorporated a standard into the agreement. [7]
6. is silent as to the fiduciary duty of care (and either does or does not permit modification or waiver of duties) and the parties have not incorporated a standard into the agreement.

The article notes that the final scenario represents the danger of a silent statute and is most troubling because the parties have not expressed their expectations. One interpretation is that the parties desired to have their agreement interpreted under a common law duty of care. Another view, however, is that the parties drafted what they thought was necessary for their relationship and did not expect the importation of common law fiduciary duties. The article notes that there is little justification for choosing one of these approaches over the other. If the agreement is not complete, the outcome of any dispute is unpredictable.

Next, the article reaches the crux of the business judgment rule issue. In the other five (5) scenarios, the parties have specified the standard of care they desire. They reasonably expect the terms of the agreement to be enforced. What they do not expect is that the agreement will be enforced, not as they have drafted it, but to a degree deemed necessary by the courts to preserve the flexibility of management. That additional deference is provided by the application of the business judgment rule; the court choosing a standard of review over the standard of care incorporated into the agreement. This presents an unworkable situation, drafters being required to properly assess the degree to which they must "draw back" the contractual standard of care so that, when combined with the judicial deference of the business judgment rule, the parties' intentions are actually achieved. This leads to a "catch-22" where perhaps the business judgment rule should not be used when parties clearly express their intentions, but perhaps should be used when they have not. This raises the question: if a state like Tennessee has invited courts to apply the business judgment rule (if only by implication), will it be applied even in situations where the parties have clearly reflected their intentions?

In conclusion, the authors opine that under statutes adopting a gross negligence standard of care (the lowest standard), there is no room for the further deference of the business judgment rule.[8] Further, the authors' opinion is that regardless of the statutory standard of care, where members have sought to specifically define a standard of care (if the statute is silent or allows modification or waiver), that standard should be enforced as written.

III. A SUMMARY OF THE SANDRA MILLER ARTICLE

This article explores the courts' role in balancing contractual freedom concerns with concerns of limiting abusive conduct in LLCs[9] and illustrates the emergence of a mandatory core of conduct for LLC participants reflected in developing case law. In other words, courts are slowly but surely filling fiduciary duty gaps as they see them in the freedom of contract based system. If not statutorily addressed, fiduciary duties are increasingly likely to be addressed by the courts.

The Contractarian Theory of the Business Entity

The article poses a foundational premise of the LLC. While LLC statutes typically contain some mandatory provisions, most simply provide a set of default rules that apply only in the absence of provisions in the parties' operating agreement. The LLC is primarily a contractual arrangement in which parties use the entity's governing documents to establish their legal relationship. The article reflects a movement in the context of unincorporated business organizations to control liability contractually, as evidenced in the uniform laws governing partnerships and LLCs. The article notes that the uniform acts do not provide complete contractual freedom but that the acts enhance contractual freedom through the use of default provisions that only apply in instances the operating agreement does not address.

This introduction establishes the starting point for LLCs that may be echoed by many proponents of the LLC: business participants should be able to strike their own business deals. Advocates for freedom from mandatory rules believe that business law should facilitate the private contracting of parties with minimal judicial or statutory intervention. The author opines that such proponents "fail to consider the human relationships that develop in privately-owned businesses."[10] While some "contractarians" believe that market forces can control managerial misconduct, such reliance may be misplaced as it regards LLCs. The article lists a couple of reasons. Private, closely-held entities lack a ready market, and they are not required to present audited financial statements.

In short, this article presents a perspective (similar to the earlier article) of why modifying our present LLC act (or adopting a statute like the RULLCA, more defined in the area of fiduciary duties) is something to consider. Both articles indicate the increasing role of the courts in determining areas not addressed by either the statute or the operating agreement.

The articles described above may assist the group in formulating recommendations addressing fiduciary duties. The present legislative stance indicates Mississippi's intention to follow a Delaware model and pro-contractual stance. These articles look to the future as case law develops in the area of LLCs to issues the group may want to anticipate.

IV. A SUMMARY OF THE SERIES LLC ARTICLE

This article offers a good overview of series LLCs. The LLC laws have evolved to add a series LLC that provides for even more segregation of liability for the company. In a series LLC, the debts, liabilities, and obligations relating to one series are only enforceable against that series. The article also discusses the seven (7) states that have adopted this form and notes that they are facing numerous questions that have remained unanswered. Finally, the article also examines tax implications which are not summarized in this discussion. [11]

A. The Framework: A Look at the State Laws

Delaware

- First state to adopt series LLCs, became the model for other states to follow.
- The series LLC was adopted to establish an LLC agreement that included multiple series that had separate rights, powers, or duties.
- Three (3) conditions to maintain that a series would only be responsible for the obligations of that series.
  1) Separate and distinct records must be maintained for each series, the series assets are accounted for in those records separately from the LLC and other series.
  2) LLC agreement must provide for the maintaining of the aforementioned records.
  3) Certificate of formation must include a notice of the limitation on liabilities.[12]
  - Offers separate governance and procedural rules for classes or members with each series.
  - Other provisions that ensure the separate nature of the each series:
  - An event that causes a manager to cease to be a manager with respect to one series will not, in itself, cause the manager to cease to be a manager of the LLC with respect to any others,[13]
  - A series can be terminated and its affairs wound up without causing the dissolution of the LLC,[14]
  - Distributions are generally limited with respect to any series to the fair market value of the assets in excess of liabilities associated with the series.[15]

Iowa

- Essentially mirrors the Delaware act with a few exceptions.
- Series may be terminated only by a unanimous decision of the members. Whereas in DE a series may be terminated by the members who own more than two-thirds (2/3) of the then-current percentage of profits in the series.

Illinois

- Similar to DE act, but contains additional provisions that increase the separation of the series.
- Provides for a series to be treated as a separate entity as set forth in the articles of organization with each series creating itself through a separate certificate of designation.
- Addresses the tax implications of a series LLC when most states have not.
  - o LLC and any of its series may elect to consolidate their operations as a single taxpayer "to the extent permitted under applicable law."[16]

Nevada

- Allows the articles of organization or operating agreement of an LLC to create one or more series of members, or to vest in one or more members or managers of the LLC or in other persons the authority to create one or more series of members.[17]

- Prohibits a distribution of profits and contributions of a series if, after giving the distribution effect, the LLC would not be able to pay the debts of the series from assets of the series as those debts become due in the usual course of business.[18]
- $125 filing fee for each series in a series LLC compared to $75 for an LLC.

Utah

- Operating agreement may provide for the establishment of one or more designated series of members, managers, or interests in the LLC having separate rights, powers or duties with respect to some property or obligations of the LLC or profits and losses associated with some property or obligations.[19]

Tennessee

- LLC documents may establish one or more designated series with respect to specified property or obligations on the LLC or with respect to profits and losses associated with specified property or obligations.[20]
- Individual series must maintain separate and distinct records.[21]

B. What the State Statutes Do Not Do

All of the states that have adopted the series LLC have in some form or another segregated the liabilities of one series from another series in the same LLC. On the other hand, all these states (with the exception of Illinois) have come up short in confirming that each series is to be treated as a separate legal entity for other purposes. For example:

1. Only Illinois allows a separate series to sue or be sued in its own name;
2. The states do not allow separately for a series to merge or consolidate with another legal entity;
3. The states do not allow a series to convert to another type of business entity; and
4. The states do not allow a series of a foreign LLC to domesticate in that jurisdiction without the domestication of the entire LLC.

C. Tax Treatment is Unclear

Even though the series LLC is growing in popularity, there is still a lack of information on how the entity should be taxed. Until there is clearer guidance, all practitioners intending to treat the series LLC as a separate taxable entities should keep all assets, contracts, correspondence, and so on separate and within the asset's specified series. The practitioner should even file a separate tax return. Even without guidance from the IRS, there is enough authority to support the separation method.

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[1] Unlike Mississippi's present Act, the Tennessee Act explicitly defines the fiduciary duties of members to other members, the LLC, and to the holders of financial rights. This is consistent with the RULLCA. Mississippi only explicitly states a duty of care for managers. Managers, and implicitly in the case of member-managed LLCs, members, are statutorily obligated to discharge their management duties in "good faith," with the care of an "ordinarily prudent person in a like position," in a manner reasonably believed to be in the best interest of the company. Absent from the Mississippi Limited Liability Company Act is a statutory duty of loyalty. However, a duty of loyalty is implied elsewhere in the act and by analogous common law duties established in corporate jurisprudence. A manager's duty of loyalty is essentially a duty to act on the company's behalf, ahead of the manager's personal interests. This duty is fiduciary in nature, and can arise in the area of self-dealing, whereupon a manager profits from transactions with the LLC, fails to fairly present business opportunities to the LLC, or uses of firm assets, which in effect may be an unauthorized compensation or distribution. A manager's competition with the LLC may also breach his or her duty of loyalty, even if the opportunity were unavailable to the LLC. The duties of management and the duty of loyalty in particular, could be an area of litigation in future years. In the absence of statutory language or case law adequately defining these duties, the prudent drafter will incorporate specific limitations and standards concerning such duties in the operating agreement or in the Certificate of Formation.

[2] The duty of care is the duty to be attentive and to be informed before making decisions that affect the company. The duty of loyalty is the duty to always conduct oneself in a manner that advances the best interests of the company.
[3] Elizabeth S. Miller and Thomas E Rutledge, The Duty of Finest Loyalty and Reasonable Decisions: The Business Judgment Rule in Unincorporated Business Organizations? 30 Del. J. Corp. L. 343 (2005). A copy of the entire article is included with these materials.
[4] *Id*. at 344-45.
[5] *VGS, Inc.* 2000 Del. Ch. LEXIS, 122 at 15-16.
[6] *Shell v. King*, a Tennessee case discussed at 378-79 of the article.
[7] The Mississippi LLC Act is silent. As discussed in the first Committee meeting, often the agreement is silent as well, particularly in situations where the members do not employ counsel.
[8] Mississippi's standard of care for managers is "in good faith, with the care an ordinarily prudent person in a like position would exercise under similar circumstances; and in a manner he reasonably believes to be in the best interests of the LLC. This standard is verbatim the standard for corporate directors in the Model Business Corporations Act §8.30 and is the same standard used by Tennessee for directors or officers in a director-managed LLC. By implication, then, in Mississippi, may LLCs operating in the corporate form with directors or officers be inviting the application of the business judgment rule by courts? There is presently no case law in Mississippi addressing this issue.
[9] Sandra K. Miller, The Role of the Court in Balancing Contractual Freedom with the Need for Mandatory Constraints on Opportunistic and Abusive Conduct in the LLC. 152 U. Pa. L. Rev. 1609.
[10] *Id*. at 1618.
[11] Michael E. Mooney, *Series LLCs: The Loaves and Fishes of Subchapter K*, 813 PLI/Tax 355 (2008).
[12] Del. Code Ann. tit. 6, section 18-215(a).
[13] Del. Code Ann. tit. 6, section 18-215(f).
[14] Del. Code Ann. tit. 6, section 18-215(j).
[15] Del. Code Ann. tit. 6, section 18-215(h).
[16] 805 ILCS section 180/37-40(b).
[17] Nev. Rev. Stat. section 86.296(1).
[18] Nev. Rev. Stat. section 86.343(2)(a).
[19] Utah Code Ann. section 48-2c-606 et seq.
[20] Tenn. Code Ann. section 48-249-309 et seq.
[21]Tenn. Code Ann. section 48-249-309(b).

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Article

*1609 THE ROLE OF THE COURT IN BALANCING CONTRACTUAL FREEDOM WITH THE NEED FOR MANDATORY CONSTRAINTS ON OPPORTUNISTIC AND ABUSIVE CONDUCT IN THE LLC

Sandra K. Miller [FNd1]

Courts are establishing a mandatory core of acceptable business conduct within the relatively new context of the limited liability company (LLC). Outside of Delaware, courts have tailored traditional notions of corporate and/or partnership fiduciary duties to the LLC, while within Delaware, courts are developing minimum standards of conduct through restricted interpretations of contractual waivers, rigorous application of the entire fairness standard, and recourse to contractually based concepts of good faith. This Article suggests that a broad and traditional approach to fiduciary duties is preferable to a narrower analysis of entire fairness or contractually oriented good faith because a broader formulation better reflects society's norms of ethical conduct, more adequately serves all sectors of the private business community, may be more effective in combating subtle freeze-out schemes, and does not presume that the parties' relationship is governed by a highly negotiated contract. Furthermore, this Article emphasizes that courts are central to all LLC modeling, including Delaware's contractarian paradigm, and are leading the way toward the development of a mandatory frame of reference for balancing the interest in contractual freedom with the need for minimum standards to curb opportunistic and abusive conduct.

Introduction

The limited liability company (LLC) has been hailed as the entity of choice in the privately owned business arena. Freed from mandatory tax classification rules, the LLC, in addition to limiting liability, can now possess the corporate characteristic of "continuity of life" and need not dissolve when a member withdraws, dies, or becomes bankrupt. [FN1] Private entrepreneurs have an unparalleled range of choices ***1610** for structuring LLC relationships, and LLC participants have access to the twin benefits of corporate limited liability and flow-through partnership tax status.

Two major forces contributed to the development of the LLC. First, practitioners sought the flexibility to structure their clients' internal relationships while continuing to receive favorable flow-through tax treatment. [FN2] Second, in an atmosphere of escalating jury awards, [FN3] practitioners advocated control over the legal liability of their clients with respect to both coinvestors and third parties. [FN4] They wanted a framework that would reduce judicial encroachment into the business deals that they negotiated and formalized. [FN5]

Each state, as well as the District of Columbia, now has its own LLC statute, [FN6] and these statutes allow a great deal of freedom in forming an LLC. [FN7] The statutes typically assume that the individual owners

***1611** will develop their own LLC operating agreements that define their respective rights, responsibilities, and remedies. Often described as enabling legislation, the LLC statutes largely provide a series of default rules that apply in the absence of contractual provisions to the contrary. [FN8] While some LLC statutes contain express mandatory fiduciary duties, [FN9] others, particularly the Delaware LLC statute, do not. [FN10] Delaware's contractarian vision of business entities is evidenced in its policy to give the maximum effect to the principles of freedom of contract and strict enforcement of LLC agreements. [FN11]

Now that over a decade has elapsed since the first LLCs were formed, it is an opportune time to evaluate the LLC experiment. How successful has enabling legislation been in reducing disputes among business associates? Has there been a reduction in the need for judicial intervention? Is Delaware's contractarian model leading to fewer lawsuits and increased freedom from judicial monitoring? The short answer to these questions is "no." [FN12]

This Article compares the developing case law on fiduciary duties both outside and inside Delaware and finds that across the board, ***1612** there is a continuing need for the imposition of judicial remedies for abusive and opportunistic conduct. Regardless of whether the LLC statutes contain express fiduciary duties or, conversely, embrace a broad mandate for contractual freedom, courts are compelled to address the enduring issue of fiduciary breaches. The LLC statutes are relatively new, but abusive conduct is not. LLC cases have arisen repeatedly in which majority-owners have removed or reduced the ownership percentages of their minority partners. [FN13] Allegations of abusive LLC conduct have included claims that business opportunities have been stolen, [FN14] that LLC members have been improperly excluded, [FN15] and that LLC assets have been improperly transferred to another entity. [FN16] These classic "squeeze-out techniques," which have a long history in the close corporation setting of the past fifty years, are now surfacing in the context of the LLC. [FN17]

In response to these abuses, courts are formulating a mandatory core of fiduciary duties as they mediate disputes among LLC business associates. How then can this development in the LLC case law be ***1613** reconciled with the contractarian model of the business entity? [FN18] At first glance, this external monitoring does not appear to fit within the contractarian equation that emphasizes the supremacy of the private contract and the importance of reducing transaction costs through lack of external interference. It is suggested, though, that the contractarian model can be reconciled with the mandatory core of duties emerging in LLC case law by recognizing that at the heart of the private contract is the notion that there is a legally enforceable bargain subject to the many mandatory constraints of the legal environment. [FN19]

The primary message of this Article is that the courts are central to all LLC models, including Delaware's contractarian paradigm, and are leading the way toward balancing the interest in contractual freedom with the need to constrain opportunistic and deceptive conduct through the development of a minimum mandatory core of acceptable business conduct. This developing LLC case law illustrates that even under Delaware's contractarian approach, the LLC is not the proper vehicle for eliminating or diminishing judicial intervention; rather, the LLC is a business entity that permits private contracting within the context of mandatory restraints. The private business entity contract can be seen as operating within a framework of mandatory fiduciary duties that may be modified, but not wholly eliminated, and that are enforced through active judicial intervention.

Part I of this Article discusses the contractarian model, its manifestations in corporate, partnership, and LLC law, and its theoretical basis. Part II examines the statutory underpinnings of fiduciary duties applicable to LLC members and managers and the policy questions that are raised. Parts III and IV explore the judicial monitoring of ***1614** fiduciary duties that has occurred in LLC cases both outside and inside Delaware.

In particular, Part III observes that in spite of the broad, permissive language that exalts the primacy of the contract, a mandatory core of minimum fiduciary duties appears to be thriving in Delaware through express statements by the Delaware courts and in cases requiring a showing of fundamental fairness where the presumption of the business judgment rule has been rebutted. Also, this network of minimum standards of acceptable business conduct is supported in Delaware through the courts' resourcefulness in using contractually based principles of good faith.

Next, Part IV addresses the common ground shared by courts outside and inside Delaware and argues that across all jurisdictions, the courts are defending plaintiffs against the usual litany of evils--clandestine, fundamental changes in the business, [FN20] unilateral transfers of assets, [FN21] sudden meetings that dramatically reduce the plaintiff's control of the company, [FN22] and the diversion of business opportunities to a competing entity. [FN23] Regardless of whether the judicial safeguards are described as a partnership-style duty to account for benefits of the business, a corporate-style duty to act in good faith in the best interests of the company, or a required showing of fundamental fairness based on a conflict of interest and lack of good faith, the courts appear to be fashioning a mandatory core of acceptable business conduct in the context of the LLC.

Finally, Part V of the Article emphasizes that all LLC models, including the contractarian paradigm, should acknowledge the influence of courts in an environment of private ordering, the valuable role played by equitable principles generally, and the role fiduciary duties play in reflecting ethical norms in the business community. [FN24]

***1615** I. The Contractarian Theory of the Business Entity

LLC statutes may be characterized as enabling legislation. While LLC statutes typically contain some mandatory rules, many simply provide default rules that apply only in the absence of contrary provisions in the parties' operating agreements. [FN25] Implicit in the structure of LLC legislation is the notion that parties will contractually fine-tune the parameters of their legal relationship in the governing documents of the business entity.

A similar situation developed earlier in the corporate context regarding directors' liability for monetary damages arising out of violations of the standard of care. Here, the concept of contractually limiting director liability manifested itself in the enactment of enabling statutes that allow shareholders to insulate directors from liability by adopting certain provisions in their articles of incorporation. [FN26] Prompted by the decision in Smith v. Van Gorkom [FN27]--holding outside directors liable for gross negligence in approving a cash-out merger without properly informing themselves about the value of the company--the Delaware legislature led what soon became a national stampede toward allowing articles of incorporation to eliminate personal director liability for monetary damages stemming from breaches of fiduciary duties, except in specific cases, i.e., violations of the duty of loyalty, acts or omissions not in good faith, and conduct involving improper personal benefits. [FN28]

***1616** In the context of the noncorporate business entity, the movement toward contractually controlling liability has been reflected in the enactment of the Revised Uniform Partnership Act (RUPA) [FN29] and the Uniform Limited Liability Company Act (ULLCA). [FN30] While neither Act permits unlimited contractual freedom, both Acts enhance it by providing default rules that apply in the absence of an agreement to the contrary. [FN31] In addition, many states have enacted their own LLC default rules, offering in varying degrees significant flexibility and contractual freedom in structuring business relationships. [FN32] The ***1617** Delaware LLC statute stands out, however, for its lack of mandatory rules and its express policy to “give maximum effect to the principle of freedom of contract." [FN33] Similarly, the ABA-drafted Prototype Limited Liability Company Act (PLLCA) contains statements regarding the duties of managers, but allows the operating agreement to eliminate, or at least limit, the personal liability of a member or manager for breaching fiduciary duties. [FN34]

The LLC legislation that has developed rests largely on a similar view that business participants should be free to strike their own business deals. This contractarian view of the business entity regards the firm as a "nexus of contracts." [FN35] Under this approach, advocates for freedom from mandatory rules believe that business law should facilitate the private contracting of parties, with minimal judicial or statutory interference. [FN36] Broad judicial rulings, particularly with regard to fiduciary duties, have been regarded with suspicion, especially by ***1618** practitioners who have sought to limit their clients' liability through contractual arrangements. [FN37]

Conceptually, the "contractarian framework" sprang from the impact of economic theory upon business law. [FN38] As explained by the English scholar Robert Goddard:

> At a prescriptive, normative level, [the contractarian approach] provides a conceptual framework capable of resisting state intervention, and one in which the state's role is dual: first, to provide an appropriate mechanism for bargain enforcement; and, secondly, to provide a framework within which bargaining is made more efficient . . . . [FN39]

In arguing for less government regulation, the contractarian scholars of the Chicago School of Economics have noted the importance of reducing transaction costs, emphasizing that the fiduciary paradigm for corporate governance interferes with the market for corporate control and impedes profit maximization. [FN40] Under this view, if mandatory fiduciary duties are imposed, the parties will have an increased cost which will be passed on to consumers, resulting in an inefficient use of resources that will ultimately cause society to suffer. [FN41]

***1619** The contractarian model and its preoccupation with transaction costs, however, fail to consider the human relationships that develop in privately owned businesses. Indeed, the theoretical framework overlooks the vulnerability that has traditionally spurred the recognition of a fiduciary relationship, and distances itself from the actual and potential harm that minority-owners have historically experienced in the close corporation setting. [FN42] The implicit value judgment underlying this contractarian view is that governmental policies based on interference and protectionism are inherently negative and should yield to the freedom of parties to contract on their own behalf. [FN43]

While some contractarians such as Professor Larry Ribstein are confident that market forces can control managerial misconduct, [FN44] this reliance may well be misplaced in the context of the LLC since the private business entity lacks a ready market and is not required to present audited financial statements. [FN45] Also, the assumption that fewer mandatory rules will result in decreased judicial intervention may not withstand the test of time. A recent study reported that the rate of lawsuits filed in connection with majority/minority disputes was significantly higher in Delaware, despite its enabling statute, than in the other states sampled. [FN46] The rate of suits filed by Delaware ***1620** practitioners who had handled majority/minority disputes was actually more than twice that of the other states considered. [FN47] Vice Chancellor Jack B. Jacobs of the Delaware Court of Chancery recently described the remarkable volume of litigation spawned by alternative business entities in Delaware as problematic. [FN48]

Embedded within this inquiry lies a related question regarding the fairness of the contractarian vision in representing the needs of the business community at large. Depending on the extent to which it fails to consider the interests of the less sophisticated and less financially privileged small entrepreneurs who may not be well represented by legal counsel, the contractarian model may be positioning certain LLC members at an initial disadvantage that is impossible to surmount. [FN49]

Ultimately, the wisdom of the contractarian vision of corporate law, and its influence on business culture, may well be questioned in the wake of the Enron debacle and subsequent accounting scandals. [FN50] ***1621** In conceptualizing the relationship among owners of the private business, the contractarian approach shifts the focus from a broad-based fiduciary-oriented regime to one that narrowly identifies the participant's contractual obligations. This perspective places primary emphasis upon one's freedom to pursue one's self-interest, rather than upon one's duties and obligations with respect to others and to the business enterprise itself. As Allan W. Vestal observes:

> Historically, the core of the "fiduciary's duty is an attitude, not a rule" for partnerships, as well as for close corporations. It is detrimental to substitute rules that invite evasion, for social principles that foster broad compliance. Abandonment of fiduciary principles may be efficient for some participants, but it is not beneficial to society. [FN51]

Recent accounting scandals serve as a warning against business cultures that place insufficient limits upon conflicts of interest and self-interested conduct and that fail to adequately emphasize the importance of one's responsibilities to others.

II. Diverse LLC Statutory Treatment of Fiduciary Duties

The LLC presents an interesting challenge to existing theories of corporate governance because of its hybrid nature. Based partially on both the partnership and corporation models, the LLC is an alternative business entity that does not always fit into existing legal paradigms. Will partnership and/or corporate precedents for the standard of conduct and duty of loyalty apply? [FN52] Should contractual obligations of good faith be used to resolve an LLC member dispute rather than fiduciary duties? [FN53] What theories should apply if there is ***1622** no written operating agreement? Should heightened fiduciary duties apply in a case involving a majority owner of a small private LLC and a minority participant?

The answers to these questions are not obvious. As it stands, the results in any particular dispute depend, in part, upon the diverse body of enabling legislation, the LLC operating agreement, and the particular court's fiduciary duty jurisprudence. It has not been clear to what extent a given dispute should be settled with reference to contract law or to fiduciary principles, and if fiduciary principles apply, whether the reference should be made to partnership or corporate principles.

Under the common law, fiduciary duties are imposed upon parties who are entrusted with special degrees of responsibility and trust. [FN54] In the trustee/beneficiary context, the trustee owes fiduciary duties to the beneficiary. [FN55] In partnership law, partners owe fiduciary duties to both the partnership and the other partners, and in the corporate realm, directors owe fiduciary duties to the shareholders. [FN56]

In both partnership and corporate law, fiduciary duties generally include both a duty of care and a duty of loyalty. [FN57] The duty of care is generally regarded as the duty to be attentive and informed before making a decision that affects the corporation. [FN58] The duty of loyalty ***1623** imposes a duty to conduct oneself in a manner that furthers the best interests of the partnership or the corporation. [FN59]

With regard to the standard of care, PLLCA provides that a member or manager of the LLC will not be liable or accountable for damages or otherwise unless the act or omission constitutes gross negligence or willful misconduct. [FN60] ULLCA similarly employs a gross negligence standard. [FN61] Comments contained in PLLCA observe that the gross negligence standard of care is analogous to the standard commonly applied to corporate directors, managing partners, or general partners of limited partnerships. [FN62] State LLC statutes vary with respect to the standard of care articulated. Some states, including Delaware, fail to adopt any express standard of care, [FN63] others utilize the gross negligence or willful misconduct language, [FN64] while still others employ language similar to that applied to directors under the Model Business Corporation Act (MBCA). [FN65] Among the latter group, some establish standards of conduct for managers but not for members. [FN66]

***1624** The statutory treatment of the duty of loyalty applicable to LLC members and managers is also quite diverse. Although some LLC statutes are silent as to fiduciary duties, [FN67] others contain express statements that the fiduciary duties of members and/or managers are limited to those specifically designated in the statute--for example, duties to account for certain benefits, to refrain from dealing with the LLC on behalf of an adverse party, or to refrain from competing with the LLC. [FN68] ULLCA has taken the latter approach. [FN69]

ULLCA's duty-to-account language has roots in the Uniform Partnership Act (UPA) [FN70] and is included in RUPA, in addition to specific statements regarding dealing in interests that are adverse to that of the partnership and competing directly with the partnership business. [FN71] Some statutes have likewise included a requirement to account ***1625** to other members for profits made from LLC transactions as a specific element of the duty of loyalty. [FN72]

The statutes also vary in the extent to which they permit contractual modifications to the statutory standards for fiduciary duties. Many LLC statutes even contain express restrictions on the right to contractually modify the member's or manager's standards of conduct in the articles of organization or operating agreement. [FN73]

In spite of the broad similarities between partnership and corporate fiduciary duties, some commentators have observed that judicial oversight of fiduciary duties has been more exacting with regard to ***1626** partnerships than with regard to public corporations. [FN74] While a corporate director must swear allegiance to the enterprise, place the best interests of the corporation and the shareholders before her own, and not exploit her position for personal profits, she is nevertheless permitted to engage in a self-dealing transaction or outside activity if it is "fair" to the corporation. [FN75] In contrast, the partnership rule is arguably more demanding insofar as a partner may not receive an individual profit without the consent of the other partners. [FN76]

A stricter interpretation of the duty of loyalty and increased judicial oversight have traditionally been observed in partnerships, where, as Chief Judge Benjamin Cardozo eloquently stated in the famous case Meinhard v. Salmon, [FN77] copartners "owe to one another . . . the duty of finest loyalty . . . . Not honesty alone, but the punctilio of an honor the most sensitive . . . ." [FN78] Although, in general, one corporate shareholder does not owe a fiduciary duty to another corporate shareholder, it may be argued that shareholders of a private corporation should owe a fiduciary duty to fellow shareholders insofar as the private corporation functions like an incorporated partnership. Thus, a heightened duty of loyalty has been extended to close corporations in some jurisdictions. [FN79]

This movement to extend heightened fiduciary duties to the close corporation setting has met strong resistance, with critics cynically ***1627** referring to it as "galloping Meinhardism." [FN80] Contractarians argue that "[f]iduciary duties are standard form terms that are not appropriate for many firms" and that "the parties might reasonably decide that standard form duties are prohibitively costly." [FN81] Thus, while traditionalists largely view fiduciary duties as moral mandates, [FN82] contractarians perceive them as economic choices. Left with this basic conflict in ideology, Delaware has attempted to steer its way toward a reasoned solution. At least with respect to the argument for heightened fiduciary duties in the close corporation context, Delaware has followed the contractarian view by refusing to recognize any alteration in the majority's fiduciary duties simply because the company is a close corporation. [FN83]

The debate surrounding the mandatory imposition of heightened fiduciary duties in the context of private business entities, and in the LLC particularly, pits the interest in freedom of contract against the need to both curtail abusive conduct and foster accountability. This clash of principles initially unfolded in the partnership context in contentious discussions surrounding the enactment of RUPA. [FN84] RUPA places limits on waivers of fiduciary duties but ultimately attempts to halt "galloping Meinhardism" by stating that there are only two ***1628** overarching fiduciary duties: the duty of care and the duty of loyalty, the latter being divided further into the duty to account, the duty not to deal with the partnership as an adversary, and the duty not to compete. [FN85]

The legal community has eagerly awaited case law to establish the parameters of these LLC member and manager fiduciary duties. In this regard, a variety of questions have been raised. For instance, will courts apply corporate fiduciary duties to LLCs that resemble small partnerships or close corporations in which the LLC owner may have an illiquid investment or will they instead employ heightened partnership-style fiduciary duties? Will increased judicial scrutiny apply to an LLC that resembles a limited partnership because of the special level of trust that nonmanaging LLC members may place in the LLC manager? To what extent will courts intervene to impose mandatory standards to curb abusive conduct, notwithstanding the fact that the LLC is designed to be a creature of private contracting? And finally, to what extent will courts respect contractual limitations on fiduciary duties?

Cases involving allegations of breach of fiduciary duties are beginning to emerge, and the discussion below separately analyzes selected cases both outside and inside Delaware. Clearly, the cases do not fully answer the many questions that LLCs raise. Nevertheless, some guidance is provided. Outside of Delaware, courts are assuming control over abusive conduct through the application of partnership- and corporate-style fiduciary duties. Within Delaware, courts have consistently refused to impute heightened fiduciary duties to LLCs because of the closely held nature of the LLC. At the same time, however, Delaware courts are exercising some control over abusive conduct, primarily by requiring the defendant to meet the entire fairness standard in conflict-of-interest transactions. This rigorous use of entire fairness may indeed become the source of considerable protection for minority LLC owners in cases that involve self-dealing in overt squeeze-outs, notwithstanding Delaware's commitment to private ordering and refusal to assign heightened fiduciary duties to closely held business enterprises. [FN86]

***1629** II. Judicial Monitoring of Fiduciary Duties Outside Delaware

Long-awaited judicial interpretations of fiduciary duties are also developing outside Delaware. Several of these cases involve typical patterns of abusive conduct that are commonly seen in a close corporation such as the theft of LLC property, [FN87] the improper transfer of LLC assets to other entities, [FN88] the usurpation of LLC clients, [FN89] and the squeeze-out of minority members. [FN90]

The judiciary appears, in at least one decision, to use partnership and corporate formulations of fiduciary duties somewhat interchangeably to combat such abusive conduct. In Fine v. Bork, [FN91] a Connecticut case involving the theft of LLC real property, the court referred to both partnership and corporate formulations of fiduciary duties to condemn the defendants' conduct. [FN92] This type of dual referencing is supported in the Connecticut LLC statute itself, which contains partnership language (e.g., the duty-to-account), as well as corporate-style formulations (e.g., the duty to discharge duties in good faith with the care of an ordinarily prudent person in like position). [FN93]

As indicated previously, some statutes apply a corporate standard of care to LLC managers, and consequently, one would expect case law to apply corporate precedents. Not surprisingly, in Flippo v. CSC Associates III, [FN94] where the Virginia LLC statute holds an LLC manager ***1630** to the standard applicable to corporate directors, [FN95] the court embraced a corporate formulation of fiduciary duties. [FN96]

In contrast, in Credentials Plus, LLC v. Calderone, [FN97] an Indiana decision involving the usurpation of business opportunities, the court applied partnership standards of fiduciary duty to the LLC. [FN98] According to the court, Indiana law provides that shareholders of close corporations owe partnership-like fiduciary duties to fellow shareholders. [FN99] The gravitation toward partnership fiduciary duties was also supported by the partnership-like duty-to-account language found in Indiana's LLC statute. [FN100]

Even absent statutory language imposing expressly stated fiduciary duties on members, it is nevertheless possible for courts to impose such duties based on corporation, close corporation, or partnership case law in the jurisdiction. For example, in Anest v. Audino, [FN101] an Illinois case involving a squeeze-out from the opportunity to participate in an exclusive distributorship, the statute did not specifically establish a standard of care during the time period in question. Relying on corporate law principles, however, the court held that LLC members and managers had obligations similar to corporate directors. [FN102] The court then concluded that the defendant had breached his fiduciary duties to the plaintiff by failing to properly disclose and tender the opportunity to the LLC, basing its decision on the corporate opportunity doctrine and close corporation precedents that imposed partnership-like fiduciary duties upon shareholders of close corporations. [FN103]

***1631** While these cases contain different mixes of partnership- and/or corporate-style statements of fiduciary duties, a common theme emerges. Whether under the guise of partnership or corporate formulations of fiduciary duty, the courts appear willing to police the more obvious patterns of opportunistic conduct ranging from theft of property to usurpation of opportunities.

A. Unilateral Dissolutions Designed to Seize or Control LLC Assets or Business Affairs

As indicated above, Fine v. Bork, the Connecticut LLC case involving the usurpation of real property, was decided against the backdrop of the Connecticut LLC statute, which integrates both traditional partnership and long-standing corporate notions of fiduciary duty. [FN104] The plaintiff and the defendant owned a parcel of commercial real estate indirectly through two LLCs, Tower Business Associates (Associates) and Tower Business Center (Center), with the real estate owned by Center. [FN105] When the relationship between the plaintiff and the defendant broke down, the defendant unilaterally and without the plaintiff's prior consent amended Center's operating agreement to allow it to exist with one member. The defendant then dissolved Associates, making himself the sole member of Center and the sole owner of the commercial real estate. [FN106]

The plaintiff filed a notice of lis pendens against the property of Center, and the court denied the defendant's motion to dissolve the notice against the property. [FN107] The court concluded that the defendant had violated the classic corporate-style standard of care contained in Connecticut's statute that requires members or managers to discharge their duties both in good faith, “with the care an ordinary prudent person in a like position would exercise under similar circumstances,” and in the best interests of the LLC. [FN108] The court also rested its decision on the statutory “duty-to-account” language requiring every member and manager to account to the LLC and hold as trustee for it any benefit derived by that person without the consent of ***1632** the majority of the disinterested managers or the majority in interest of the disinterested members. [FN109] This latter provision is very similar to the “duty-to-account” language in the Uniform Partnership Act and the Revised Uniform Partnership Act. [FN110]

In Flippo v. CSC Associates III, [FN111] the Supreme Court of Virginia also used a traditional corporate-style formulation of the standard of care and the business judgment rule to award compensatory and punitive damages against the manager of an LLC who, in order to achieve his own estate planning goals, transferred the LLC assets to another entity without the prior knowledge or consent of the other members. [FN112]

Flippo Land & Timber Co., L.L.C. (FLTC) was created to hold the assets which consisted of family-owned timberlands. [FN113] Three members of the family had created their own LLC, CSC Associates III, which in turn owned their part interests in FLTC. [FN114] In turn, those three family members--through CSC Associates III--refused to permit the other members of FTLC to create separate LLCs to hold their own interests in FLTC. [FN115] Thereafter, the defendant, Carter Flippo, dissolved FLTC, transferred its non-cash assets to a new venture, and offered CSC the option of joining the new venture if the members agreed to the terms of its operating agreement. [FN116]

The court upheld the imposition of compensatory and punitive damages against the defendant, relying on an LLC statute that embraced a corporate-style formulation of the business judgment rule. [FN117] The Virginia statute states that an LLC manager must discharge her duties in accordance with a good faith business judgment of the best interests of the LLC. [FN118] In upholding the lower court's finding that ***1633** Carter Flippo was liable for a breach of fiduciary duty, the Supreme Court of Virginia emphasized that Flippo had transferred the LLC's assets not to further the business interests of the LLC, but rather to achieve his personal estate planning goals. [FN119]

B. Traditional Judicial Monitoring to Police Diversion of LLC Business Opportunities

As many expected, some courts are using traditional partnership-style fiduciary duties to combat unfair appropriations of LLC opportunities. Chief Judge Cardozo's admonishment that partners owe each other “the duty of the finest loyalty” [FN120] first permeated partnership law, then close corporation law. It is now beginning to color the development of LLC law as courts seek to establish a fiduciary core that is applicable to LLC participants.

In Credentials Plus, L.L.C. v. Calderone, [FN121] Credentials Plus sued its one-third owner and former manager, Jill Calderone, for breach of fiduciary duty and intentional interference with business relations after she began soliciting the customers of Credentials Plus for her own company, National Credentials Corporation. [FN122] The defendant had managed the LLC, which assembled credentials-related data for physicians in client practice groups, but left to pursue her own business interests following a dispute with one of the other LLC owners that involved allegations of sexual harassment. [FN123]

The Indiana District Court granted the plaintiff's motion for summary judgment, holding that the defendant had breached her fiduciary duties to the LLC. [FN124] The court cited the defendant's correspondence with physician groups as evidence that she had engaged in self-dealing and had breached her duty of loyalty by soliciting clients and asking them not to mention her new company to the other owners of Credentials Plus. [FN125] In making its determination, the court relied heavily on the application of well-established fiduciary duties among partners. The traditional partnership-like language used by Indiana's LLC statute, reminiscent of the statutory language in Fine, ***1634** requires that "[u]nless otherwise provided in a written operating agreement, each member and manager must account to the [LLC] and hold as trustee for it any profit or benefit derived by the manager or member without the consent of a majority of the disinterested managers or members." [FN126] After noting that Indiana courts have treated closely held corporations as incorporated partnerships, the court indicated that shareholder/partners owe a fiduciary duty to deal fairly not only with the corporation, but also with other shareholders, and that they may not appropriate a business opportunity that belongs to the corporation. [FN127]

Along similar lines, in Anest v. Audino, the Illinois Appellate Court reversed the original determination by the trial court that the plaintiff, Bill Anest, did not owe a fiduciary duty to the defendant, David Audino. [FN128] Employing the corporate opportunity doctrine, the appellate court held that, as a coinvestor in the LLC, Anest did, in fact, owe a fiduciary duty to the defendant and had breached this duty when he failed to properly tender a business opportunity to develop an exclusive distributorship. [FN129]

Anest initially became a member of Precision Pour, LLC, because he was a creditor of Audino, who had been one of three owners of the LLC. [FN130] Following a recapitalization, Anest and the other LLC members, except for Audino, decided to form a new LLC to exercise an exclusive distributorship that initially had been offered to Precision Pour. The decision to form the new LLC without the defendant was made following an emergency meeting that had been called hastily in violation of the company's five-day notice requirement. [FN131] Defendant Audino counterclaimed that Anest owed and had breached a fiduciary duty to him. [FN132] At the time, the Illinois LLC statute did not contain an ***1635** express standard of care or loyalty, but provided that members and managers of LLCs would be liable to the extent that corporate shareholders or managers would be liable. [FN133] The appellate court observed that member-managers of an LLC, like corporate directors, owe a duty to deal openly and honestly with each other and to exercise the utmost good faith and honesty. [FN134] The court emphasized that, under Illinois law, directors and officers owe each other fiduciary duties similar to those of partners in a partnership. [FN135]

Thus, outside Delaware, the courts have been applying a mixture of partnership and/or corporate fiduciary duties to rein in opportunistic conduct, whether involving unilateral transfers of LLC property, seizure of LLC opportunities, or competitive conduct tantamount to theft of the LLC business.

III. Judicial Monitoring of LLC Fiduciary Duties in Delaware

The Delaware LLC statute itself contains no express duty of care or duty of loyalty [FN136] and, in fact, includes very strong statements endorsing the policy of freedom of contract and the ability to enlarge or limit various duties. [FN137]

Not surprisingly, the Delaware LLC cases that have emerged do not impose heightened fiduciary duties upon closely held enterprises. In light of the permissive tone of Delaware's LLC statute, one may wonder whether mandatory minimum duties exist and whether Delaware's contractarian approach can effectively police predatory and opportunistic conduct.

***1636** Several recent cases lend support to the view that such a mandatory minimum of acceptable conduct is unfolding in order to govern LLC managers or members. Behavioral restraints appear to be developing through three approaches: (1) the imposition of restrictions on the scope of permitted waivers of traditional fiduciary duties arising in Delaware limited partnerships; (2) the rigorous application of the entire fairness standard, which requires managers to prove a fair process and a fair price in the face of self-interested conduct; and (3) the application of contractually rooted concepts of good faith.

A. Narrowing the Permissible Scope of Contractual Waivers of Fiduciary Duties

The Delaware LLC statute contains an express statement establishing the preeminence of the contract between the parties. In particular, it declares its policy to "give the maximum effect to the principle of freedom of contract and to the enforceability of limited liability company agreements . . . . The member's or manager's or other person's duties and liabilities may be expanded or restricted by provisions in the limited liability company agreement." [FN138]

Virtually identical language deferring to the parties' contract is found under Delaware's Revised Uniform Limited Partnership Act (DRULPA). [FN139] Indeed, considering that so much of the Delaware LLC statute was taken almost verbatim from DRULPA, one can expect that precedents involving Delaware's limited partnership arena will be of particular relevance in resolving LLC disputes. [FN140]

Some Delaware decisions have been so deferential to the parties' contracts that they create an impression that general partners and LLC members may substantially and materially restrict common law ***1637** fiduciary duties. [FN141] In Sonet v. Timber Co., [FN142] for instance, the Delaware Chancery Court noted that DRULPA "apparently [allows] broad license to enhance, reform, or even eliminate fiduciary duty protections. [FN143] In Walker v. Resource Development Co. Ltd., L.L.C., [FN144] the Delaware Chancery Court reiterated Delaware's deference to the parties' contracts, observing that "'[t]he basic approach of the Delaware Act is to provide members with broad discretion in drafting the [Operating] Agreement and to furnish default provisions when the members' agreement is silent."' [FN145] The court further stated that "'[o]nce members exercise their contractual freedom in their limited liability company agreement, they can be virtually certain that the agreement will be enforced in accordance with its terms."' [FN146] The Delaware Chancery Court went on to state that "LLC members' rights begin with and typically end with the Operating Agreement." [FN147]

In light of the sweeping license this language appears to give to the contract, one might argue that it is permissible to very substantially reduce or even eliminate common law fiduciary duties in a Delaware LLC operating agreement. [FN148] However, a recent Delaware ***1638** Supreme Court opinion, Gotham Partners v. Hallwood Realty Partners, [FN149] indicates that while a partner's fiduciary duties may be restricted, they may not be completely eliminated. [FN150] Also, in Walker v. Resource Development Co., L.L.C., [FN151] notwithstanding the broad language on the important role of the operating agreement, the chancery court stated that Delaware's LLC provision allowing members of an LLC to rely in good faith on the terms of the operating agreement was never intended to allow the members of an LLC to misappropriate property from another member and avoid returning that property or otherwise compensating the wronged member. [FN152]

In Gotham Partners, the Delaware Supreme Court had not been asked to opine on whether a contract could eliminate common law fiduciary duties. [FN153] The Delaware Chancery Court had granted summary judgment, holding that the defendants had violated their contractual duties in connection with a tender offer. The only issue on appeal focused on damages. Nevertheless, the Delaware Supreme Court went out of its way to correct dicta in the chancery court ***1639** opinion which had stated that DRULPA expressly authorized the elimination, modification, or enhancement of fiduciary duties. [FN154] The Delaware Supreme Court observed that this erroneous dicta could be misinterpreted in future cases as a correct rule of law. [FN155] It went on to admonish courts, commentators, and practitioners:

> [W]e are constrained to draw attention to the statutory language and the underlying general principle in our jurisprudence that scrupulous adherence to fiduciary duties is normally expected.
> Section 17-1101(d)(2) states: "the partner's or other person's duties and liabilities may be expanded or restricted by the provisions in the partnership agreement." There is no mention . . . that a limited partnership agreement may eliminate the fiduciary duties or liabilities of a general partner. [FN156]

Questions of the scope of acceptable contractual waivers of fiduciary duties in Delaware have also been raised in the context of a takeover of a corporation. In Omnicare, Inc. v. NCS Healthcare, Inc., [FN157] the Delaware Supreme Court was required to determine whether the directors of an insolvent corporation, NCS, had violated their fiduciary duties by approving a merger transaction. The merger agreement obligated the directors to bring the merger proposal to a shareholder vote even if the directors failed to approve it; restricted the directors' rights to consider other merger agreements; required two of the directors, who were also sixty-five percent owners of the target, to vote in favor of the merger; and established appraisal rights for minority owners. [FN158] The case is significant both because the Delaware Supreme ***1640** Court employed enhanced judicial scrutiny and because it subordinated the parties' contractual expectations to the overriding policy interest in having directors properly discharge their fiduciary duties. [FN159] As the court observed:

> In the context of this preclusive and coercive lock up case, the protection of Genesis' contractual expectations must yield to the supervening responsibility of the directors to discharge their fiduciary duties on a continuing basis. The merger agreement and voting agreements, as they were combined to operate in concert in this case, are inconsistent with the NCS directors' fiduciary duties. To that extent, we hold that they are invalid and unenforceable. [FN160]

Although the Omnicare holding is limited to the context of coercive measures in connection with the merger of a public company, it has significance to all business entities insofar as it reveals the Delaware Supreme Court's willingness to place limitations on the extent to which directors may contract away their fiduciary duties in private agreements.

Based on the principles enunciated in Gotham and Omnicare, and the similarity between Delaware's limited partnership and LLC statutes, one would expect that the Delaware Supreme Court will not permit a broad and/or complete elimination of fiduciary duties in the LLC. Although the court has not yet addressed this issue, the Delaware LLC cases that have emerged do reflect an active judicial posture.

In Solar Cells, Inc. v. True North Partners, LLC, [FN161] for example, the Delaware Chancery Court ultimately enjoined a clandestine attempt to merge First Solar, LLC, into defendant's wholly owned subsidiary. [FN162] The defendant, True North Partners, LLC, controlled three of First Solar's five managers, while the plaintiff, Solar Cells, Inc., appointed the other two. [FN163] These latter two managers were not advised of the ***1641** proposed merger until shortly before it was to close. [FN164] Although a full board meeting was held the day before the three True North managers gave their written consent to the merger, the three failed to inform the other two board members of the merger. [FN165] If consummated, the merger would have had the effect of diluting the plaintiff's interest from a fifty percent interest to a five percent interest. [FN166] The True North managers defended their actions based on the contractual limitation of their fiduciary duties. [FN167] Nevertheless, while the operating agreement of First Solar did contain a fairly broad waiver of conflicts of interests, the court latched onto the fact that it had not eliminated the duty to act in good faith. [FN168] As a result, the court ultimately enjoined the merger. Had the court more broadly interpreted the waiver clause, however, a different decision might have been reached.

B. Minimum Standards Flowing From the Evidentiary Burden of Establishing Entire Fairness

A potential source of minimum standards of acceptable LLC manager conduct in Delaware may well emerge through the evidentiary burden of requiring LLC managers to prove that a self-interested transaction was fundamentally fair.

In Solar Cells and in VGS, Inc. v. Castiel, [FN169] another LLC merger case, the mergers were successfully challenged on the grounds that the managers' conduct was self-interested and the defendants would not be able to meet the burden of establishing that the mergers were fundamentally fair. [FN170]

Normally, in Delaware the business judgment rule provides that a director is presumed to act on an informed basis, in good faith, and in the best interests of the company. [FN171] The evidentiary burden is initially ***1642** placed on the plaintiff to rebut this presumption. [FN172] If and when the presumption is rebutted, the directors' conduct is examined under the entire fairness standard, whereby the court scrutinizes the fairness of the process and the fairness of the price. [FN173]

Since the presumption of the business judgment rule presupposes that there has been an independent, disinterested decision maker, it does not apply where a director has a conflict of interests. [FN174] Where a director is tainted by self interest, the presumption of the business judgment rule is inapplicable and the burden of proof is effectively placed upon the defendant. The court becomes the "objective arbiter," [FN175] and the self-interested director must demonstrate that her conduct has been fair, which entails an analysis of whether the transaction was undertaken in a fair process and at a fair price. [FN176]

It has been through this analysis of fundamental fairness that plaintiffs have received protection from opportunistic conduct in connection with mergers. In VGS Inc. v. Castiel, [FN177] the Delaware Chancery Court held that two of three board members had breached their duty of loyalty to the plaintiff. [FN178] The two board directors had failed to notify the plaintiff of the proposed merger, which had the effect of ***1643** divesting the plaintiff of majority control of the business. [FN179] Because the directors were on both sides of the transaction, they had to establish that the merger was accomplished in a fair process and at a fair price. They failed to do so and the merger was enjoined. [FN180]

Similarly, in Solar Cells, mentioned above, the Delaware Chancery Court enjoined a merger at the request of an LLC member. [FN181] The court believed that the waiver of conflicts of interest did not extinguish all fiduciary duties. [FN182] In deciding the motion for preliminary injunction, the court determined that the defendants would be asked to prove the entire fairness of the merger. [FN183] Under this standard, it was unlikely that the defendants could establish that the merger was the product of fair dealing and that it offered a fair price. [FN184]

Thus, as illustrated in both VGS and Solar Cells, express squeeze-out strategies have been combated in Delaware through a rigorous application of the entire fairness test.

C. Resourceful Use of Contractually Based Standards to Build a Mandatory Core in Delaware

Restraints growing out of traditional contract law doctrines can serve as yet another potential source of restraint against predatory and opportunistic conduct by LLC members and/or managers. In Delaware, for example, the contractually based concept of "good faith" has the potential to become an important means of establishing a mandatory minimum for acceptable LLC manager and/or member conduct.

Many scholars have distinguished the fiduciary obligation from the contractual standard of good faith. Professor Deborah A. DeMott, for instance, has observed that the fiduciary obligation rests on the notion that the beneficiary is vulnerable to the exercise of the fiduciary's abuse of power, whereas the contractual standard proceeds on the assumption that the parties stand on a relatively level playing field and are bargaining at arms length. [FN185] She further points out that the ***1644** standard of good faith looks to how the parties actually perform the obligations in the contractual agreement, cannot be disclaimed, and does not prohibit self-interested conduct. [FN186] In contrast, the fiduciary obligation broadly commits the fiduciary to exercise discretion in the interests of the beneficiary, [FN187] generally prohibits self-interested conduct, [FN188] but may be susceptible to being limited. [FN189]

While academicians visualize the standard of good faith as residing on a significantly lower plane than that occupied by the fiduciary duty of loyalty, [FN190] the contractual obligation of good faith may nevertheless be an important mechanism through which the courts can police abusive conduct in the LLC context. For example, the standard of good faith was useful to justify enjoining the clandestine merger in Solar Cells, discussed above. [FN191] A contractual waiver of conflicts of interest was not interpreted as a waiver of all fiduciary duties, and the court observed that the operating agreement itself expressly contained a requirement that the managers act in good faith. [FN192] The court then proceeded to state that the defendant's actions did not appear to be those of fiduciaries acting in good faith. [FN193] The court believed that the defendants would be required to show the entire fairness of the proposed merger and did not believe they would be able to ***1645** sustain their burden of proof. [FN194] Therefore, the merger was enjoined. [FN195]

The court did not distinguish between good faith as an express contractual standard and good faith in a fiduciary sense. Whether meant in a contractual or fiduciary sense, the apparent bad faith of the defendants' conduct led to the finding that the predatory conduct should be enjoined.

IV. A Common Thread of Mandatory Duties Outside and Inside Delaware LLCs

The above discussion examines several decisions outside of Delaware that apply traditional concepts of partnership and/or corporate fiduciary duties to combat patterns of misconduct now emerging in the LLC. Despite mounting criticism, [FN196] these hardy fiduciary constructs successfully combated the majority's seizure of LLC real estate in Fine [FN197] and capably thwarted the unilateral estate planning restructuring in Flippo. [FN198] As the workhorse and backbone of business entity law, fiduciary constraints were well suited to attack a manager's usurpation of the LLC's business in Credentials Plus, [FN199] and were effective in preventing the clandestine formation of a new company that would exclude the minority in Anest. [FN200] Would Delaware's approach of scrutinizing self-interested conduct through the entire fairness test have achieved similar results, and if so, does it matter which approach is taken?

It could be argued that the entire fairness test would have produced similar results in Fine, for example, in which the managing owner essentially stole the LLC's real estate. It could have been argued that the defendant stood on both sides of the transaction and that the transaction lacked entire fairness. The same could have been said for the restructuring in Flippo and the clandestine, exclusionary ***1646** merger in Anest. In addition, a contractarian-minded court could have reached a similar result in Credentials Plus by using the contractually oriented standard of good faith.

Regardless of the specific legal doctrine used to combat opportunism, courts both outside and inside of Delaware are signaling that one is expected to behave in a trustworthy manner. Even within the context of a business entity governed by a private contract, the essential message is that there are social constraints and social responsibilities to others. At first blush, the broad policy statements exalting the freedom of contract in Delaware may create the impression of an LLC landscape without limits, but the recent statements by the Delaware Supreme Court in both partnership and corporate contexts, the application of the entire fairness test, and the concept of "good faith" illustrate that, within the contractarian environment, there is indeed a mandatory core of acceptable business conduct. However, the specific contours of fiduciary duties owed in Delaware LLCs have yet to be fully defined. Because Delaware does not recognize heightened fiduciary duties in close corporations, a valid concern is that the fiduciary protections in the context of the Delaware LLC might be narrow, stemming primarily either from contract or from the entire fairness test.

Many factors may make it more effective to curb opportunistic LLC conduct through a broad formulation of fiduciary duties than through contractual limitations or through a more focused scrutiny of self-interested conduct using the entire fairness test. A narrower contract-oriented approach to fiduciary duties may inappropriately serve the interests of the more affluent and may be unrealistic in terms of the practical usage of the LLC by certain members of the business community. Also, an expansive view of fiduciary duties may be preferable to a narrower approach if that better reflects positive ethical norms in the business community. Finally, a broader approach to fiduciary duties may be a more effective legal doctrine than a narrower conception of entire fairness in policing subtle freeze-outs.

In terms of the practical usage of the LLC, it is evident that some investors may be quite casual about drafting LLC agreements and, indeed, may not even have LLC operating agreements. [FN201] Others may simply select a form agreement themselves, in the interest of keeping ***1647** down organizational costs. [FN202] As a result, the contractarian approach of relying on contractual provisions to protect against opportunistic conduct may be more well suited to big business than to the work-a-day world of small business. The general partner of a real estate investment is likely to be represented by a national law firm. She may have engaged highly sophisticated attorneys and be in a position to tailor-make contracts. However, small business entities present an entirely different picture. The law should serve the needs of the full business community, including those with fewer financial resources who nevertheless make up an important sector of our economy. [FN203] While the attorney representing the real estate syndicator may well prefer a minimalist judicial posture, this preference may work at a distinct disadvantage to the smaller, less-sophisticated business owner whose legal counsel may be a general practitioner without a great deal of specialization in the nuances of LLC operating agreements. In a less-than-perfect world of private ordering, a balanced approach to fiduciary duties may be called for, which may necessitate judicial discretion.

A traditional endorsement of fiduciary duties may be preferable to a narrower, contract-oriented approach insofar as it sends a message to the business community that appropriate social behavior requires an entity and the individuals who compose it to conduct themselves in a trustworthy and honest manner, which means considering first and foremost, the welfare of the collective business unit rather than one's self-interest. [FN204] A broader statement of duties may better reflect society's norms of ethical behavior than a narrower formulation of

***1648** responsibilities. [FN205] On the other hand, if fiduciary duties are articulated in a manner that is overly broad and unduly protective of the minority, majority owners may be deterred from investing in enterprises with minority owners. Thus, the judicial and statutory legal environment must strive for a balanced approach that considers the interests of the majority as well as the interests of the minority. [FN206]

The entire fairness approach, entailing a fair price and fair process, may gloss over the nature and scope of damages and required remedies in the context of a small, owner-managed business enterprise. A fairness analysis may thus overlook the actual injuries sustained in a private business. As Professor Douglas K. Moll has articulated in his investment model of the corporation, the owner's entire investment in the firm must be considered, including the interest the owner has in employment, her work product, and her customer base. [FN207] In a privately owned business, the entrepreneur's investment in the business entity has tangible and intangible components. Fundamentally fair conduct, consisting of a buyout pursuant to a fair process and at a fair price, may not make one whole when one's interests in the enterprise are more complex, partly intangible, and/or nonmonetary. Thus, a broader and more flexible judicial approach may be necessary to properly identify the injuries in the context of the private business entity.

Also, on a practical level, the entire fairness test may not prove adequate to combat all types of freeze-outs and squeeze-outs that occur in a small, private business. As discussed by Professor Robert A. Ragazzo in the context of corporate squeeze-outs, the entire fairness test may be effective against overt freeze-outs, but may be difficult to apply to more subtle patterns of abuse in the LLC, such as failures to make distributions to the minority. [FN208] In private entities, decisions ***1649** concerning salaries, distributions, hiring, and firing could be tainted by self-interest. To be an effective tool in the private business setting, the entire fairness test might need extensive triggers. [FN209]

V. Adjusting the Contractarian Model to Accept Private Ordering with a Mandatory Minimum: The Role of the Court

The comparative analysis of the developing case law outside and inside Delaware, which is presented in Part IV, reveals the need to reevaluate the LLC's contractarian model. The contractarian paradigm is widely perceived as a theory that promotes the supremacy of the contract above all other values. However, experience with the LLC, as reflected by the various cases discussed, underscores the need for judicial monitoring of this type of business relationship. Courts recognize the importance of fiduciary duties, the significant role equitable principles play in mediating LLC disputes, the value of the law in promoting ethical standards of conduct, and the need to bridge the gap between legal theory and business practice.

Although academics have placed much emphasis on the Nixon decision in Delaware, [FN210] which failed to impose heightened fiduciary duties, less attention has been focused recently on long-standing endorsements of fiduciary duties both in other jurisdictions and in Delaware itself. It was the Delaware Supreme Court that stated in 1939:

> A public policy, existing through the years, and derived from a profound knowledge of human characteristics and motives, has established a rule that demands of a corporate officer or director, peremptorily and inexorably, the most scrupulous observance of his duty, not only affirmatively to protect the interests of the corporation committed to his charge, but also to refrain from doing anything that would work injury to the corporation, or to deprive it of profit or advantage which his skill and ***1650** ability might properly bring to it, or to enable it to make in the reasonable and lawful exercise of its powers. [FN211] Perhaps

the contractarian model should acknowledge the continuing relevance of fiduciary duties, the broader social context in which private business entities exist, and the wide array of mandatory legal constraints that apply even in our landscape of private ordering.

A. Recognizing the Need for Flexible Judicial Concepts Within the Contractarian Paradigm

As previously discussed, courts will intervene in the affairs of private business when fundamental notions of fairness have been violated. Courts have been willing to adapt a variety of behavioral standards to combat self-interested opportunistic conduct, whether it consists of fundamental changes, [FN212] unilateral asset transfers, [FN213] or sudden meetings that squeeze out another owner's interest. [FN214]

The critical role of the judiciary and the need for flexible judicial concepts and equitable doctrines is evident in emerging LLC case law, yet both are virtually lost, conceptually, in the contractarian model because of its emphasis on contractual freedom. As London School of Economics Professor C.A.E. Goodhart observed: "[F]or the law to ignore questions of equity is rather like asking Mrs. Lincoln whether she otherwise liked the play." [FN215] Professor Goodhart quite correctly goes on to point out that the law and economics approach seems, at times, to elevate the achievement of economic efficiency above concepts of justice and equity. [FN216]

***1651** Delaware Chief Justice E. Norman Veasey has stated that "[t]he defining tension in corporate governance today is the tension between deference to directors' decisions and the scope of judicial review." [FN217] At least with regard to private business entities, I suggest that the defining tension resides in the collision between a legislature that wants to constrain the judiciary in the interests of contractual freedom and an independent judiciary poised to promote fundamental notions of equity and fairness that every investor legitimately expects courts to protect. [FN218]

The courts are doing their job of enforcing the private bargain while also establishing equitable protections against unduly exploitative and deceptive conduct, whether through statements of fiduciary duties or by shifting the burden of proof to require a showing of fundamental fairness where the presumption of a disinterested, informed decision made in good faith has been rebutted. While some of the LLC decisions discussed above reflect discretionary judgments regarding violations of fiduciary duties, several cases illustrate judicial self-restraint. In these latter cases, courts have been willing to deny relief in order to enforce the contract between the parties, even though the enforcement appeared, on some level, to produce an unfair result.

Where the unfair result has occurred because the plaintiff entered into a poor bargain, a number of courts have refused to fashion broad remedies that change the outcome. For example, in Lieberman v. Wyoming.com LLC, [FN219] the Wyoming Supreme Court refused to order the defendants to repay more than the plaintiff's $20,000 capital contribution. In that case, the plaintiff withdrew from the LLC and demanded the fair market value of his interest in it. [FN220] The court, however, upheld the LLC operating agreement, which provided only for the return of capital contributions. [FN221] Although the case was remanded for further proceedings to establish whether the plaintiff in fact retained his ownership interest and/or was entitled to be paid interest on its fair market value, [FN222] the court failed to superimpose a solution that would have fashioned an equitable payment in settlement ***1652** of the dispute. Similarly, in Whitmore v. Hawkins, [FN223] the Fourth Circuit refused to require the defendants to pay plaintiff the fair market value of his interest in two LLCs upon his withdrawal because the applicable LLC operating agreements expressly stated that the involuntarily withdrawn member was not entitled to the fair market value of the interest if the LLCs were continued. [FN224] Likewise, courts have respected and enforced various other LLC operating agreements even where they have curtailed specific fiduciary duties, e.g., by permitting competition, [FN225] by denying the right to remove a manager, [FN226] or by providing work-in-progress payments to retiring or deceased members but not to withdrawing members. [FN227]

Although predictability and certainty are important policy goals that evolving statutory and judicial LLC law should embrace, the continuing occurrence of predatory and exploitative patterns of conduct seen in the close corporation and LLC settings illustrates the need for judicial flexibility and equitable concepts to combat conduct that violates fundamental notions of fair play.

Elastic concepts such as fiduciary duty are not out of place in a system designed to enforce contractual expectations within the business entity, but rather are the very backbone of our system of private ***1653** ordering. [FN228] Constructs that leave room for judicial discretion, such as fiduciary duties, unconscionability, and the contractual concept of good faith, are indispensable because they enable courts to police opportunistic conduct in something resembling a fair legal environment. [FN229]

As a practical matter, the LLC judicial and statutory environment must attempt to serve the interests of clarity and predictability, as well as the policy goals of achieving fairness and safety from opportunistic conduct. “Contextualists” claim that the most important thing in a legal system is for the laws to be flexible and fair, and to avoid arbitrariness. [FN230] “Neoformalists” argue that broad standards are problematic and believe that legislators should flesh out the law. [FN231] As noted by Robert A. Hillman, both the goals of fairness and predictability are important. [FN232] Legislators should try to make LLC statutes clear and predictable. However, legislators should not attempt to strip the judiciary of its rightful role of reviewing each case on its facts and applying equitable principles in its decision-making process. Finally, legislators should not presume that most members of the business community have made the costly investment to execute highly negotiated organizing documents. Well-developed statutory default rules (for those without elaborate LLC operating agreements) and safety valves, such as fiduciary duties, are needed to combat opportunistic conduct that has long plagued the private business enterprise.

Conclusion

The emerging body of LLC case law in Delaware and other states is recognizing a mandatory core of conduct, whether described in terms of partnership and/or corporate-style fiduciary duties, good faith, or the duty to show entire fairness. In one way or another the courts are embracing a mandatory core that is essential, particularly where there are gaps in the parties' agreements or where the parties stand in unequal positions. [FN233] These developments are positive, ***1654** although too much protection could become counterproductive if courts become too solicitous of minority interests.

The developing strains of business entity governance hold the promise of promoting the interest in contractual freedom while, at the same time, balancing the important need for minimum standards to protect legitimate expectations of fair and equitable conduct on the part of one's business partners. The contractarian model should acknowledge the need for and importance of such mandatory minimum standards to govern business relationships.

Regardless of how courts articulate their judicial tests, reverence for the written contract must be tempered with the recognition that judicial review is a good and essential thing, as is a mandatory core of acceptable manager and/or member conduct. It has been said that the “defining tension” in corporate governance today is the tension between deference to directors' decisions and the scope of judicial review. [FN234] In this debate, I have suggested that the uncertainty of the law, and the corresponding specter of judicial intervention, are not unfortunate consequences to be avoided by the creation of a perfect statutory phrase or judicial test. Rather, judicial review is the healthy price and the all-important force that deters overreaching and enables the application of behavioral constraints within the context of our contractual scheme of self-governance. [FN235] A broad approach to fiduciary duties is arguably preferable to a narrower test of entire fairness or a contractually oriented standard of good faith because it better reflects society's norms of ethical conduct, may be more effective in combating subtle freeze-out schemes, and does not rest on the assumption that the parties' relationship is governed by a highly negotiated and well-conceived contract.

***1655** Appendix A

States with LLC Statutes

State	Statutory Provisions
Alabama	Ala. Code §§ 10-12-1 to -61 (1999 & Supp. 2002)
Alaska	Alaska Stat. §§ 10.50.010-.995 (Michie 2002)
Arizona	Ariz. Rev. Stat. Ann. §§ 29-601 to -857 (West 1998 & Supp. 2003)
Arkansas	Ark. Code Ann. §§ 4-32-101 to -401 (Michie 2001 & Supp. 2003)
California	Cal. Corp. Code §§ 17,000-17,655 (West Supp. 2004)
Colorado	Colo. Rev. Stat. §§ 7-80-101 to -1101 (2003)
Connecticut	Conn. Gen. Stat. Ann. §§ 34-100 to -242 (West 1997 & Supp. 2003)
Delaware	Del. Code Ann. tit. 6, §§ 18-101 to -1109 (1999 & Supp. 2002)
District of Columbia	D. C. Code Ann. §§ 29-1001 to -1075 (2001 & Supp. 2003)
Florida	Fla. Stat. Ann. §§ 608.401-.705 (West 2001 &

	Supp. 2004)
Georgia	Ga. Code Ann. §§ 14-11-100 to -1109 (2003)
Hawaii	Haw. Rev. Stat. §§ 428-101 to -1302 (Supp. 2001)
Idaho	Idaho Code §§ 53-601 to -672 (Michie 2000 & Supp. 2003)
Illinois	805 Ill. Comp. Stat. Ann. 180/1-1 to /60-1 (West Supp. 2003)
Indiana	Ind. Code Ann. §§ 23-18-1-1 to -13-1 (West 1994 & Supp. 2003)
Iowa	Iowa Code Ann. §§490A.100-.1601 (West 1999 & Supp. 2003)
Kansas	Kan. Stat. Ann. §§17-7663 to -76,142 (Supp. 2002)
Kentucky	Ky. Rev. Stat. Ann. §§275.001-.455 (Michie Supp. 2003)
Louisiana	La. Rev. Stat. Ann. §§12:1301-:1369 (West 1994 & Supp. 2004)
Maine	Me. Rev. Stat. Ann. tit. 31, §§ 601-762 (West 1996 & Supp. 2003)
Maryland	Md. Code Ann., Corps. & Ass'ns §§ 4A-101 to -1103 (1999 & Supp. 2002)
Massachusetts	Mass. Ann. Laws ch. 156C, §§ 1-68 (Law. Co-op. 1996 & Supp. 2003)
Michigan	Mich. Comp. Laws Ann. §§ 450.4101-.5200 (West 2002 & Supp. 2003)
Minnesota	Minn. Stat. Ann. §§ 322B.01-.960 (West 1995 & Supp. 2004)

Mississippi	Miss. Code Ann. §§ 79-29-101 to -1204 (1999 & Supp. 2003)
Missouri	Mo. Ann. Stat. §§ 347.010-.740 (West 2001 & Supp. 2003)
Montana	Mont. Code Ann. §§ 35-8-101 to -1307 (2003)
Nebraska	Neb. Rev. Stat. §§ 21-2601 to -2653 (1997 & Supp. 2003)
Nevada	Nev. Rev. Stat. Ann. §§ 86.011-.590 (Michie 1999 & Supp. 2001)
New Hampshire	N. H. Rev. Stat. Ann. §§ 304-C:1 to:85 (1995 & Supp. 2003)
New Jersey	N. J. Stat. Ann. §§ 42:2B-1 to -70 (West Supp. 2003)
New Mexico	N. M. Stat. Ann. §§ 53-19-1 to -74 (Michie 2001 & Supp. 2003)
New York	N. Y. Ltd. Liab. Co. Law §§ 101-1403 (McKinney 2004)
North Carolina	N. C. Gen. Stat. §§ 57C-1-01 to -10-07 (2003)
North Dakota	N. D. Cent. Code §§ 10-32-01 to -156 (2001 & Supp. 2003)
Ohio	Ohio Rev. Code Ann. §§ 1705.01-.58 (Anderson 2001 & Supp. 2002)
Oklahoma	Okla. Stat. Ann. tit. 18, §§ 2000-2060 (West 1999 & Supp. 2004)
Oregon	Or. Rev. Stat. §§ 63.001-.990 (2003)
Pennsylvania	15 Pa. Cons. Stat. Ann. §§ 8901-8998 (West 1995 & Supp. 2003)

Rhode Island	R. I. Gen. Laws §§ 7-16-1 to -75 (1999 & Supp. 2003)
South Carolina	S. C. Code Ann. §§ 33-44-101 to -1207 (Law. Co-op. Supp. 2003)
South Dakota	S. D. Codified Laws §§ 47-34-1 to -34A-1207 (Michie 2000 & Supp. 2003)
Tennessee	Tenn. Code Ann. §§ 48-201-101 to -248-606 (2002 & Supp. 2003)
Texas	Tex. Rev. Civ. Stat. Ann. art. 1528n, §§ 1.01-11.07 (Vernon 2003 & Supp. 2004)
Utah	Utah Code Ann. §§ 48-2c-101 to -1902 (2002)
Vermont	Vt. Stat. Ann. tit. 11, §§ 3001-3162 (1997 & Supp. 2003)
Virginia	Va. Code Ann. §§ 13.1-1000 to -1123 (Michie 1999 & Supp. 2003)
Washington	Wash. Rev. Code Ann. §§ 25.15.005-.902 (West Supp. 2004)
West Virginia	W. Va. Code Ann. §§ 31B-1-101 to -13-1306 (Michie 2003)
Wisconsin	Wis. Stat. Ann. §§ 183.0102-.1305 (West 2002 & Supp. 2003)
Wyoming	Wyo. Stat. Ann. §§ 17-15-101 to -147 (Michie 2003)

***1658** Appendix B

Table 1: LLC Statutes Using Good Faith Prudent Person Language [FNa1]

State	Statutory Provision
Alaska	Alaska Stat. § 10.50.135(a) (Michie 2002)
Colorado	Colo. Rev. Stat. § 7-80-406(a) (2003)
Connecticut	Conn. Gen. Stat. Ann. § 34-141(a) (West 1997)
Georgia	Ga. Code Ann. § 14-11-305(1) (2003)
Iowa	Iowa Code Ann. §490A.706(1) (West 1999)
Louisiana	La. Rev. Stat. Ann. §12:1314(A)(1) (West 1994 & Supp. 2004)
Maine	Me. Rev. Stat. Ann. tit. 31, § 652(1) (West 1996)
Michigan	Mich. Comp. Laws Ann. § 450.4404(1) (West 2002)
Minnesota	Minn. Stat. Ann. § 322B.69 (West 1995)
Mississippi	Miss. Code Ann. § 79-29-402(1) (1999)
Missouri	Mo. Ann. Stat. § 347.088(1) (West 2001)
New York	N. Y. Ltd. Liab. Co. Law § 409(a) (McKinney 2004)

North Carolina	N. C. Gen. Stat. § 57C-3-22(b) (2003)
North Dakota	N. D. Cent. Code § 10-32-96 (2001 & Supp. 2003)
Ohio	Ohio Rev. Code Ann. § 1705.29(B) (Anderson 2001)
Oklahoma	Okla. Stat. Ann. tit. 18, § 2016(1) (West 1999 & Supp. 2004)
Pennsylvania	15 Pa. Cons. Stat. Ann. §§ 8943, 1712(a) (West 1995 & Supp. 2003)
Rhode Island	R. I. Gen. Laws § 7-16-17(a) (1999)
Tennessee	Tenn. Code Ann. §§ 48-239-115(a), -241-111(a) (2002)
Vermont	Vt. Stat. Ann. tit. 11, § 3059(c) (1997)
Virginia	Va. Code Ann. § 13.1-1024.1 (Michie 1999)

***1659** Table 2: LLC Statutes Using Gross Negligence or Willful Misconduct Language

State	Statutory Provisions
Alabama	Ala. Code § 10-12-21(g), (k)(2) (1999)
Arkansas	Ark. Code Ann. § 4-32-402 (Michie 2001 &

	Supp. 2003)
California	Cal. Corp. Code § 17,153 (West Supp. 2004)
District of Columbia	D. C. Code Ann. § 29-1003 (2001)
Florida	Fla. Stat. Ann. § 608.4225(1)(b) (West 2001 & Supp. 2004)
Hawaii	Haw. Rev. Stat. § 428-409(c) (Supp. 2001)
Idaho	Idaho Code § 53-622(1) (Michie 2000)
Illinois	805 Ill. Comp. Stat. Ann. 180/15-3 (West Supp. 2003)
Indiana	Ind. Code Ann. § 23-18-4-2 (West 1994)
Kentucky	Ky. Rev. Stat. Ann. § 275.170(1) (Michie Supp. 2003)
Montana	Mont. Code Ann. § 35-8-310(3) (2003)
New Hampshire	N. H. Rev. Stat. Ann. § 304-C:31(IV) (1995)
New Mexico	N. M. Stat. Ann. § 53-19-16(B) (Michie 2001)
Oregon	Or. Rev. Stat. § 63.155(3) (2003)

South Carolina	S. C. Code Ann. § 33-44-101 to -1207 (Law. Co-op. Supp. 2003) ....
Utah	Utah Code Ann. § 48-2c-807(1) (2002) ....
Washington	Wash. Rev. Code Ann. § 25.15.155(1) (West Supp. 2004) ....
West Virginia	W. Va. Code Ann. § 31B-4-409(c) (Michie 2003) ....
Wisconsin	Wis. Stat. Ann. § 183.0402(1) (West 2002) ....

[FNd1]. Associate Professor, Widener University School of Business Administration. I would like to thank Dean and Professor Donald J. Weidner, Florida State University College of Law, as well as Professors Barbara Ann Banoff, James Rossi, Mark Seidenfeld, and the other faculty members at Florida State University College of Law, who offered helpful comments when I presented an outline of this Article at Florida State University College of Law earlier this year. I am grateful to Elizabeth Stone Miller for reading a draft of this Article and would like to give special thanks to Kenneth Miller for his many insights and editorial suggestions.

[FN1]. See Classification of Certain Business Entities 26 C.F.R. § 301.7701-3 (2001) (permitting the LLC to elect its classification for federal tax purposes); Laurel Wheeling Farrar & Susan Pace Hamill, Dissociation from Alabama Limited Liability Companies in the Post Check-the-Box Era, 49 Ala. L. Rev. 909, 912-13 (1998) (highlighting the increased flexibility afforded by the Internal Revenue Service to structure LLCs like corporations with continuity of life and remarking on an amendment in Alabama's LLC statute that eliminates the possibility of dissolution or dissociation even if members die or leave the LLC); see also Conrad S. Ciccotello & C. Terry Grant, LLCs and LLPs: Organizing to Deliver Professional Services, Bus. Horizons, Mar.-Apr. 1999, at 85, 85 (“Nearly 25 times as many new LLC registrations occurred in 1996 as in 1992.”). See generally Thomas M. Hayes, Note, Checkmate, the Treasury Finally Surrenders: The Check-the-Box Treasury Regulations and Their Effect on Entity Classification, 54 Wash. & Lee L. Rev. 1147, 1160-68 (1997) (detailing the changes to the tax entity classification rules).

[FN2]. See Susan Pace Hamill, The Limited Liability Company: A Catalyst Exposing the Corporate Integration Question, 95 Mich. L. Rev. 393, 394-96 (1996) (discussing the LLC's partnership-style benefits of pass-through taxation and limited liability and noting concerns that the LLC could pose a serious challenge to the double taxation regime, which taxes corporate profits both when the corporation earns them and when they are distributed to the shareholders).

[FN3]. See Liability Awards Are on the Rise, Corp. Leg. Times, June 2000, at 22, 22 (indicating that national jury awards in most liability suits have risen significantly).

[FN4]. See Dale A. Oesterle, Subcurrents in LLC Statutes: Limiting the Discretion of State Courts to Restructure the Internal Affairs of Small Business, 66 U. Colo. L. Rev. 881, 881 (1995) (discerning a movement among some tort reformers to expand the role of the LLC as a potential solution to excessive liability); cf. James A. Henderson, Jr., The Boundary Problems of Enterprise Liability, 41 Md. L. Rev. 659, 662-76 (1982) (suggesting a list of liability triggers to provide increased certainty in the law).

[FN5]. See Oesterle, supra note 4, at 883 (observing that state legislatures' push to "relax judicial supervision of small businesses" was a leading factor in the rise of the LLC); see also Donald J. Weidner, Three Policy Decisions Animate Revision of Uniform Partnership Act, 46 Bus. Law. 427, 428 (1991) (articulating practitioners' concern with certainty of the law and their fear that their clients' contractually negotiated business deals could be undone by "fuzzy" notions of fiduciary duty).

[FN6]. Infra Appendix A.

[FN7]. See Ann E. Conaway Stilson, The Agile Virtual Corporation, 22 Del. J. Corp. L. 497, 518 (1997) (recognizing that "the present trend in LLC ... legislation reflects an attitude favoring maximum freedom of contract among LLC ... participants"). See generally Carter G. Bishop & Daniel S. Kleinberger, Limited Liability Companies (1996) (offering a comprehensive treatise on LLCs nationwide); Larry E. Ribstein & Robert R. Keatinge, Ribstein and Keatinge on Limited Liability Companies (2002) (rendering a detailed analysis of LLCs and containing indices that categorize the manner in which states approach various issues of operation from formation to dissolution).

[FN8]. See Larry E. Ribstein, The Deregulation of Limited Liability and the Death of Partnership, 70 Wash. U. L.Q. 417, 425-38 (1992) (providing insight into the history of the LLC and its goal of offering partnership-like flexibility through the primacy of the LLC operating agreement).

[FN9]. See, e.g., Cal. Corp. Code § 17,153 (West Supp. 2004) (indicating that the fiduciary duties a manager owes to the LLC and its members are those of a partner to a partnership and to the partners of the partnership); Fla. Stat. Ann. § 608.4225 (West 2001 & Supp. 2004) (outlining the duties of loyalty and care); N.Y. Ltd. Liab. Co. Law § 409 (McKinney 2004) (mandating that a manager perform her duties "in good faith and with that degree of care that an ordinarily prudent person in a like position would use under similar circumstances"); 15 Pa. Cons. Stat. Ann. § 8943(b) (West 1995 & Supp. 2003) (adopting a corporate standard of care for LLCs with managers).

[FN10]. See Del. Code Ann. tit. 6., § 18-1101(b) (1999) (deferring to the freedom of contract).

[FN11]. Id.

[FN12]. See Jack B. Jacobs, Entity Rationalization: A Judge's Perspective, 58 Bus. Law. 1043, 1044-46 (2003) (discussing the astonishingly large volume of litigation created by alternative entity forms, including LLCs, in Delaware); Sandra K. Miller, A New Direction for LLC Research in a Contractarian Legal Environment, 76 S. Cal. L. Rev. 351, 396 (2003) (observing a particularly high rate of litigation with majority/minority LLC disputes in Delaware).

[FN13]. See, e.g., VGS, Inc. v. Castiel, No. 17995, 2000 Del. Ch. LEXIS 122, at *13-14 (Del. Ch. Aug. 31,

2000) (holding that two of three LLC board members breached their fiduciary duties by failing to notify a third board member of a proposed merger); see also Solar Cells, Inc. v. True N. Partners, LLC, No. 19477, 2002 Del. Ch. LEXIS 38, at *18-19 (Del. Ch. Apr. 25, 2002) (deciding that a merger should be enjoined as an unfair transaction where defendants unilaterally structured the terms that would dilute plaintiff's ownership and voting rights).

[FN14]. See, e.g., Lynch Multimedia Corp. v. Carson Communications, L.L.C., 102 F. Supp. 2d 1261, 1261-62 (D. Kan. 2000) (claiming that other LLC member companies breached their fiduciary duties by independently acquiring other cable franchises).

[FN15]. See, e.g., Anest v. Audino, 773 N.E.2d 202, 210 (Ill. App. Ct. 2002) (alleging that defendant breached his fiduciary duty as a fellow member of the LLC by failing to present plaintiff with the opportunity to enter into an exclusive distributorship agreement that was offered to the LLC), appeal denied, 787 N.E.2d 154 (Ill. 2002).

[FN16]. See, e.g., Flippo v. CSC Assocs. III, 547 S.E.2d 216, 221-22 (Va. 2001) (affirming court's ruling that defendant breached his fiduciary duty to plaintiff by transferring assets to a new entity to achieve personal estate planning goals).

[FN17]. See, e.g., Fine v. Bork, No. 010808586, 2002 Conn. Super. LEXIS 181, at *2-4 (Conn. Super. Ct. Jan. 15, 2002) (involving a unilateral amendment to an LLC operating agreement allowing the LLC to be owned by one member and a subsequent dissolution of the LLC resulting in a squeeze-out of the minority); see also Credentials Plus, LLC v. Calderone, 230 F. Supp. 2d 890, 893-94, 896-900 (N.D. Ind. 2002) (concerning a breach of fiduciary duty where the minority LLC manager quit working for the LLC and started her own company, taking the LLC's business with her). See generally 2 F. Hodge O'Neal & Robert B. Thompson, O'Neal's Close Corporations § 9.02 (3d ed. Supp. 2003) (discussing the problems of dissension, oppression, and deadlock in the context of close corporations).

[FN18]. See John C. Coffee, Jr., The Mandatory/Enabling Balance in Corporate Law: An Essay on the Judicial Role, 89 Colum. L. Rev. 1618, 1618-23 (1989) (identifying the clash between the policy interest in contractual freedom and the competing interest in a mandatory core of corporate regulation).

[FN19]. Regarding the judicial role in private agreements, Professor John C. Coffee states:

[A]n exclusive focus on economics ignores an important feature common to all forms of long-term relational contracts: namely that courts have invariably played an active and indispensable role in monitoring and interpreting such agreements. Indeed, the feasibility of such contracting probably depends upon the parties' ability to rely upon the courts to play such a role.

Id. at 1620-21 (footnote omitted); see also Deborah A. DeMott, Fiduciary Obligation Under Intellectual Siege: Contemporary Challenges to the Duty to Be Loyal, 30 Osgoode Hall L.J. 471, 484 (1992) (observing that "contract law itself includes mandatory rules not subject to being trumped or ousted by the parties' agreement").

[FN20]. See, e.g., Fine, 2002 Conn. Super. LEXIS 181, at *2-4 (concerning a majority shareholder that changed the terms of the LLC without the minority's knowledge or consent).

[FN21]. See, e.g., Flippo, 547 S.E.2d at 219-20 (involving two of three shareholders selling their interests to a separate company in order to force a dissolution of the LLC).

[FN22]. See, e.g., VGS, Inc. v. Castiel, No. 17995, 2000 Del. Ch. LEXIS 122, at *5 (Del. Ch. Aug. 31, 2000) (regarding the failure to notify a board member of a proposed merger that had the effect of divesting that member of his majority control of the business).

[FN23]. See, e.g., Credentials Plus, LLC v. Calderone, 230 F. Supp. 2d 890, 899-900 (N.D. Ind. 2002) (concluding that the solicitation of a previous LLC/employer's business opportunities while retaining shares in that LLC was a breach of fiduciary duties).

[FN24]. See generally Margaret M. Blair & Lynn A. Stout, Trust, Trustworthiness, and the Behavioral Foundations of Corporate Law, 149 U. Pa. L. Rev. 1735, 1738-43 (2001) (noting and examining the social context of trustworthy behavior and stressing the behavioral dimensions of corporate law).

[FN25]. See Bishop & Kleinberger, supra note 7, P 7.02(1) (stating that “under all but one enabling statute the statutory structure is a default rule,” and suggesting that, even under a mandatory regime, an LLC's operating agreement could substantially affect an LLC's management structure).

[FN26]. See Douglas M. Branson, Assault on Another Citadel: Attempts to Curtail the Fiduciary Standard of Loyalty Applicable to Corporate Directors, 57 Fordham L. Rev. 375, 381-82 (1988) (indicating that, for the most part, other states have followed Delaware's lead by permitting corporations to opt out of liability for violations by their officials); Coffee, supra note 18, at 1619 (discussing the central role played by courts in monitoring and interpreting agreements in the corporate setting); Harvey Gelb, Director Due Care Liability: An Assessment of the New Statutes, 61 Temp. L. Rev. 13, 28-32 (1988) (reviewing statutory efforts to alleviate director concerns about liability for due care violations).

[FN27]. 488 A.2d 858, 859 (Del. 1985) (directing the Delaware Chancery Court to award damages where the members of a board of directors were not entitled to the presumption that their business decision was an informed one).

[FN28]. See Del. Code Ann. tit. 8, § 102(b)(7) (2001); Stephen A. Radin, The Director's Duty of Care Three Years After Smith v. Van Gorkom, 39 Hastings L.J. 707, 744-54 (1988) (analyzing the statutory response to the Van Gorkom decision). Delaware passed the first authoritative provision that allowed the articles of incorporation to limit or even exclude corporate directors' liability for any breach of duty of care provided that the provision did not eliminate or limit the liability for a breach of loyalty, for acts or omissions not in good faith or involving intentional misconduct, or for transactions from which the director derived improper personal benefits. Branson, supra note 26, at 380-82. Other states have for the most part followed Delaware's lead by permitting corporations to opt out of liability for violations by their officials. Id.

[FN29]. See Revised Unif. P'ship Act §§ 103(b), 404(a) (1997) (limiting partners' duties to the duty of loyalty and the duty of care, although restricting the ability of the partnership agreement to eliminate the duty of loyalty, unreasonably reduce the duty of care, or remove the obligations of good faith and fair dealing); see also Dennis Hynes, Fiduciary Duties and RUPA: An Inquiry into Freedom of Contract, Law & Contemp. Probs., Spring 1995, at 29, 34-35 (noting that the drafters of RUPA attempted to deny the courts the power to create new and different fiduciary duties); id. app. B (listing the states and territories that have adopted the revisions). See generally Gerard C. Martin, Comment, Duties of Care Under the Revised Uniform Partnership Act, 65 U. Chi. L. Rev. 1307 (1998) (providing an excellent analysis of the standard of care under RUPA).

[FN30]. See Unif. Ltd. Liab. Co. Act § 103 (1996) (following the RUPA approach to utilizing the statute in default of an agreement to the contrary, but arguably taking a more middle-of-the road approach by limiting the

LLC agreement's ability to unreasonably restrict access to information, eliminate the duty of loyalty, unreasonably reduce the duty of care, or eliminate the obligation of good faith and fair dealing); see also Nat'l Conference of Comm'rs on Unif. State Laws, A Few Facts About the Uniform Limited Liability Company Act, at http://www.nccusl.org/nccusl/uniformact_factsheets/uniformacts-fs-ullca.asp (last visited Feb. 23, 2004) (indicating that ULLCA has been adopted by Alabama, Hawaii, Illinois, Montana, South Carolina, South Dakota, U.S. Virgin Islands, Vermont, and West Virginia).

[FN31]. See Revised Unif. P'ship Act § 103(a) (establishing the authority of RUPA to govern absent a partnership agreement to the contrary); Unif. Ltd. Liab. Co. Act § 104 (explaining that an operating agreement may modify or eliminate any rule except those matters specified in section 104(b) and providing in part that "[t]o the extent not otherwise mentioned in subsection (b), every section of [the] Act is simply a default rule, regardless of whether the language of the section appears to be otherwise mandatory"); Hynes, supra note 29, at 34-35 (examining RUPA's efforts to enhance freedom of contract by "keep[ing] the list of mandatory duties as narrow as possible," but acknowledging the fact that RUPA does not give complete freedom to waive fiduciary duties).

[FN32]. See, e.g., Cal. Corp. Code § 17,005 (West Supp. 2004) (providing that California's LLC statute governs relations among members "[t]o the extent the articles of organization or operating agreement do not otherwise provide," but also placing some restrictions on the use of such private provisions); Del. Code Ann. tit. 6, § 18-305 (1999 & Supp. 2002) (outlining members' and managers' rights to access LLC information but stating that the rights as provided may be restricted in the operating agreement); N.Y. Ltd. Liab. Co. Law § 402 (McKinney 2004) (setting forth rules for voting rights to be applied "[e]xcept as provided in the operating agreement"); 15 Pa. Cons. Stat. Ann. § 8942 (West 1995 & Supp. 2003) (establishing voting rules to be followed except as provided in the operating agreement); see also Ribstein & Keatinge, supra note 7, apps. 5-1, 7-1 (containing chart summaries of state default allocation rules for profits, losses, and distributions, and waivers of fiduciary duties).

[FN33]. Del. Code Ann. tit. 6, § 18-1101(b) (1999); see also § 18-108 (permitting an LLC to have the power to "indemnify and hold harmless any member or manager or other person from and against any and all claims and demands whatsoever"); Walker v. Res. Dev. Co., 791 A.2d 799, 813 (Del. Ch. 2000) (indicating that the basic approach of the Delaware LLC Act is to confer broad discretion in drafting the LLC operating agreement and that, once members exercise this discretion, the specific terms of the agreement can then be enforced). A few other states have adopted similar "freedom of contract" language. See, e.g., Ga. Code Ann. § 14-11-1107(b) (2003); Idaho Code § 53-668(1) (Michie 2000); N.M. Stat. Ann. § 53-19-65A (Michie 2001).

[FN34]. See Prototype Ltd. Liab. Co. Act §§ 402, 404 (1993) (permitting the LLC agreement to eliminate or limit liability for breaches of fiduciary duties and allowing indemnification of members or managers).

[FN35]. See Branson, supra note 26, at 395 n.95 (conceiving the firm as "nothing more than a 'nexus' or 'web' 'of contracts' among providers of capital, managers, lenders, labor, suppliers and consumers").

[FN36]. See id. at 394 (stating that under the contractarian approach, "corporate law's only function should be to facilitate citizens' organization of their business affairs at the lowest possible cost"). But see Coffee, supra note 18, at 1619-20 (emphasizing the importance of the judicial role in monitoring and interpreting the corporate contract); see also Scott FitzGibbon, Fiduciary Relationships Are Not Contracts, 82 Marq. L. Rev. 303, 305 (1999) (asserting that fiduciary relationships "arise and function in ways alien to contractualist thought," particularly in that they "facilitate the doing of justice,... promote virtue, and... enhance freedom").

[FN37]. See Donald J. Weidner, A Perspective to Reconsider Partnership Law, 16 Fla. St. U. L. Rev. 1, 38 (1988) (suggesting that reforms of the Uniform Partnership Act should focus on the duties of loyalty and care); Weidner, supra note 5, at 462 (theorizing that RUPA § 21(b) was "motivated in part by a sense that vague, broad statements of a powerful duty of loyalty cause too much uncertainty"); see also Donald J. Weidner, RUPA and Fiduciary Duty: The Texture of Relationship, Law & Contemp. Probs., Spring 1995, at 81, 86 (observing that RUPA offers "an attempt to add more determinacy to language that is often indeterminate"). But see Allan W. Vestal, Fundamental Error in the Revised Uniform Partnership Act of 1992, 73 B.U. L. Rev. 523, 536-37 (1993) (arguing that RUPA is incapable of adapting to new and evolving situations, defeats participants' reasonable expectations, and sends the wrong societal message).

[FN38]. See Stephen M. Bainbridge, Director Primacy: The Means and Ends of Corporate Governance, 97 Nw. U. L. Rev. 547, 547-48 (2003) (remarking upon the increased role that economics has played in business law since Ronald H. Coase's famous article, The Nature of the Firm, 4 Economica (N.S.) 386 (1937), and tracing contractarian theory back to that article); see also Robert Goddard, Enforcing the Hypothetical Bargain: Sections 459-461 of the Companies Act 1985, 20 Company Law. 66, 66-67 (1999) (discussing the remedy for unfairly prejudicial conduct under United Kingdom law and the theoretical framework of the contractarian view of the business entity).

[FN39]. Goddard, supra note 38, at 67-68.

[FN40]. See Thomas Lee Hazen, The Corporate Persona, Contract (and Market) Failure, and Moral Values, 69 N.C. L. Rev. 273, 275-76 (1991) (discussing the attack by the Chicago School of Economics on the contract model of corporate governance).

[FN41]. See Claire Moore Dickerson, Equilibrium Destabilized: Fiduciary Duties Under the Uniform Limited Liability Company Act, 25 Stetson L. Rev. 417, 453-55 (1995) (explaining contractarian theory but criticizing its cost-sensitive approach to fiduciary duties). See generally O'Neal & Thompson, supra note 17 (providing an exhaustive treatise on the legal issues commonly encountered by the privately owned corporation).

[FN42]. See Dickerson, supra note 41, at 454-55 (analyzing the contractarian view of relationships and concluding that this perspective "still neglects actual harm that can be suffered when fiduciary duties are not mandatory").

[FN43]. See Daniel R. Fischel, The "Race to the Bottom" Revisited: Reflections on Recent Developments in Delaware's Corporation Law, 76 Nw. U. L. Rev. 913, 944 (1982) (observing that corporate law has little role to play "[a]part from minimizing transaction costs and possibly facilitating the operation of market forces that discipline management").

[FN44]. See Larry E. Ribstein, Bubble Laws, 40 Hous. L. Rev. 77, 97 (2003) (suggesting that deregulation, rather than increased regulation, may be the answer to misconduct involving over-hyping, inadequate disclosure, or flimsy capital structures).

[FN45]. See Christopher A. Riley, Contracting Out of Company Law: Section 459 of the Companies Act 1985 and the Role of the Courts, 55 Mod. L. Rev. 782, 789 (1992) (arguing that shareholders of small companies are denied the protection that contractarians see in the market for corporate control because private companies are not traded).

[FN46]. See Miller, supra note 12, at 394-95 (reporting the results of a survey of 770 practitioners and their experience working with LLCs in California, Delaware, New York, and Pennsylvania and observing that 50% of Delaware practitioners who had handled minority disputes said that a lawsuit had been filed, while only 21%, 9%, and 25% indicated that suits had been instituted in California, New York, and Pennsylvania, respectively). See generally James R. Burkhard, LLC Member and Limited Partner Breach of Fiduciary Duty Claims: Direct or Derivative Actions?, 7 J. Small & Emerging Bus. L. 19, 45-51 (2003) (addressing LLC litigation and the question of whether a breach of fiduciary duty should be brought as a direct or derivative suit).

[FN47]. Miller, supra note 12, at 394-95.

[FN48]. Jacobs, supra note 12, at 1044-45.

[FN49]. See Barbara Ann Banoff, Company Governance Under Florida's Limited Liability Company Act, 30 Fla. St. U. L. Rev. 53, 79-80 (2002) (observing that the unsophisticated LLC owner (the "do-it-yourselfer") may be unpleasantly surprised by the lack of a default buyout rule in the revised Florida LLC statute); see also Comm. on Corporate Laws, ABA Section of Bus. Law, Managing Closely Held Corporations: A Legal Guidebook (2003), reprinted in 58 Bus. Law. 1073, 1077-1126 (2003) (providing some direction and guidance to non-lawyers by offering "a concise, practical overview of important legal principles governing directors, officers and shareholders of closely held corporations").

[FN50]. For background on the Enron collapse, see Kurt Eichenwald & Diana B. Henriques, Enron Buffed Image to a Shine Even as It Rotted from Within, N.Y. Times, Feb. 10, 2002, at 1 (detailing the company's use of alternative entities to hide debt); Wendy Zellner, The Fall of Enron, Bus. Wk., Dec. 17, 2001, at 30 (indicating that Enron had about $20 billion of undisclosed off-balance-sheet partnership debt for which it was liable). There is much debate over the appropriate regulatory response to the Enron collapse. See, e.g., Faith Stevelman Kahn, Bombing Markets, Subverting the Rule of Law: Enron, Financial Fraud, and September 11, 2001, 76 Tul. L. Rev. 1579, 1615 (2002) (arguing for a more activist approach to corporate regulation despite the prevailing sentiment among academics and practitioners that regulatory minimalism promotes profitability and economic efficiency); David Millon, Why is Corporate Management Obsessed with Quarterly Earnings and What Should Be Done About It?, 70 Geo. Wash. L. Rev. 890, 913 (2002) (discussing the need to remove the legal structures that fuel management's drive to meet analysts' expectations); Robert B. Thompson, Corporate Governance After Enron, 40 Hous. L. Rev. 99, 107-11 (2003) (questioning why the states did not do more in response to the severity of the governance problems exposed after Enron and observing that state corporate statutes provide only minimal control over corporate power by subjecting directors to judicially imposed fiduciary duties while leaving the markets to regulate everything else). But see Ribstein, supra note 44, at 89 (criticizing the Sarbanes-Oxley Act as "regulat[ion] in a panic" that "ignored potential market solutions to corporate fraud"); Larry E. Ribstein, Market vs. Regulatory Responses to Corporate Fraud: A Critique of the Sarbanes-Oxley Act of 2002, 28 J. Corp. L. 1, 61 (2002) (suggesting that "[m]arkets are capable of responding more quickly and precisely than regulation to corporate fraud").

[FN51]. Vestal, supra note 37, at 539-40 (quoting Chiles v. Robertson, 767 P.2d 903, 912 (Or. Ct. App. 1989)).

[FN52]. See Sandra K. Miller, What Standards of Conduct Should Apply to Members and Managers of Limited Liability Companies?, 68 St. John's L. Rev. 21 (1994) (comparing partnership, corporate, and agency standards of conduct as possible precedents for LLC standards of conduct); see generally Sandra K. Miller, What Buy-out Rights, Fiduciary Duties, and Dissolution Remedies Should Apply in the Case of the Minority Owner of a Limited Liability Company?, 38 Harv. J. on Legis. 413 (2001) (discussing the need to provide corporate buyout rights to minority LLC members).

[FN53]. See Jacobs, supra note 12, at 1044 (arguing that courts have to develop an entirely new predicate layer of analysis that requires the court to decide which set of principles--"fiduciary law, contract law, or a combination of both"--apply in a particular case).

[FN54]. See Tamar Frankel, Fiduciary Law, 71 Cal. L. Rev. 795, 800 (1983) (noting that in the fiduciary relation, one party, the entrustor, is dependent upon the other party, the fiduciary).

[FN55]. See id. at 801 (describing how a fiduciary may "enter into a fiduciary relation without regard to his own needs").

[FN56]. See Victor Brudney, Contract and Fiduciary Duty in Corporate Law, 38 B.C. L. Rev. 595, 624-25 (1997) (indicating that in the case of trusts, principal and agent relationships, and corporate management, the fiduciary must act for the beneficiary's exclusive benefit, and that in the case of partnership or corporate controllers, the fiduciary must act for the beneficiary's shared benefit in proportions designated ex ante).

[FN57]. See 1 Principles of Corporate Governance: Analysis and Recommendations 137 (1994) (indicating that the legal obligations of directors and officers have been traditionally divided into the categories of duty of care and duty of loyalty); see also Bishop & Kleinberger, supra note 7, PP 10.01[1][a]-[b] (providing an overview of fiduciary duties in the LLC and discussing the components of duty of care and duty of loyalty); Ribstein & Keatinge, supra note 7, §§ 9.10-.11 (comparing the duties of LLC managers with the corporate and partnership duty of care and duty of loyalty); cf. Paul M. Altman et al., Contractually Defining Duties of General Partners in Delaware Limited Partnerships, 19 A.B.A. Sec. Bus. L. Newsl. Comm. on Partnerships & Unincorporated Bus. Orgs. 8, 8 (2002) (offering an overview of general partners' fiduciary duties).

[FN58]. 1 Principles of Corporate Governance, supra note 57, at 137.

[FN59]. Id. (noting that the duty of loyalty entails the commitment of allegiance to the enterprise such that the best interests of the corporation and shareholders must prevail over individual interests).

[FN60]. Prototype Ltd. Liab. Co. Act § 402(A) (1993). The Business Law Section of the American Bar Association is currently working on a revision of PLLCA. Also, the National Conference of Commissioners on Uniform State Laws is in the process of revising ULLCA.

[FN61]. See Unif. Ltd. Liab. Co. Act § 409(c) (1996) (stating that a partner's duty of care is to refrain from engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law).

[FN62]. In particular, PLLCA provides the following commentary to section 402(A):

> Subsection (A) sets forth the gross negligence standard of care for those participating in management. This is similar to the standard commonly applied to corporate directors, managing partners, or general partners of limited partnerships. In general, as long as managers avoid self-interested and grossly negligent conduct, their actions are protected by the business judgment rule.

Prototype Ltd. Liab. Co. Act § 402(A); see also Ribstein & Keatinge, supra note 7, app. 9-1 (summarizing the various standards of care by state).

[FN63]. See Del. Code Ann. tit. 6, § 18-1101 (1999) (providing no express standards of conduct for members and managers but indicating that an operating agreement may expand or restrict any duties at law or equity); Tex. Bus. Corp. Act Ann. arts. 2.12-.20 (1999) (containing rules pertaining to managers but failing to specify a standard of care). Other states that fail to provide a statutory duty of care include Arizona, Kansas, Nebraska, Nevada, South Dakota, Utah and Wyoming. Thomas A. Humphreys, Limited Liability Companies § 4.02(3) n.55 (1998).

[FN64]. For a list of statutes taking this approach, see infra Appendix B tbl.2.

[FN65]. See Mod. Bus. Corp. Act § 8.30 (rev. 2002) (mandating that directors act "(1) in good faith, and (2) in a manner the director reasonably believes to be in the best interests of the corporation"). For a list of statutes adopting this type of language, see infra Appendix B tbl.1. See also Bishop & Kleinberger, supra note 7, P 10-16 (sorting the duty of care provisions into five categories); Ribstein & Keatinge, supra note 7, app. 9-1 (containing a chart categorizing the standards of care in different states).

[FN66]. See, e.g., Colo. Rev. Stat. § 7-80-406 (1999) (identifying the duties and standards for managers but not specifying explicit standards for members).

[FN67]. See, e.g., Alaska Stat. § 10.50.130 (Michie 2002) (providing that unless otherwise provided in the operating agreement, the member does not have the fiduciary duty of a manager); Ark. Code Ann. § 4-32-402 (Michie 1997) (containing no statements about the duty of good faith or loyalty); Del. Code Ann. tit. 6, § 18-1101 (1999 & Supp. 2002) (avoiding any statement on fiduciary duties by indicating that, "to the extent that, at law or in equity, a member or manager or other person has duties (including fiduciary duties) and liabilities," any such person shall not be liable for the good faith reliance on the provisions of the LLC agreement, and the duties and liabilities may be expanded or restricted by the agreement); D.C. Code Ann. § 29-1021 (2001) (containing no restrictions on transactions between members or managers and the LLC).

[FN68]. See Ala. Code § 10-12-21(f) (1999) (indicating that a member's duty of loyalty in a member-managed LLC is limited to (1) accounting and holding as trustee any of the LLC's property, profit, or benefit including the appropriation of the LLC's opportunity, (2) refraining from dealing with the LLC as or on behalf of a party having an adverse interest, and (3) refraining from competing with the LLC); Cal. Corp. Code § 17,154 (West Supp. 2004) (providing that the fiduciary duties that a manager owes to the LLC and its members are those of a partner to a partnership); Haw. Rev. Stat. § 428-409 (Supp. 2001) (indicating that the duty of loyalty is limited to accounting for property, profits, or benefits; refraining from dealing with the LLC as an adverse party; and refraining from competing with the LLC); 805 Ill. Comp. Stat. 180/15-3 (West Supp. 2003) (declaring that the fiduciary duties include the duty to account for certain benefits, to act fairly when acting on behalf of a party with an adverse interest to the company, and to refrain from competing with the company); see also Bishop & Kleinberger, supra note 7, P 10-16 (classifying the duty of loyalty provisions into four categories).

[FN69]. Unif. Ltd. Liab. Co. Act § 409 (1996).

[FN70]. Unif. P'ship Act (amended 1997), 6 U.L.A. 143 (pt. I) (2001).

[FN71]. Section 404(b) of UPA, provides in part:

A partner's duty of loyalty to the partnership and the other partners is limited to the following:

(1) to account to the partnership and hold as trustee for it any property, profit, or benefit derived by the partner in the conduct and winding up of the partnership business or derived from a use by the partner of partnership property, including the appropriation of a partnership opportunity;

(2) to refrain from dealing with the partnership in the conduct or winding up of the partnership business as or on behalf of a party having an interest adverse to the partnership; and

(3) to refrain from competing with the partnership in the conduct of the partnership business before the dissolution of the partnership.

Section 409 of ULLCA contains substantially similar language. Unif. Ltd. Liab. Co. Act § 409.

[FN72]. See Humphreys, supra note 63, § 4.02(3)(b) (indicating that one group of LLC statutes tracks section 21 of UPA and requires accounting to other LLC members). Section 21 of UPA provides that:

Every partner must account to the partnership for any benefit, and hold as trustee for it any profits derived by him without the consent of the other partners from any transaction connected with the formation, conduct, or liquidation of the partnership or from any use by him of its property.

Unif. P'ship Act § 21(1) (amended 1997), 6 U.L.A. 194 (pt. II) (2001). A number of LLC statutes adopt similar language pertaining to the duty to account to other members for profits.

[FN73]. See, e.g., Ala. Code § 10-12-21(l) (1999) (noting that an operating agreement may modify a member's or manager's duties but may not unreasonably restrict rights to information or records or eliminate the duty of loyalty); Colo. Rev. Stat. Ann. § 7-80-108 (2003) (providing that an operating agreement may not unreasonably restrict access to books and records, unreasonably reduce the duty of care, or eliminate good faith requirements); Del. Code Ann. tit. 6, § 18-1101(c) (Supp. 2002) (providing that, to the extent a member or manager has duties at law or in equity, including fiduciary duties and liabilities relating to the LLC or to another member or manager, the member or manager shall not be liable for good faith reliance on the operating agreement and the operating agreement may expand or restrict the person's duties and liabilities); D.C. Code Ann. § 29-1020(a) (2001) (indicating that liability may be limited or eliminated in the articles of organization except if the manager or member engaged in willful misconduct); Fla. Stat. Ann. § 608.423(2)(a)-(c) (West 2001 & Supp. 2004) (providing that the agreement may not unreasonably restrict the right to information or records, eliminate the duty of loyalty, or unreasonably reduce the duty of care); see also Ribstein & Keatinge, supra note 7, app. 9-1 at 11 (summarizing the state provisions dealing with waivers of fiduciary duties in LLCs).

[FN74]. See John C. Coffee, Jr., No Exit?: Opting Out, the Contractual Theory of the Corporation, and the Special Case of Remedies, 53 Brook. L. Rev. 919, 940 (1988) (positing that, "in the case of the partnerships and close corporations, courts seem to have been stricter in the enforcement of fiduciary duties than in the case of publicly held corporations").

[FN75]. As the MBCA suggests:

A director's conflicting interest transaction may not be enjoined, set aside, or give rise to an award of damages or other sanctions, in a proceeding by a shareholder or by or in the right of the corporation, because the director, or any person with whom or which he has a personal, economic, or other association, has an interest in the transaction, if...the transaction, judged according to the circumstances at the time of commitment, is established to have been fair to the corporation.

Mod. Bus. Corp. Act §8.61(b) (rev. 2002).

[FN76]. See Ribstein & Keatinge, supra note 7, § 9.10, at 35-36 (claiming that corporate managers are subject to a lesser standard than general partners based on the "fairness" exception in the corporate context).

[FN77]. 164 N.E. 545 (N.Y. 1928).

[FN78]. Id. at 546.

[FN79]. See, e.g., Donahue v. Rodd Electrotype Co. of New Eng., 328 N.E.2d 505, 515-17 (Mass. 1975) (applying the more exacting duties of a partnership to a close corporation based on the similar levels of trust and confidence that govern both kinds of business relationships).

[FN80]. Banoff, supra note 49, at 59.

[FN81]. Ribstein & Keatinge, supra note 7, § 9.04, at 12.

[FN82]. See Banoff, supra note 49, at 59 (describing the traditionalists' view of fiduciary duties in the ongoing debate with contractarians); see also Lawrence E. Mitchell, The Death of Fiduciary Duty in Close Corporations, 138 U. Pa. L. Rev. 1675, 1677-82 (1990) (arguing that courts have implicitly rejected the assumptions on which fiduciary duties are based and now seem content to rely on “the morals of the marketplace” rather than some more abstract, higher standard).

[FN83]. See Riblet Products Corp. v. Nagy, 683 A.2d 37, 39 n.2 (Del. 1996) (noting that, in a lawsuit for breach of fiduciary duty brought by a minority shareholder/employee, the business's status as a closely held company did not alter the duties of the majority or minority shareholders); Nixon v. Blackwell, 626 A.2d 1366, 1379-81 (Del. 1993) (refusing to develop any judicially created rules to protect minority investors of closely held, but not statutory close corporations); Olsen v. Seifert, No. 97-6456, 1998 Mass. Super. LEXIS 592 (Mass. Super. Ct. Aug. 28, 1998) (indicating that Delaware would review a particular transaction for overall fairness where it is alleged that a controlling shareholder has benefited excessively, but will not impose broad fiduciary duties on close corporations); see also Theresa L. Kelly, Recent Development, Nixon v. Blackwell: Fairness but Not Equality for Minority Shareholders, 19 Del. J. Corp. L. 533, 533 (1994) (“[T]he court made it clear that minority shareholders in closely-held corporations are not entitled to special judicially-created protections.”).

[FN84]. Compare Hynes, supra note 29, at 31 (arguing that RUPA endorses too great an invasion into the freedom of contract), with Vestal, supra note 37, at 524-25 (arguing that the contractarian error in RUPA is so basic and the effects are so profound that the National Conference of Commissioners on Uniform State Laws should withdraw the act).

[FN85]. Revised Unif. P'ship Act § 404(a)-(b) (1997); see also Unif. Ltd. Liab. Co. Act § 409(a)-(b) (1996) (enumerating the requirements imposed by the duty of loyalty).

[FN86]. See Robert A. Ragazzo, Toward a Delaware Common Law of Closely Held Corporations, 77 Wash. U. L.Q. 1099, 1142-44 (1999) (maintaining that Delaware's entire fairness test may provide substantial protection against overt squeeze-outs but may not be as effective in combating more subtle types of abuse such as the failure to pay dividends and the attempt to purchase shares at a bargain price).

[FN87]. See Fine v. Bork, No. 010808586, 2002 Conn. Super. LEXIS 181, at *1 (Conn. Super. Ct. Jan. 15, 2002) (concerning the unlawful appropriation of LLC real estate property by the majority owner).

[FN88]. See Flippo v. CSC Assocs. III, 547 S.E.2d 216, 220 (Va. 2001) (recounting the unilateral transfer of an LLC's assets to a new entity in order to achieve personal estate planning goals).

[FN89]. See Credentials Plus, L.L.C. v. Calderone, 230 F. Supp. 2d 890, 896-900 (N.D. Ind. 2002) (holding that a former LLC manager's solicitation of LLC clients for her new venture constituted an improper seizure of LLC business opportunities).

[FN90]. See Anest v. Audino, 773 N.E.2d 202, 205-08 (Ill. App. Ct. 2002) (presenting a claim brought by an LLC member that was excluded from participation in an exclusive distributorship), appeal denied, 787 N.E.2d 154 (Ill. 2002).

[FN91]. 2002 Conn. Super. LEXIS 181.

[FN92]. Id. at *5-6.

[FN93]. Conn. Gen. Stat. Ann. § 34-141(a), (e) (West 1997 & Supp. 2003).

[FN94]. 547 S.E.2d 216.

[FN95]. See Va. Code Ann. § 13.1-1024.1(A) (Michie 1999) (requiring LLC managers to discharge their duties in accordance with their "good faith business judgment of the best interests of the limited liability company").

[FN96]. Flippo, 547 S.E.2d at 221.

[FN97]. 230 F. Supp. 2d 890 (N.D. Ind. 2002).

[FN98]. Id. at 898-99.

[FN99]. Id.

[FN100]. See Ind. Code Ann. § 23-18-4-2 (West 1994) (containing relevant material in § 2(a) limiting liability unless the conduct was willful or reckless, § 2(b) forcing each member and manager to account for certain benefits and profits unless otherwise provided in the operating agreement, and § 2(c) indicating that a member who is not a manager does not have duties to the LLC or other members solely by acting as a member).

[FN101]. 773 N.E.2d 202 (Ill. App. Ct. 2002), appeal denied, 787 N.E.2d 154 (Ill. 2002).

[FN102]. Id. at 210.

[FN103]. See id. at 209-11; see also 805 Ill. Comp. Stat. 180/15-3 (West Supp. 2003) (stating that members in a member-managed LLC owe to each other fiduciary duties of loyalty and care); 805 Ill. Comp. Stat. 180/55-15 (West Supp. 2003) (applying the fiduciary duties of section 180/15-3 to existing LLCs only on their election prior to January 1, 2000).

[FN104]. Supra notes 91-93 and accompanying text.

[FN105]. No. 010808586, 2002 Conn. Super. LEXIS 181, at *2-3 (Conn. Super. Ct. Jan. 15, 2002).

[FN106]. Id. at *3-4.

[FN107]. Id. at *7.

[FN108]. Id. at *5.

[FN109]. Id. at *6 (citing Conn. Gen. Stat. Ann. § 34-141(e) (West 1997 & Supp. 2003)).

[FN110]. See Unif. P'ship Act § 21(1) (amended 1997), 6 U.L.A. 194 (pt. II) (2001) ("Every partner must account to the partnership for any benefit, and hold as trustee for it any profits derived by him without the consent of the other partners....”); Revised Unif. P'ship Act § 404(b)(1), 6 U.L.A. 143 (pt. I) (2001) (requiring a partner “to account to the partnership and hold as trustee for it any property, profit, or benefit derived by the partner in the conduct and winding up of the partnership business or derived from a use... of partnership property”).

[FN111]. 547 S.E.2d 216 (Va. 2001).

[FN112]. Id. at 221-23.

[FN113]. Id. at 219-20.

[FN114]. Id. at 220.

[FN115]. Id.

[FN116]. Id.

[FN117]. Id. at 221-23.

[FN118]. Va. Code Ann. § 13.1-1024.1(A) (Michie 1999).

[FN119]. 547 S.E.2d at 222.

[FN120]. Meinhard v. Salmon, 164 N.E. 545, 546 (N.Y. 1928).

[FN121]. 230 F. Supp. 2d 890 (N.D. Ind. 2002).

[FN122]. Id. at 894-95.

[FN123]. Id.

[FN124]. Id. at 900.

[FN125]. Id. at 897.

[FN126]. Ind. Code Ann. § 23-18-4-2(b) (West 1994).

[FN127]. Credentials Plus, 230 F. Supp. 2d at 899 (citing Melrose v. Capitol City Motor Lodge, Inc., 705 N.E.2d 985, 990-91 (Ind. 1998); McLinden v. Coco, 765 N.E.2d 606, 615 (Ind. Ct. App. 2002)).

[FN128]. 773 N.E.2d 202, 211 (Ill. App. Ct. 2002), appeal denied, 787 N.E.2d 154 (Ill. 2002).

[FN129]. Id. at 209-11.

[FN130]. Id. at 205.

[FN131]. Id. at 206-07. Precision Pour's operating agreement required five days notice, unless unanimous consent was given to waive it. The notice faxed to the defendant's attorney stated that the meeting was necessary to discuss restructuring the company's business from that of a nonexclusive distributorship to an importer and the effects of this change. At the meeting itself, a call was made to Audino's attorney who stated that Audino would not attend the meeting. Id.

[FN132]. Id. at 207.

[FN133]. See id. at 209-10 (explaining that, effective January 1, 1998, the Illinois LLC statute was amended to provide "that members in a member-managed [LLC] owe to each other the fiduciary duties of loyalty and care").

[FN134]. Id. at 209-10.

[FN135]. At the relevant time, there was no direct statutory provision regarding fiduciary duties. See 805 Ill. Comp. Stat. 180/10-10(b) (West Supp. 2003) (providing that a manager of an LLC shall be personally liable for any act, debt, obligation, or liability of the LLC or another manager or member to the extent that a director of an Illinois business corporation has liability in analogous circumstances under Illinois law). A subsequent statutory amendment, codified at 805 Ill. Comp. Stat. 180/15-3 (West Supp. 2003), ensured that in a member-managed LLC members would owe each other the fiduciary duties of loyalty and care.

[FN136]. Bishop & Kleinberger, supra note 7, PP 14-98 to -99 (indicating that the Delaware statute is devoid of express statutory standards for the duty of care and duty of loyalty).

[FN137]. Del. Code Ann. tit. 6, §18-1101(b), (c)(2) (1999 & Supp. 2002).

[FN138]. Id.

[FN139]. See id. §17-1101(c) (providing that "[i]t is the policy of this chapter to give maximum effect to the principle of freedom of contract and to the enforceability of partnership agreements"); see also Elf Atochem N. Am., Inc. v. Jaffari, 727 A.2d 286, 291-92 (Del. 1999) (holding, in a derivative suit on an LLC's behalf, that the LLC agreement was subject to a forum selection clause and an arbitration clause notwithstanding the fact that a derivative claim was filed and also stressing that the LLC Act's basic approach is similar to that applicable to limited partners and that both Acts permit partners to have the broadest possible discretion in drafting their agreements).

[FN140]. See Bishop & Kleinberger, supra note 7, P 14-101 (observing the almost verbatim language that can be traced from the Delaware Limited Partnership statute to the Delaware LLC statute).

[FN141]. The common law fiduciary duties of general partners have been regarded as similar to that of directors of a Delaware corporation. One would therefore expect that these same duties should be applicable to Delaware LLC members and managers unless they have been modified acceptably by contractual duties in the operating agreement. These common law fiduciary duties include: (1) a duty of care requiring a fiduciary to be attentive and well informed of all material facts relevant to a business decision; (2) a duty of loyalty requiring the fiduciary to act in the best interests of the business and its owners; and (3) a duty to disclose all material facts that would have a significant impact on business decisions. See Altman et al., supra note 57, at 8 (describing the common law fiduciary duties of partners).

[FN142]. 722 A.2d 319 (Del. Ch. 1998).

[FN143]. Id. at 323; see also David Rosenberg, The Two Cycles of Venture Capital, 28 J. Corp. L. 419, 432-33 (2003) (observing that contractual flexibility is one explanation why Delaware is attractive for limited partnerships and indicating that courts "will always defer to the duties embodied in the contract itself" when the parties clearly intended to displace default fiduciary duties).

[FN144]. 791 A.2d 799 (Del. Ch. 2000).

[FN145]. Id. at 813 (quoting Elf Atochem N. Am., Inc. v. Jaffari, 727 A.2d 286, 291 (Del. 1999)) (alteration in original).

[FN146]. Id. (quoting R.F. Balotti & J.A. Finkelstein, The Delaware Law of Corporations and Business Organizations § 20.4 (2000)).

[FN147]. Id.

[FN148]. See Bishop & Kleinberger, supra note 7, P 14-96 (raising the question of whether fiduciary duties exist under Delaware LLC law). But see Altman et al., supra note 57, at 9-10 (indicating that contractual rights and duties may only preempt common law duties if they create an irreconcilable conflict and are set forth clearly and unambiguously). Altman et al. cite R.S.M. Inc. v. Alliance Capital Management Holdings, 790 A.2d 478 (Del. Ch. 2001), which involved a challenged reorganization of a publicly traded partnership. In that case, the chancery court held that since common law fiduciary duties did not irreconcilably conflict with the contractual rights and expectations, common law fiduciary duties were not supplanted, even though the agreement did not expressly provide for this. Id. at 497-98. The authors also cited Miller v. American Real Estate Partners, No. 16788, slip op. at 20-21 (Del. Ch. 2001), available at http:// webman.widener.edu/documents/opinions/16788-044.pdf, which indicated that restrictions on fiduciary duties must be set forth clearly and unambiguously.

[FN149]. 817 A.2d 160 (Del. 2002).

[FN150]. Gotham Partners involved plaintiffs who were limited partners and who challenged a series of transactions that had placed the limited partnership under the control of the general partner's corporate parent at an unfair price. Id. at 164-65. The Delaware Chancery Court upheld the contractual fiduciary duty claims but dismissed the traditional fiduciary duty claims on the grounds that any common law duties had been supplanted by the contractual agreement. Gotham Partners v. Hallwood Realty Partners, No. 15754, 2000 Del. Ch. LEXIS 146, at *40 (Del. Ch. Sept. 27, 2000). Although the plaintiffs were awarded money damages, they contested the remedy offered by the Chancery Court. Gotham Partners, 817 A.2d at 170-73. The Delaware Supreme Court affirmed the chancery court's ruling that the general partner had violated its contractual standard of fairness and partially affirmed the lower court's decision with regard to damages. Id. at 178. However, the Delaware Supreme Court stated in dicta that nothing in the Delaware Revised Limited Partnership Act or elsewhere allows a limited partnership agreement to eliminate the fiduciary duties of a general partner. Id. at 167-68.

[FN151]. 791 A.2d 799 (Del. Ch. 2000).

[FN152]. Id. at 813-15 (addressing the question of whether the members of a majority in interest of a Delaware LLC could remove the plaintiff as a member of the LLC and declare his interest in the LLC forfeited and holding that, unless expressly granted a power of removal by contract, the majority of the members or stockholders of a business entity have no right to take the property of other members).

[FN153]. Gotham Partners, 817 A.2d at 160.

[FN154]. Id. at 167-68; see also Gotham Partners, 2000 Del. Ch. LEXIS 146, at *34 (construing DRULPA to permit the elimination of partners' fiduciary duties).

[FN155]. Gotham Partners, 817 A.2d at 167.

[FN156]. Id. at 167-68 (emphasis added) (quoting Del. Code Ann. tit. 6, § 17-1101(d)(2) (1999)).

[FN157]. 818 A.2d 914, 936 (Del. 2003).

[FN158]. Id. at 925-26. The directors of NCS approved the terms of a merger with Genesis, a publicly traded Pennsylvania company that promised to pay off all of NCS's creditors and to replace NCS shares with its own. Id. at 919, 924-25. Genesis insisted on the restrictive clauses. In addition, it gave the four-member NCS board of directors less than twenty-four hours in which to approve the merger agreement and gave the two board members who collectively owned sixty-five percent of the stock the same accelerated timetable for signing the related voting agreements. Id. at 925. NCS shareholders sued to enjoin the Genesis merger and for breach of fiduciary duties. Id. at 919. The Delaware Chancery Court initially held that the board's defensive measures were reasonable. Id. at 934. In a rare 3-2 split, Delaware Supreme Court reversed, observing that the NCS board was required to contract for an effective fiduciary out clause to exercise its continuing fiduciary responsibility to its minority stockholders. Id. at 936-37. The voting agreements and the defensive measures in the merger agreement were regarded as being inextricably combined and as requiring enhanced judicial scrutiny. Id. at 934. Employing the two-part test established in Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985), the court stated that the NCS directors had to establish that they had reasonable grounds for believing that a danger to corporate policy and effectiveness existed and that that their defensive response was reasonable in relation to the threat posed. Omnicare, 818 A.2d at 935. After analyzing each provision, the court held that the defensive measures had failed to fall within the range of reasonableness. Id. at 936.

[FN159]. Omnicare, 818 A.2d at 939.

[FN160]. Id.

[FN161]. No. 19477, 2002 Del. Ch. LEXIS 38 (Del. Ch. Apr. 25, 2002).

[FN162]. Id. at *2.

[FN163]. Id. at *5.

[FN164]. Id. at *15.

[FN165]. Id.

[FN166]. Id.

[FN167]. Id. at *13.

[FN168]. Id. at *15.

[FN169]. No. 17995, 2000 Del. Ch. LEXIS 122 (Del. Ch. Aug. 31, 2000).

[FN170]. Solar Cells, 2002 Del. Ch. LEXIS 38, at *22 ("Solar Cells has demonstrated a reasonable likelihood of success on the merits of its entire fairness claim...."); VGS, 2000 Del. Ch. LEXIS 122, at *14-17 (holding that the managers' secret attempt to obtain control of the LLC violated their duty of loyalty).

[FN171]. See Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984) (indicating that the business judgment rule "is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company"); see also Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946, 958 (Del. 1985) (stating that "unless it is shown... that the directors' decisions were primarily based on perpetuating themselves in office, or some other breach of fiduciary duty...a Court will not substitute its judgment for that of the board"); Sinclair Oil Corp. v. Levien, 280 A.2d 717, 720 (Del. 1971) (noting that the business judgment will be upheld if there is any rational business purpose).

[FN172]. Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1156, 1162 (Del. 1995).

[FN173]. Id. at 1162-63.

[FN174]. See Nixon v. Blackwell, 626 A.2d 1366, 1376 (Del. 1993) ("In business judgment rule cases, an essential element is the fact that there has been a business decision made by a disinterested and independent corporate decisionmaker. When there is no independent decisionmaker, the court may become the objective arbiter." (citations omitted)).

[FN175]. Id.

[FN176]. See Weinberger v. UOP, Inc., 457 A.2d 701, 710-11 (Del. 1983) (holding that a director with a conflict of interest must show the entire fairness of the transaction, which incorporates the concepts of fair dealing and fair price); see also Nixon, 626 A.2d at 1376 (holding that an entire fairness analysis is required when there is no independent corporate decision maker).

[FN177]. No. 17995, 2000 Del. Ch. LEXIS 122 (Del. Ch. Aug. 31, 2000), aff'd 781 A.2d 696 (Del. 2001).

[FN178]. Id. at *14; see also VGS, Inc. v. Castiel, No. 17995, 2003 Del. Ch. LEXIS 16, at *40, *51 (Del. Ch. Mar. 10, 2003) (holding that the defendant directors had breached their duty of loyalty to Castiel when they secretively consented to merge Virtual Geo into VGS, Inc. without informing him), reargument granted, 2003 Del. Ch. LEXIS 31 (Del. Ch. Mar. 27, 2003).

[FN179]. VGS, 2000 Del. Ch. LEXIS 122, at *5.

[FN180]. Id. at *2.

[FN181]. Solar Cells, Inc. v. True N. Partners, LLC, No. 19477, 2002 Del. Ch. LEXIS 38, at *26-27 (Del. Ch. Apr. 25, 2002).

[FN182]. Id. at *15.

[FN183]. Id. at *16.

[FN184]. Id. at *20.

[FN185]. See Deborah A. DeMott, Beyond Metaphor: An Analysis of Fiduciary Obligation, 1988 Duke L.J. 879, 902 (suggesting that fiduciary obligations are often justified by the fact that a party is vulnerable to a fiduciary's abuse of power, whereas contract law often presupposes free bargaining power of parties on equal social and economic footings).

[FN186]. Id. at 899-901.

[FN187]. Id. at 908.

[FN188]. Id. at 900.

[FN189]. Id. at 901.

[FN190]. See Victor Brudney, Contract and Fiduciary Duty in Corporate Law, 38 B.C. L. Rev. 595, 624-25 (1997) (indicating that "the fiduciary must act for the beneficiary's exclusive benefit," while the classic contractual relationship allows each party to act in his or her own interests); Dickerson, supra note 41, at 458-61 (discussing the actual harm that can occur when fiduciary duties are not mandatory and criticizing ULLCA for allowing the standards of performance to drop down to the level of good faith); Mitchell, supra note 82, at 1715-16 (criticizing the courts' application of fiduciary duties in the context of freeze-outs in close corporations and stressing that there has been a conceptual shift in the application of fiduciary duties from an emphasis on selfless conduct, whereby the fiduciary duty functions as a moral precept, to the pragmatic view that self-interested conduct is permitted in the absence of the fiduciary's malfeasance); D. Gordon Smith, The Critical Resource Theory of Fiduciary Duty, 55 Vand. L. Rev. 1399, 1485-86 (2002) (asserting that the recent trend in partnership law, epitomized by the Revised Uniform Partnership Act, is to displace fiduciary duties with narrower contractual standards).

[FN191]. Supra note 168 and accompanying text.

[FN192]. Solar Cells, Inc. v. True N. Partners, LLC, No. 19477, 2002 Del. Ch. LEXIS 38, at *15 (Del. Ch. Apr. 25, 2002).

[FN193]. Id. at *15-16.

[FN194]. Id. at *20.

[FN195]. Id. at *27.

[FN196]. See Banoff, supra note 49, at 69 (indicating that fiduciary duties are regarded in some circles as the "f-word" to be purged from LLC legislation).

[FN197]. Fine v. Bork, No. 010808586, 2002 Conn. Super. LEXIS 181 (Conn. Super. Ct. Jan. 15, 2002); supra notes 104-09 and accompanying text.

[FN198]. Flippo v. CSC Assocs. III, 547 S.E.2d 216 (Va. 2001); supra notes 111-19 and accompanying text.

[FN199]. Credentials Plus, L.L.C. v. Calderone, 230 F. Supp. 2d 890 (N.D. Ind. 2002); supra notes 121-27 and accompanying text.

[FN200]. Anest v. Audino, 773 N.E.2d 202, 211 (Ill. App. Ct. 2002), appeal denied, 787 N.E.2d 154 (Ill. 2002); supra notes 128-35 and accompanying text.

[FN201]. See, e.g., New Horizons Supply Co-op. v. Haack, 590 N.W.2d 282 (Wis. Ct. App. 1999) (unpublished table decision) (indicating that an LLC agreement was never entered into evidence), available at 1999 Wis. App. LEXIS 108, at *3.

[FN202]. See, e.g., W. Dean Brown, How to Form a Corporation, LLC or Partnership in Pennsylvania (2000) (compiling forms, certificates, and easy-to-follow instructions on the formation of business entities in Pennsylvania); Scott E. Friedman, How to Profit by Forming Your Own Limited Liability Company (1996) (detailing how to form, manage, and dissolve LLCs and including sample forms and a comparison of legal entities); Martin M. Shenkman et al., Starting a Limited Liability Company (1996) (providing a guide on how to establish an LLC).

[FN203]. See U.S. Census Bureau, Statistics of U.S. Business: 2000: All Industries United States (indicating that out of 5,652,544 total firms, 726,862 had no employees, 2,669,870 firms had one to four employees, and 1,021,210 had five to nine employees), available at http:// www.census.gov/epcd/susb/2000/us/US--.HTM (last modified Dec. 15, 2003); see also Press Release, Patricia Buscher, U.S. Census Bureau, 'Mom-and-Pop' Shops Increase (Oct. 22, 2002) (stating that "[b]usinesses with no paid employees grew 2.3 percent between 1999 and 2000 from 16.2 million to 16.5 million"), available at http://www.census.gov/Press-Release/www/2002/cb02-138.html.

[FN204]. Blair & Stout, supra note 24, at 1738-43.

[FN205]. See generally Symposium, Norms and Corporate Law, 149 U. Pa. L. Rev. 1607 (2001) (exploring the role of norms in influencing human behavior); see also Timothy L. Fort, Goldilocks and Business Ethics: A Paradigm that Fits "Just Right," 23 J. Corp. L. 245, 247-48, 263-65 (1998) (analyzing the structure of corporations as mediating institutions to promote ethical behavior necessary for moral development).

[FN206]. See Weidner, supra note 37, at 103-04 (advocating a balanced policy of partnership relationships and observing that the cost of eliminating mandatory minima is the cost of authorizing lawlessness in business relationships).

[FN207]. Douglas K. Moll, Shareholder Oppression v. Employment at Will in the Close Corporation: The Investment Model Solution, 1999 U. Ill. L. Rev. 517, 520 (recognizing that there may be many components to a shareholder's investment in a corporation).

[FN208]. See Ragazzo, supra note 86, at 1142-47, 1151 (acknowledging the possibility that the entire fairness test might not effectively prevent subtle freeze-out schemes in closely held corporations but indicating that the only obstacle would be in defining the elements of a freeze-out (e.g., the discharge of the minority, failure to pay dividends, or preclusion of board participation) as a form of self-dealing).

[FN209]. Cf. id. at 1134 (citing the flexibility of the Delaware Supreme Court regarding the rules of judicial review and the potential that, when presented with the right case, the court may reconsider its views and hold that a majority owner of a close corporation owes a fiduciary duty of fairness to the minority).

[FN210]. For examples of academic work analyzing Nixon v. Blackwell, 626 A.2d 1366 (Del. 1993), see James D. Cox, Mergers and Acquisitions: Equal Treatment for Shareholders, 19 Cardozo L. Rev. 615, 616-19 (1997); Kelly, supra note 83; James M. Van Vliet Jr. & Mark D. Snider, The Evolving Fiduciary Duty Solution for Shareholders Caught in a Closely Held Corporation Trap, 18 N. Ill. U. L. Rev. 239, 242 (1998).

[FN211]. Guth v. Loft, Inc., 5 A.2d 503, 510 (Del. 1939).

[FN212]. E.g., Fine v. Bork, No. 010808586, 2002 Conn. Super. Ct. LEXIS 181, at *6 (Jan. 16, 2002) (involving a situation where a managing member of the LLC "took advantage of his position" and amended the operating agreement in order to appropriate a company asset for his own personal benefit).

[FN213]. E.g., Flippo v. CSC Assocs. III, 547 S.E.2d 216, 219 (Va. 2001) (affirming a manager's liability for breach of fiduciary duty for conveying all of the LLC's property to a new venture).

[FN214]. E.g., Anest v. Audino, 773 N.E.2d 202, 206-07 (Ill. App. Ct. 2002) (finding a breach of fiduciary duties where, without the fifth member's consent, four members formed a new entity, which did not include the fifth LLC member, to handle the LLC's business), appeal denied, 787 N.E.2d 154 (Ill. 2002).

[FN215]. C.A.E. Goodhart, Economics and the Law: Too Much One-Way Traffic?, 60 Mod. L. Rev. 1, 12 (1997).

[FN216]. See id. at 14 (discussing specific performance in the context of contract law, which requires a party to perform her obligations rather than pay more economically efficient, nonperformance damages).

[FN217]. E. Norman Veasey, The Defining Tension in Corporate Governance in America, 52 Bus. Law. 393, 403 (1997).

[FN218]. See Jacobs, supra note 12, at 1044-45 (discussing the inherent tension underlying many enabling statutes between a policy that protects the legitimate expectations of investors and a policy that favors freedom of contract).

[FN219]. 11 P.3d 353 (Wyo. 2000).
[FN220]. Id. at 355.

[FN221]. Id. at 359.

[FN222]. Id. at 361.

[FN223]. No. 99-1443, 2000 U.S. App. LEXIS 14670 (4th Cir. June 27, 2000).

[FN224]. Id. at *20-23.

[FN225]. McConnell v. Hunt Sports Enters., 725 N.E.2d 1193, 1210 (Ohio Ct. App. 1999) (holding that there was no breach of fiduciary duty where the LLC agreement permitted competition and the defendant successfully competed); see also Lynch Multimedia Corp. v. Carson Communications, L.L.C., 102 F. Supp. 2d 1261, 1264 (D. Kan. 2000) (holding that where an LLC agreement permitted the LLC members to engage independently or with others in other business ventures of every nature and description, a member did not violate any duties when he independently acquired a competing cable franchise).

[FN226]. JTB Enters., L.C. v. D & B Venture, L.C. (In re Deluca), 194 B.R. 79, 86-87 (Bankr. E.D. Va. 1996) (denying plaintiff's right to remove the defendant-debtor as manager of the LLC because the implication under the amended operating agreement was that the plaintiff and the defendant had equal voting rights and the plaintiff lacked the majority block needed to remove the defendant as manager).

[FN227]. Goldstein & Price, L.C. v. Tonkin & Mondl, L.C., 974 S.W.2d 543, 550-51 (Mo. Ct. App. 1998) (reversing the trial court's award of fifty-nine percent of a fee paid to the plaintiff and substituting a thirteen percent fee payment because, although the LLC's operating agreement made no provision for awards of fees earned by withdrawing members for work in progress, the LLC members had orally amended the LLC operating agreement to pay the plaintiff thirteen percent of the fee in question upon his withdrawal).

[FN228]. See Banoff, supra note 49, at 69-70 (analyzing Florida's revised LLC statute and observing that the statute has removed the term "fiduciary" in an apparent attempt to curb so-called "galloping Meinhardism" by the judiciary).

[FN229]. Robert A. Hillman, The Richness of Contract Law 132-46 (1997).

[FN230]. Id. at 168.

[FN231]. Id.

[FN232]. Id.

[FN233]. See Claire Moore Dickerson, From Behind the Looking Glass: Good Faith, Fiduciary Duty & Permitted Harm, 22 Fla. St. U. L. Rev 955, 977-78 (1995) (supporting a view that takes into account the perspectives of the parties, does not necessarily support the stronger party, and is more balanced than the law and economics efficiency principle).

[FN234]. Veasey, supra note 217, at 403; see also Omnicare, Inc. v. NCS Healthcare, Inc., 818 A.2d 914, 928 (Del. 2003) (discussing the level of scrutiny to which managerial decisions are subjected before the business judgment rule is applied).

[FN235]. Coffee, supra note 18, at 1622-23 ("Judicial activism is the necessary complement to contractual freedom.").

[FNa1]. The actual language employed varies from statute to statute. For comprehensive tables, discussion, and analysis of duty of care and duty of loyalty provisions, see Bishop & Kleinberger, supra note 7, P 10-16; Ribstein & Keatinge, supra note 7, app. 9-1.
152 U. Pa. L. Rev. 1609

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***343** THE DUTY OF FINEST LOYALTY AND REASONABLE DECISIONS: THE BUSINESS JUDGMENT RULE IN UNINCORPORATED BUSINESS ORGANIZATIONS?

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Abstract

The business judgment rule, a cornerstone of the jurisprudence of the duty of care in the corporate context, holds a less defined role in the contractually driven realm of unincorporated business organizations such as the partnership, limited partnership, and limited liability company. This uncertainty has in recent years been exacerbated by rapid developments in statutory schemes. This article examines (1) the business judgment rule as applied in the corporate context, (2) the recent developments in the laws of unincorporated business organizations, and (3) the interplay of the business judgment rule and the often contractually defined (but at default fiduciary) models of the various unincorporated business organizations.

I. Introduction

Compare, if you will, the following rather unambiguous rulings on the application of the business judgment rule in the context of an unincorporated business organization: "We have determined the business judgment rule may apply to partnerships, thus eliminating judicial review of business decisions in the best interest of the partnership if they are made in good faith and with the care of an ordinarily prudent person." [FN1] "[T]he business judgment rule also is inapposite in the partnership context because it is a function of the unique corporate setting." [FN2] "We hold that in a limited ***344** partnership the duty of the general partner to the limited partners is a duty to discharge his responsibilities according to the business judgment rule." [FN3]

If a mark of insanity is the ability to simultaneously maintain two irreconcilable thoughts, then we must conclude that the law is schizophrenic on the question of whether and how the business judgment rule applies in the context of unincorporated business organizations. [FN4] The business judgment rule is not a rule of conduct, but, rather, a principle of judicial review under which the decisions of corporate directors are afforded great deference when those decisions are challenged as violating the standard of care. The conundrum to be addressed may be stated as follows:

> If all fiduciary relationships in business organizations include a duty of care, regardless of the statutory or common law formulation of that duty, is there any reason the same judicial standard of review should not apply to every challenge asserting a violation of the duty of care, or are the standards of care of the different organizational forms of such a different nature that a single principle of review is inappropriate?

Part I of this article reviews the business judgment rule as it has developed in the corporate context, the effect of its application, and the requirements for avoiding the application of the rule. Furthermore, Part I distinguishes the rule from a simple gross negligence standard of liability. Part II reviews some of the recent developments in unincorporated business organization laws, focusing on structural changes that have altered the relationship of owners among themselves and to the entity. Part II also focuses on the degree to which the business judgment rule has (or has not) been incorporated into the fiduciary provisions of unincorporated business organization laws. Part III reviews the limited case law addressing the ***345** application or rejection of the business judgment rule in unincorporated business organizations. Part IV considers the uneasy interplay of the business judgment rule in the contractual environment of unincorporated business organizations, positing that in most instances the business judgment rule is inapplicable in this environment.

II. The Business Judgment Rule

A. The Corporate Standard of Care and the Business Judgment Rule

The business judgment rule, which originally existed as a common law standard, [FN5] but is now codified in part, [FN6] is a standard of judicial review that protects the broad discretion conferred on a corporate board of directors from excessive judicial interference. [FN7] If a board has exercised a minimum level of care, [FN8] typically satisfied by reference to the procedures utilized in arriving at its decision, then courts will not second-guess the merits of that decision. [FN9] As applied by the Delaware Supreme Court in Aronson v. Lewis, [FN10] the business judgment rule:

> ***346** is a presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company. Absent an abuse of discretion, that judgment will be respected by the courts. The burden is on the party challenging the decision to establish facts rebutting the presumption. [FN11]

The business judgment rule focuses on the mechanisms and procedures used by the board of directors in arriving at its decision, rather than the "after the fact examined" wisdom of that decision. [FN12] The directors, consequently, are not liable for, and decisions will not be set aside due to, a mere error in judgment. [FN13]

***347** Under the Delaware formulation, in order to override the presumption of the business judgment rule, the burden is on the plaintiff to show that:

(1) the directors made no decision; [FN14]
(2) the directors' decision was uninformed; [FN15]
(3) the directors were not disinterested or independent; [FN16] or
(4) the decision involved gross negligence. [FN17]

Where the business judgment rule may shield the decision from judicial scrutiny, the party challenging the decision carries the burden to establish facts rebutting the application of the presumption. [FN18] If the challenging party presents the facts necessary to set aside this presumption, the burden shifts to the directors to prove the "entire fairness" of the subject transaction. [FN19]

The business judgment rule has also been incorporated by The American Law Institute (ALI) into its Principles of Corporate Governance, [FN20] which state:

> ***348** (c) A director or officer who makes a business judgment in good faith fulfills the duty under this Section if the director or officer:
>
> (1) is not interested [§ 1.23] in the subject of the business judgment;
>
> (2) is informed with respect to the subject of the business judgment to the extent the director or officer reasonably believes to be appropriate under the circumstances; and
>
> (3) rationally believes that the business judgment is in the best interests of the corporation. [FN21]

The Delaware and ALI-PCG formulations differ. The former model is a presumption, while the latter is a safe harbor. [FN22] This distinction, however, is not relevant to this analysis. The MBCA contains a somewhat detailed provision that recognizes the business judgment rule and provides guidance as to its application. [FN23] The MBCA comment states that the provision "does ***349** not codify the business judgment rule . . . . Because the elements of the business judgment rule and the circumstances for its application are continuing to be developed by the courts, it would not be desirable to freeze the concept in a statute." [FN24]

It has been suggested that a distinction between the business judgment rule and business judgment doctrine may exist. The rule shields directors from personal liability for damages stemming from decisions that are protected by the business judgment rule, while the business judgment doctrine serves to protect from judicial scrutiny the decisions rendered by those directors. [FN25] As used herein, the business judgment rule is interpreted ***350** as equally applicable to both the decision and any resulting liability. The rule versus doctrine dichotomy, therefore, does not apply.

B. Justifications for the Business Judgment Rule

At least five justifications have been provided for the business judgment rule: [FN26]

(1) Recognition of the possibility of error and the need to apply a relaxed standard before imposing liability so as to maintain the pool of potential directors; [FN27]

(2) The need to encourage the efficient acceptance of risk; [FN28]

(3) Protection of the courts from enmeshment in corporate decision-making; [FN29]

***351** (4) Protection of the board of directors' franchise to direct the management of the corporation; [FN30] and

(5) The remedy available to the shareholders in the ability to replace the directors. [FN31]

When the business judgment rule is not available, the directors bear the heavy burden of proving the entire fairness of the transaction. [FN32] For ***352** instance, the business judgment rule does not apply when directors are interested in the challenged transaction or cannot demonstrate satisfaction of the procedures that would indicate due investigation.

C. Differentiating the Business Judgment Rule from the Standard of Care

It is important to note the difference between the standard of care, which is the standard of conduct expected of directors in their decision making, and the business judgment rule, which is the standard of review that determines whether directors will be held liable for a poor decision. [FN33] ***353** Where the business judgment rule applies, a director will not be held liable for a decision, "even one that is unreasonable" [FN34] and results in a loss to the corporation, so long as the director was not grossly negligent in reaching the decision. [FN35] Furthermore, while the plaintiff is required to show gross negligence in order to overcome the presumption of the business judgment rule, proof of a grossly negligent decision alone is not sufficient to set aside the decision or yield an award of damages. Liability may be avoided in the absence of causation or damages, [FN36] or where the directors can establish the fairness of the challenged transaction. [FN37] The decision, in such instances, will be respected, [FN38] and the directors will not be exposed to personal liability.

D. Exoneration from Liability Does Not Define the Standard of Care

It also must be noted that provisions limiting the personal liability of directors [FN39] or partners are generally not viewed as defining the applicable fiduciary duty. Rather:

> [t]he liability of a general partner to a limited partnership and to other partners does not define the scope of the fiduciary duty of the general partner. Instead, it merely deals with the consequences, i.e., liabilities, which flow from a breach of duty. A similar view has been articulated in connection with Section 102(b)(7) of the Delaware General Corporation Law ***354** (the "GCL") . . . . Commentators generally agree that Section 102(b)(7) of the GCL is not a modification or elimination of the fiduciary duty owed to stockholders. Rather, it is viewed as a modification of the remedies available for breaches of such fiduciary duty. [FN40]

III. The Evolving Structure of Unincorporated Business Organizations

It is necessary to consider the current state of unincorporated business organizations law in order to fully appreciate how and why certain courts have applied the business judgment rule in that context. Since 1988, the law of unincorporated business organizations has undergone monumental, and at times bewildering, changes. These developments include new unincorporated business forms and increased detail in the organizational statutes, as well as modification, alteration, and sometimes reversal of prior statutes and/or common law rules. One consequence of ***355** these changes is that much of the common law predating these developments is of little, if any, continuing authority. These changes have also altered the frame of reference for the interpretation of the organic documents of the unincorporated business organization.

A. The Evolving Partnership (and the Limited Liability Partnership)

The venerable partnership and the Uniform Partnership Act (1914) [FN41] were revised and repackaged in the Uniform Partnership Act (1997). [FN42] In the process, issues and treatments once understood as central to the partnership were revised, leaving in place a structure with the same name, but a different look.

One of the most striking changes was the wholesale modification of the rule of limited liability. First, while UPA provided for joint liability for certain claims and joint and several liability for other claims, [FN43] RUPA substituted a single rule of joint and several liability. [FN44] RUPA also provided a mechanism for eliminating all vicarious liability of the partners, thereby introducing the feature of limited liability to the general partnership context. In response to concerns among professionals about the rules of personal liability incorporated in UPA Section 15, the limited liability partnership emerged as an elective status for a partnership under which the ***356** partners would be afforded limited liability. [FN45] While this elimination of vicarious liability to third parties was the most discussed aspect of the limited liability partnership, for purposes of this article the more important feature is the modification of the intra-partnership obligations that arise out of limited liability partnership status. The election of limited liability partnership status, as provided in RUPA Section 306(c), not only eliminates vicarious liability among the partners, but also voids pre-election ***357** obligations of indemnification and/or contribution. [FN46]

Though the development of the LLP and the abolition of vicarious liability for partnership debts were certainly revolutionary aspects of RUPA, a change of equal if not greater significance took place with respect to fiduciary duties. UPA relied almost entirely upon a common law formulation of the fiduciary duties [FN47] among the partners, most famously expressed as:

> ***358** Joint adventurers, like copartners, owe to one another, while the enterprise continues, the duty of the finest loyalty. Many forms of conduct permissible in a workaday world for those acting at arm's length, are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive, is then the standard of behavior. As to this there has developed a tradition that is unbending and inveterate. Uncompromising rigidity has been the attitude of courts of equity when petitioned to undermine the rule of undivided loyalty by the "disintegrating erosion" of particular exceptions. [FN48]

This formulation, while addressing the standard of loyalty imposed upon partners, failed to address the standard of care that may apply, and the standard of care in partnerships has generally received far less attention than the standard of loyalty. [FN49] When courts have addressed the standard of ***359** care applicable to partners in the direction and operation of the partnership, there has been a tendency to eschew holding a partner liable for mere mismanagement or simple negligence. [FN50]

Whether the UPA standard of care was that of an ordinarily prudent person, [FN51] a more relaxed standard than ordinary care, [FN52] or merely good faith, [FN53] has long been the subject of debate. [FN54] Indeed, one may conclude that the relative paucity of case law and the varying language employed by the courts have not yielded the necessary critical mass of decisional law required to derive and impose a consistent standard. In addition, regardless of the standard of care employed, the question of whether such standard could be prospectively modified by the partnership agreement has also been the subject of some debate. [FN55]

RUPA has supplanted the common law of fiduciary obligations and replaced it with an exclusive statutory formulation. [FN56] RUPA states that "[a] partner's duty of care to the partnership and the other partners in the conduct and winding up of the partnership business is limited to refraining ***360** from engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law." [FN57] Furthermore, this standard of care may be reduced by an agreement of the partners unless the reduced standard is unreasonable. [FN58]

During the drafting process, language expressly addressing "errors in judgment" was considered for inclusion in RUPA. [FN59] The final version of RUPA, however, does not contain an express articulation of the business judgment rule. [FN60] Thus, it may be argued that a court should not apply the business judgment rule when considering alleged violations of the duty of care under RUPA. The Official Comment to RUPA Section 404(c), however, references Rosenthal v. Rosenthal, [FN61] a case that applied the business judgment rule in the partnership context. [FN62] It may be argued, therefore, that RUPA does incorporate a business judgment rule. Either argument, in fact, may correctly state the rule depending upon what is ***361** meant by the "business judgment rule." To the extent that the business judgment rule results in a gross negligence standard of liability, [FN63] the RUPA provision can fairly be characterized as embodying the business judgment rule. On the other hand, to the extent the business judgment rule connotes a relaxed standard of review (and accordingly a relaxed standard of liability) when measuring conduct against a stated standard of care, it is inappropriate to apply the business judgment rule under RUPA because the apparent intent behind the statute is to impose a duty of care that defines both the standard of conduct and standard of liability in terms of gross negligence.

B. The Evolving Limited Partnership (and the Limited Liability Limited Partnership)

Following the revision of UPA, [FN64] NCCUSL undertook a similar effort to modernize and update its limited partnership statute. The result was the Uniform Limited Partnership Act (2001), commonly referred to as "ReRULPA." [FN65] Building upon the lessons learned in the course of drafting RUPA, ReRULPA modified long accepted rules of liability within the limited partnership and adopted a statutory formula of fiduciary duties and obligations. [FN66]

ReRULPA expressly provides for the limited liability limited partnership. This new format, analogous to the limited liability partnership, allows a limited partnership to elect a status in which limited liability is enjoyed by not only the limited partners, but the general partners as well. [FN67] At the same time, ReRULPA provides greater liability protection to the limited partners in that, unlike the RULPA formulation, protection is not ***362** subject to forfeiture as a consequence of "excessive" involvement in the management and operation of the partnership. [FN68]

RULPA, like its predecessor, the Uniform Limited Partnership Act of 1916, [FN69] does not address partner fiduciary duties and relies on "linkage" to the law of general partnerships to supply the rules for this area. [FN70] While partner fiduciary duties are only vaguely addressed in UPA, [FN71] RUPA explicitly defines a partner's fiduciary duties and delineates the extent to which partners may contractually modify those duties. [FN72] How well the concept of linkage to UPA or RUPA works has been the subject of some debate. [FN73] Illustrating their doubt about the success of linkage, the drafters of ReRULPA determined that ReRULPA should not be linked to UPA or RUPA, and the new act was drafted as a stand-alone statute. [FN74] Thus, under ReRULPA, the fiduciary duties of both the general and limited partners are determined solely by the terms of ReRULPA.

Under ReRULPA, "[a] general partner's duty of care to the limited partnership and the other partners in the conduct and winding up of the limited partnership's activities is limited to refraining from engaging in ***363** grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law." [FN75] The general partner's duty of care under ReRULPA, therefore, is articulated in language identical to that used in RUPA [FN76] and does not include an express articulation of the business judgment rule. ReRULPA also follows the RUPA model with respect to contractual modification of a general partner's duty of care by precluding the partnership agreement from unreasonably reducing a general partner's duty of care. [FN77]

ReRULPA specifies that "[a] limited partner does not have any fiduciary duty to the limited partnership or to any other partner solely by reason of being a limited partner." [FN78] Any duty of care on the part of a limited partner would arise only as a result of provisions in the partnership agreement expressly imposing such a duty or creating a role for a limited partner, which gives rise to such a duty under other law (e.g., the law of agency). [FN79]

These changes have moved the limited partnership model closer to the corporate model in some significant respects, just as the changes to RUPA had the same effect on the general partnership model. It is possible to view the gross negligence standard of care in RUPA and ReRULPA as encompassing the business judgment rule to the extent that it has been interpreted to result in a gross negligence standard of liability. [FN80] As is the case under RUPA, however, it is inappropriate to apply the business judgment rule under ReRULPA to the extent that the business judgment rule connotes a relaxed standard of review (and thus, a relaxed standard of liability) when measuring conduct against a stated standard of care. The apparent intent behind ReRULPA, like RUPA, is to specify both the standard of conduct and standard of liability involved in the duty of care in terms of gross negligence.

C. The Rise of the Limited Liability Company

The 1990s also saw the rise and rapid development of a new form of unincorporated business organization, the limited liability company ***364** (LLC). [FN81] The LLC combined for the first time limited liability for all participants with maximum freedom of contract to structure the enterprise in accordance with the desires of the participants. [FN82] An anomaly in 1988 (existing under only Wyoming and Florida law), the LLC was by 1996 a form of organization authorized by the laws of all fifty states, the District of Columbia, and the Virgin Islands. [FN83]

LLC statutes vary widely. A number of state statutes drew heavily from the Prototype Limited Liability Company Act, which was a product of a working group organized under the American Bar Association, Section of Business Law, Committee on Partnerships and Unincorporated Business Organizations. [FN84] Relatively few states have adopted the Uniform Limited Liability Company Act [FN85] promulgated by NCCUSL.

The duty of care imposed on managing members and managers under ULLCA is based on the RUPA definition of a partner's duty of care and ***365** does not contain an express articulation of the business judgment rule. Section 409(c) of ULLCA provides: "A member's duty of care to a member-managed company and its other members in the conduct and winding up of the company's business is limited to refraining from engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law." [FN86] Similarly, in a manager-managed LLC, a manager is held to the same standard of care prescribed for a member in a member-managed company. [FN87] ULLCA also follows the RUPA model regarding contractual modification of the duty of care in the operating agreement; the operating agreement may not unreasonably reduce the duty of care defined in the statute. [FN88]

The ABA Prototype addresses the duty of care of a member or manager as follows:

> A member or manager shall not be liable, responsible or accountable in damages or otherwise to the limited liability company or to the members of the limited liability company for any action taken or failure to act on behalf of

the limited liability company unless the act or omission constitutes gross negligence or willful misconduct. [FN89]

The commentary to this provision of the ABA Prototype likens this standard to the model commonly applied to corporate directors, managing partners, or general partners of limited partnerships and implies that the standard embodies the protection of the business judgment rule. [FN90]

***366** State LLC acts reflect various approaches to the duty of care of managers and managing members. Eight states have adopted ULLCA. [FN91] Seven of the eight retained the RUPA-based ULLCA formulation of the duty of care, which limits the duty of care to refraining from engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law. [FN92] Several non-ULLCA states have adopted a duty of care standard like that found in ULLCA, [FN93] while the Wisconsin act merely prohibits criminal violations and willful misconduct. [FN94]

Approximately eighteen state LLC statutes parallel language formerly used in the MBCA [FN95] and require managers and managing members ***367** to act in good faith and exercise the care of an ordinarily prudent person in a like position under similar circumstances. [FN96] Most of these states also specify that managers and managing members must act in a manner reasonably believed to be in the best interests of the company. [FN97] Virginia ***368** simply requires that managers act in accordance with their good faith business judgment of the best interests of the limited liability company. [FN98]

Approximately nine states do not specify a standard of care, but provide immunity from liability in the absence of gross negligence, willful misconduct, or similar culpable conduct. [FN99] The LLC statutes of approximately eleven other states specify neither a standard of conduct nor a threshold of liability, [FN100] albeit some of these statutes imply that there are fiduciary duties and associated liability for breach. [FN101]

Many state LLC statutes explicitly give members the flexibility to define duties or liabilities of managers and managing members, at least to some extent, in the LLC's operating agreement or articles of organization. These statutes, however, address this issue in a variety of ways. [FN102] The ULLCA approach permits the operating agreement to define the duty of care, but the default gross negligence standard may not be unreasonably reduced. [FN103] Some statutes have provisions similar to the types found in corporate statutes permitting director exculpation in the articles of incorporation. [FN104] A number of jurisdictions permit the operating agreement ***369** to modify duties and/or liabilities without expressly limiting such power. [FN105] In perhaps the ultimate expression of freedom of contract, the recently amended Delaware statute states that the fiduciary duties of a member or manager "may be expanded or restricted or eliminated by provisions in the limited liability company agreement." [FN106]

Although LLC statutes currently reflect a variety of approaches to the duty of care, the end result for the standard of liability is similar under the various statutes. To the extent that the statutes reflect a corporate approach towards the duty of care, the courts can be expected to apply the corporate business judgment rule. The ULLCA model sets a gross negligence standard of care, and, presumably, a gross negligence standard of liability, [FN107] which results in a standard of liability similar to that resulting from application of the business judgment rule. [FN108] Likewise, the ABA Prototype model addresses the duty of care in terms of a standard of liability, rather than a standard of care, which results in a standard of liability consistent with application of the business judgment rule. [FN109] In states where the statute is silent, the courts will likely apply standards ***370** similar to those traditionally applied in the corporate or partnership context, which ultimately protect managing persons from liability for mere negligent mismanagement. Thus far, there is little case law dealing with the duty of care in the limited liability company context. As is the case with the corporate and partnership case law, the duty of loyalty has received more attention than the duty of care. [FN110]

D. The Changed Landscape of Unincorporated Business Entity Law and the

Diminution of Co-Venturer Oversight

As unincorporated business organization law has adopted certain features that have traditionally been the hallmark of the corporate model, i.e., limited liability, the degree to which venturers expect and need to engage in extensive oversight of one another has been diminished. [FN111] Once ***371** the corporation was the structure of choice for most ventures in which passive capital was sought. The limited partnership was used when taxation under Subchapter K was a material aspect of the transaction, such as real estate syndications. Common to both of these structures was the provision of limited liability to passive investors. The investors, in these situations, could accept a passive role, being one in which they engaged in little if any oversight of the managers because their exposure to the venture in question was limited to the amount invested. [FN112] The UPA partnership, conversely, was seldom used for ventures of significant magnitude because the rule of personal liability for partnership obligations imposed extensive oversight responsibilities among the partners and the high costs of maintaining and distributing the information necessary to respond to those demands. [FN113]

Today, the menu of available business structures is such that limited liability is no longer restricted to corporate shareholders and limited partners. Limited liability is now available for all venturers by utilizing a limited liability partnership, limited liability limited partnership, or limited liability company. The practical limitations upon the availability of capital from passive investors that previously limited the size of most partnerships ***372** have now been largely eliminated. [FN114] While the corporation is generally the vehicle of choice for publicly held companies, publicly held limited partnerships and limited liability companies are not unheard of. Thus, the unincorporated business organization, which was previously restricted to the closely-held and closely-managed realm, is now available for the largest, as well as the smallest, of ventures.

As unincorporated business organizations take on aspects and characteristics traditionally enjoyed by the corporate form, there is a danger that corporate jurisprudence may be indiscriminately applied to unincorporated organizations. Wholesale application of corporate case law would do great violence to the differing default obligations undertaken by, and the contractual flexibility afforded to, the participants of those ventures. Rather, any application of corporate principles to unincorporated organizations must take place only after a careful review of the appropriateness of doing so. [FN115]

***373** IV. The Mixed History of the Business Judgment Rule in Unincorporated Business Organization Law

As noted in the introduction, there are conflicting decisions on whether the business judgment rule applies in the realm of unincorporated business organizations. [FN116] A number of facts may have given rise to these disagreements, including uncertainty as to the applicable formulation of the standard of care, less than exacting appreciation of the purpose and effect of the business judgment rule, and the indiscriminate application of corporate law rules to an unincorporated law question.

A. General and Limited Partnerships

Courts have yet to apply the duty of care as articulated in either RUPA [FN117] or ReRULPA, [FN118] but a number of cases have applied a business judgment rule in the partnership context. For example, in Rosenthal v. Rosenthal, [FN119] the Maine Supreme Court pronounced that partners are subject to the same fiduciary duties of care and loyalty owed by a corporate director under Maine law. [FN120] After describing the duty of care as requiring that degree of diligence, care, and skill which ordinarily prudent persons would exercise under similar circumstances, the court provided a lengthy explanation of how and why the business judgment rule insulates partners from liability for informed decisions so long as the partners were not ***374** motivated by fraud or bad faith. [FN121]

Various articulations of the business judgment rule have appeared in other partnership cases that have insulated partners from liability for decisions involving carelessness, [FN122] failure to use ordinary skill and care, [FN123] poor business judgment, [FN124] simple negligence, [FN125] unwise investment ***375** schemes, [FN126] negligence with no breach of trust, [FN127] or an abuse of discretion. [FN128] Other courts have stated the rule more abstractly, finding there was no liability where there was no fraud or misconduct, [FN129] the Aronson v. Lewis standard was satisfied, [FN130] there was no allegation of interestedness, [FN131] there was good faith and reasonable diligence, [FN132] or the care rendered was that of an ordinary prudent person. [FN133] Some courts appear to apply the business judgment rule as a substantive rule without specifying a standard of liability or review. [FN134] On the other hand, at least ***376** one court has stated that the business judgment rule is not applicable in the partnership context at all. [FN135] One commentator has summed up the state of the case law as follows:

> Partners have a duty to use appropriate care in managing the partnership business, and they can be held accountable for poor business management which violates the requisite duty. Traditionally, the courts have held partners to a reasonable care standard or a good faith standard with respect to partnership business. Under a reasonable care standard, a partner is liable to the partnership or the other partners if his or her conduct was unreasonable. The reasonable care standard has fallen into general disuse, and the good faith standard has become the accepted method for determining partner liability for a breach of his or her duty of care. Under a good faith standard of care, a partner is not liable to the partnership or his or her co-partners for acts which are not fraudulent or wanton and which are undertaken in good faith. When the good faith standard is applied, there is no need to consider whether a partner used ordinary care in managing the partnership business, and a partner will not be liable if his or her conduct results from a mistake or an honest error in judgment. Partners have been held liable for mismanagement when they were grossly negligent or acted in reckless disregard for the affairs of the partnership. [FN136]

Consequently, whether the jurisdiction applies the reasonable care or the good faith standard determines whether a relaxed standard of review is appropriate. Insomuch as RUPA applies a gross negligence standard of care, equal to the standard of review under the business judgment rule, it would appear that a court applying both the RUPA standard and the business judgment rule would either be duplicating its efforts or providing excessive deference to the actions under challenge.

***377** B. Limited Liability Companies

Because no widely accepted approach to the duty of care has emerged in the limited liability company statutes, it is difficult to draw broadly applicable principles from those statutes. Further, because there is little case law focusing on the duty of care of a member or manager of a limited liability company, there is a dearth of judicial guidance on whether liability for breach of the standard of care will be determined under a relaxed standard of culpability.

The first LLC cases addressing the duty of care and business judgment rule were decided in the context of statutes that did not specify a duty of care or standard of liability. In the Maryland case of Froelich v. Erickson, the court applied the corporate business judgment rule because the LLC operating agreement specified that the LLC's directors were subject to the duties of a corporate fiduciary as defined by Maryland law. [FN137] In VGS, Inc. v. Castiel, [FN138] the Delaware Court of Chancery implied that the business judgment rule is applicable in the LLC context, but rejected the defendant managers' argument that the business judgment rule protected them in that case. [FN139] The court found that the defendant managers breached their duty of loyalty by secretly orchestrating a squeeze-down merger; therefore, the court concluded the business judgment rule did not protect the managers even though they may have conscientiously believed the plan was in the best interest of the LLC. [FN140] In Carson v. Lynch Multimedia Corp., a breach of fiduciary case involving a Kansas LLC, a federal district ***378** court in Kansas assumed that Kansas courts would follow the corporate business judgment rule as articulated in Delaware. [FN141] The court, however, concluded the alleged conduct would not be protected because it involved actions that were taken for reasons "wholly unrelated to the business" of the

LLC. [FN142]

A few cases addressing statutory formulations of the duty of care have appeared, but these cases generally yield little more than recitation of the statutory provisions followed by a conclusion that the duty was or was not breached. [FN143] Shell v. King, a mismanagement case in which the ***379** Tennessee Court of Appeals interpreted Tennessee's MBCA-based articulation of a manager's duty of care in the context of allegations against an LLC's "Chief Manager," [FN144] could have been a vehicle for exploring the relationship between the statutorily prescribed standard of conduct and the standard of liability, but the court did not do so. Although the manager argued he was protected by provisions permitting delegation of duties and reliance on financial information prepared by others, the court concluded that the chief manager's wholesale delegation of financial matters to another individual, without taking any steps to verify whether the individual was correctly performing these responsibilities, was negligent and a breach of the manager's fiduciary obligations to the LLC. [FN145] The court spoke in terms of mere negligence and did not discuss the business judgment rule or make any distinction between the standard of conduct articulated by the statute and the standard of liability imposed by the court.

V. The Business Judgment Rule in a Contract Law Environment

To the extent that any definitive statements can be made in this realm, the business judgment rule has no application in a duty of care analysis under the formulation of RUPA, ReRULPA, or ULLCA. [FN146] In each of these instances, the organic acts provide a standard of care of gross negligence. Conduct that does not rise to the level of gross negligence does not give rise to liability-there has been no violation of the standard. On the other hand, where gross negligence is present, liability and culpability should attach (assuming such other requisites as damages, causation, etc.). There is no place for a relaxed standard of review when gross negligence is already applied by the standard of care. [FN147] A relaxed standard of review would serve no purpose-unless the desire is to avoid culpability-until there is behavior such as willful misconduct that is more egregious than ***380** mere gross negligence. Dropping the standard of review below the gross negligence threshold would result in a more relaxed standard of review than typically applied under the business judgment rule. This further relaxed standard would not reflect the business judgment rule as heretofore generally understood.

Unincorporated business organizations, as contrasted with corporations, are uniquely creatures of contract in which the participants have broad discretion to craft the agreement amongst themselves, including matters of fiduciary duties. The primacy of the organic documents organizing an LLC was addressed in In re Lake Country Investments, [FN148] where the court observed:

> Limited liability companies are neither general corporations nor general or limited partnerships. They are a specially recognized form of entity . . . . The case law applicable to partnerships and construing partnership law, which has been briefed and discussed at length, is of limited utility. The specific written agreements must be given effect, and even the statute relied upon by [defendants] recognizes the primacy of the structural and organizational documents in the context of limited liability companies. [FN149]

This overlap of contract and fiduciary law gives rise to a new challenge, one requiring a mechanism for assessing which frame of reference will be applied when considering a question. [FN150] Courts could apply a contract analysis, assessing the action to determine if it is permitted or forbidden by the terms of the agreement entered into between the parties. [FN151] Alternatively, the question may be assessed under a fiduciary model wherein the limitations imposed serve to protect the non-managerial investors from overreaching by those in management. This problem can ***381** exist regardless of entity form. [FN152] A decision, nevertheless, needs to be made as to which frame of reference will control. [FN153] May an action that is sanctioned by the agreement be permitted to stand where it clearly implicates and indeed violates general fiduciary standards?

The interplay of the contract and fiduciary duty models of analysis in unincorporated business organizations yields multiple scenarios for answering this question. Specifically, there are at least six viable scenarios:

. The underlying statute expressly provides for a fiduciary duty of care and permits it to be waived or modified in the agreement, [FN154] and the parties have, by agreement, waived or modified the duty;

. The underlying statute expressly provides for a fiduciary duty of care, but is silent regarding waiver or modification, and the parties have, by agreement, waived or modified the duty;

. The underlying statute expressly provides a fiduciary duty of care, and the agreement is otherwise silent;

. The underlying statute is silent as to a fiduciary duty of care, but permits modification or waiver of duties, and the parties have incorporated a standard into the agreement;

. The underlying statute is silent as to a fiduciary duty of care and as to modification or waiver of duties, and the parties have incorporated a standard into the agreement; [FN155]

. The underlying statute is silent as to a fiduciary duty of care (and either does or does not permit modification or waiver of duties), and the parties have not incorporated a standard into the agreement. [FN156]

***382** In the first scenario, the parties have provided by agreement the appropriate standard of care, and exceptions thereto, for their intended relationship. This contractual provision was made in accordance with the express statutory authority to do so. [FN157] As the waiver or modification of the standard is permitted by the underlying statute, the agreement of the parties should be given its full effect, [FN158] and the interpretation of the waiver or modification should be on the basis of contract law. A fiduciary analysis should not apply to determine whether the waiver or modification was fair ***383** to the participants or whether it permits overreaching by those in control. [FN159] Only if the waiver or modification exceeds the scope permitted by the statute should a fiduciary analysis be applied, which presents another question. As the parties sought to modify the fiduciary duty of care to a degree not permitted, should the managers' actions be assessed based upon the default standard of care, or rather against the standard of care as it may be modified without violation of the underlying statute? It can be debated whether the courts do more violence to the agreement of the parties by adopting one outcome or the other.

The second scenario should result in the enforcement of the contractual standard of care that was accepted by the parties. This enforcement should apply notwithstanding the absence of statutory authority for the modification of the standard. It would be the height of paternalism for the courts to determine that a negotiated standard should be rejected and the statutory standard applied simply because the legislature did not address contractual modification of duties. [FN160] The absence of an express right of modification should not be interpreted as equivalent to an express legislative statement barring modification. While it may be unwise for investors to participate in a venture in which those in control are not bound by a standard of care, or in which the care demanded of them is minimal, courts should be reluctant to prohibit the parties from entering into such an agreement absent a clear manifestation of legislative intent that the standard is not subject to waiver or modification. [FN161]

The third scenario is the most related to the corporate law situation, namely that there is a statutorily defined standard of care which must be applied by the courts, unmodified by any agreement of the parties. If there is an appropriate situation in the realm of unincorporated business organization law for the application of the business judgment rule, this would be it. As has been set forth above, however, the applicable standard of care under RUPA, ReRULPA, and ULLCA is already one of gross negligence. As previously noted, additional deference to the conduct of those managing the organization would seem inappropriate and excessively ***384** lenient. [FN162]

Scenarios four and five involve the question of whether the parties may by contract modify the otherwise applicable common law. The answer is clear if the statute expressly permits such modification. Even in the absence of such express authorization, the parties should be able to do so. There is case law stating that they may, [FN163] and there is no patent rationale for rejecting the standard that the parties might adopt. [FN164] As discussed below, there is no justification in either scenario for applying a reduced standard of review to the standard of care defined by the participants. In these cases, we simply assume that the parties said what they meant to say [FN165] and that if they intended a relaxed standard of review, they would have so provided in the document. As with any universal statement, however, there is at least one exception: if the agreement in question incorporates a corporate standard of care (either by reciting the corporate formulation in the document or by a statement to the effect that those in control of the unincorporated business are subject to the standards of a corporate director), and the state law applies the business judgment rule, [FN166] it would be appropriate to apply the rule to the actions of those acting on behalf of the unincorporated organization. While doing so involves an assumption that the drafter meant to incorporate the business judgment rule, it is a greater assumption to determine that the drafter sought to reject the standard of review applied to that standard of care.

The final scenario is the most troubling because the participants have provided no contemporaneous description of their expectations. One view would be that the parties sought to have their agreement interpreted by the common law fiduciary duty of care. [FN167] An alternate and equally valid view would be that the parties drafted the agreement pursuant to what they thought was necessary for their relationship. While they did accept common law rules of contract interpretation and enforcement, including ***385** good faith and fair dealing, they did not contract on the basis of the importation of fiduciary rules. There is little, if any, justification for either of these views, and even less justification for accepting one over the other. Perhaps a fiduciary analysis is not required, as the parties have addressed all of the issues they deem important and have retained the information and oversight rights sufficient to protect against abuse. [FN168]

Important for our purposes is that in five of the six scenarios the contracting parties have specified the standard of care they deem necessary and appropriate to their dealings. The contracting parties, in such a situation, reasonably expect the terms of their agreement to be enforced. What they do not expect is that the terms of their agreement will be enforced not as they have written, but to a degree deemed necessary to preserve the flexibility of management. That is, however, exactly what the application of the business judgment rule (i.e., additional deference) does when applied to these situations. The differentiation in the standards of care and review will result in the court enforcing a more lenient standard of conduct that is contiguous with the standard of review, which is not the parties' contracted standard. If contracting parties are not able to expect that the limitations they impose on the care of the managers will be enforced as written, then they must draft the modifications not to the limit of what is permitted, but rather to some unknown limitation that is more restrictive than the actual agreement. Then, in an action for enforcement, the court's deference to the manager will grant additional flexibility, which, when combined with the contractual grant, will equal the standard of care actually intended by the parties.

***386** Clearly, this situation is unworkable. It would not be possible for contracting parties to properly assess the degree to which they must draw back the contractual standard of care so that, when combined with the effective grant of authority resulting from the application of the business judgment rule, the intentions of the parties are actually achieved. As such, the business judgment rule should not be applied in unincorporated business organizations that utilize a gross negligence standard of care or culpability.

Admittedly, a determination not to apply the business judgment rule where the parties, by agreement, have adopted a particular formulation for the standard of care fails to provide any guidance with respect to the application of the business judgment rule where the parties have made no express (or clearly implicit) decision regarding the standard of care. Such organizations will fall into one of three categories: (1) inadvertent partnerships, in which no thought has been given to the standard of care; (2) minimally lawyered entities, where little if any thought has been given to the standard of care and the advisors may be unaware that the standard of care is subject to modification or lack the sophistication necessary to confidently modify the standard; or (3) organizations lawyered by sophisticated advisors who do not deem any modification of the default standard of care necessary.

In this situation, there exist at least two rationales for not applying the business judgment rule in the context of unincorporated business organizations. The first is the need to ensure consistency on review among both lawyered and unlawyered organizations. Extensively lawyered organizations, with sophisticated organic documents specifying a standard of care, are entitled to the enforcement of a specified standard without application of the business judgment rule. Arguably, they should not be subject to a standard of review that differs from that applied to the unlawyered or where the default statutory or common law standard has been adopted.

Secondly, the business judgment rule should not be applied to the new unincorporated business forms because it generally does not appear in the organizational statutes. [FN169] The business judgment rule was well ***387** developed by the time that RUPA, ReRULPA, ULLCA, and the ABA Prototype were drafted and at the time the various state legislatures crafted their own statutes based upon these acts. The drafters of the statutes, by and large national and regional experts in unincorporated business organization law, typically did not incorporate the business judgment rule into the fiduciary duty formulations setforth in the statute. While it is always somewhat problematic to draw conclusions from the absence of a provision from a statute, the absence of such an important concept as the business judgment rule is worthy of note and indicative of legislative intent. This argument by absence is even stronger in the case of RUPA and ReRULPA where the business judgment rule was expressly considered and in the end not incorporated into the uniform act. [FN170]

VI. Conclusion

The business judgment rule has proved to be an ever-evolving legal concept, [FN171] and its contour and application have proved exceptionally difficult to reduce to a precise formulation. [FN172] At the same time, statutory formulations of the duty of care have only recently been adopted in the context of the unincorporated business organizations reviewed in this ***388** article. These statutory formulations largely divorce current law from the limited, and occasionally contradictory, prior case law regarding the standards of care and review. What, if any, role a relaxed standard of review (as reflected in the corporate business judgment rule) should play in the context of unincorporated business organizations has never been clearly and consistently articulated by the courts. The introduction of the new statutory schemes has further complicated the analysis. What is presently clear is that under those unincorporated business organizations statutes that have adopted a gross negligence standard of care, there exists no room for a further reduced standard of review.

Furthermore, as a matter of contractual construction, where the participants in an unincorporated business organization seek to specifically define a standard of care, that standard should be enforced as written. It would do violence to the agreement to apply a more relaxed standard of review (and, ultimately culpability) than applied by the contract. While there will be particularized exceptions to this principle, the application of the written standards should be the first rule. Some may fear that this rule of construction will signal a departure from the fiduciary realm of unincorporated business organizations. Such concern, however, is misplaced. Legislatures remain fully capable of defining the fiduciary standards that will apply in unincorporated business organizations and the limits on departures from those statutorily defined standards. This is what we have seen in the last decade in RUPA, ReRULPA, and ULLCA. Fiduciary principles will likewise continue to be applicable in those situations in which the underlying statute does not express a standard of care and the parties to the agreement have not sought to craft one to govern their relationship.

Just as the last decade has seen significant developments in the area of unincorporated business organization law, we can expect that the next decade will see development in the case law on how these new formulas should be applied and, in the case of partnerships and limited partnerships, how they will differ from their predecessors. It will be the sum of those developments in the law that will determine, in the unincorporated business organization realm, whether or not a relaxed standard of review will apply to alleged violations of the standard of care.

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[FN1]. Kuznik v. Bees Ferry Assocs., 538 S.E.2d 15, 28 (S.C. Ct. App. 2000).

[FN2]. Henkels & McCoy, Inc. v. Adochio, 138 F.3d 491, 502 (3d Cir. 1998) (citing 3A William Meade Fletcher et al., Fletcher Cyclopedia of the Law of Private Corporations §§ 1036-37 (perm. ed. rev. vol. 1994)). Cf. Lamden v. La Jolla Shores Clubdominium Homeowners Ass'n, 980 P.2d 940, 946- 50 (Cal. 1999) (stating corporate business judgment rule did not directly apply to action taken by unincorporated homeowners' association, but holding deference to decision of board of such association was appropriate where board "acted upon reasonable investigation, in good faith, and in a manner the [b]oard believed was in the best interest of the [a]ssociation and its members").

[FN3]. Jackson v. Marshall, 537 S.E.2d 232, 236 (N.C. App. 2000).

[FN4]. In this article, the term "unincorporated business organizations" encompasses only the partnership, limited partnership, limited liability company, limited liability partnership, and limited liability limited partnership. Because of the novel application of trust law to the business trust, it is not considered herein, and no effort to review the law of other unincorporated organizations, such as the cooperative, has been undertaken. We note, however, that the business judgment rule has been applied in the context of a donative trust. See, e.g., Wood Prince v. Lynch, No. 03-1975, 2005 R.I. Super. LEXIS 24, at *11-*17(R.I. Super. Ct. Feb. 8, 2005).

[FN5]. Gries Sports Enters., Inc. v. Cleveland Browns Football Co., 496 N.E.2d 959, 963 (Ohio 1986) (noting that the business judgment rule has a history of at least 150 years as part of the common law); Model Bus. Corp. Act § 8.31, cmt. note on the Business Judgment Rule (1984) [hereinafter MBCA]; see Resolution Trust Corp. v. Dean, 854 F. Supp. 626, 636 (D. Ariz. 1994); FDIC. v. Stahl, 854 F. Supp. 1565, 1571 (S.D. Fla. 1994); Paramount Communications v. QVC Network, 637 A.2d 34, 46 (Del. 1993).

[FN6]. See infra notes 20-24 and accompanying text.

[FN7]. As with most legal principles, there are cases in which the business judgment rule has been entirely misapplied. For example, in Baker v. 16 Sutton Place Apartment Corp., 768 N.Y.S.2d 198 (N.Y. App. Div. 2003), decisions by a landlord to forego certain maintenance work, purportedly in violation of lease covenants, were held to be protected by the business judgment rule.

[FN8]. As noted in Cede & Co. v. Technicolor, Inc., under Delaware law directors are "charged with an unyielding fiduciary duty to protect the interests of the corporation and to act in the best interests of the shareholders." Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 360 (Del. 1993) (subsequent history omitted). The broader application of the business judgment rule to questions of loyalty or of good faith, as discussed in Cede, is beyond the scope of this article.

[FN9]. See, e.g., FDIC v. Castetter, 184 F.3d 1040, 1046 (9th Cir. 1999); Smith ex rel. Boston Chicken, Inc. v. Arthur Andersen, LLP, 175 F. Supp. 2d 1180 (D. Ariz. 2001); Kahn v. Roberts, 679 A.2d 460, 467 (Del. 1996); Citron v.

Fairchild Camera & Instrument Corp., 569 A.2d 53, 66 (Del. 1989); Smith v. Van Gorkom, 488 A.2d 858, 872-73 (Del. 1985); Solomon v. Armstrong, 747 A.2d 1098, 1111-13 (Del. Ch. 1999); Weiss v. Samsonite, 741 A.2d 366, 371-72 (Del. Ch. 1999); Cinerama, Inc. v. Technicolor, Inc., 663 A.2d 1134, 1140 (Del. Ch. 1994); Potter v. Pohlad, 560 N.W.2d 389, 392 (Minn. App. 1997); Green Party of N.J. v. Hartz Mountain Indus., Inc., 752 A.2d 315, 326 (N.J. 2000); Koos v. Cent. Ohio Cellular, Inc., 641 N.E.2d 265, 274 (Ohio 1994). In Delaware jurisprudence, the duty of due care first appears in Graham v. Allis-Chalmers Mfg. Co., 188 A.2d 125, 130 (Del. 1963).

[FN10]. 473 A.2d 805 (Del. 1984).

[FN11]. Id. at 812 (citations omitted). See also Navellier v. Sletten, 262 F.3d 923, 946 n.12 (9th Cir. 2001) (applying Delaware law); Huang v. Lanxide Thermocomposites, Inc., 760 N.E.2d 14, 22 (Ohio Ct. App. 2001) (applying Delaware law). The standard of care applicable to the director of a Delaware corporation is a product of the common law and is not set forth in the corporate statute. States that follow the Delaware model for their corporate codes, such as Nevada, Oklahoma, and Texas, similarly do not have a statutory formula for the standard of care. By way of contrast, the Model Business Corporation Act (MBCA) includes a statutory formulation of the duty of care. The current MBCA formulation of a director's duty of care provides:

> The members of the board of directors or a committee of the board, when becoming informed in connection with their decision-making function or devoting attention to their oversight function, shall discharge their duties with the care that a person in a like position would reasonably believe appropriate under similar circumstances. MBCA § 8.30(b) (2002). Earlier versions of the MBCA provided that "[a] director shall discharge his duties . . . with the care an ordinary prudent person in a like position would exercise under similar circumstances."

MBCA § 8.30(a)(2) (1984). The former or current MBCA formulation has been adopted in the vast majority of the states, but not always without modification. For example, the Kentucky adoption of MBCA § 8.30(b) substitutes "honestly" for "reasonably." Ky. Rev. Stat. Ann. § 271B.8-300(1)(c) (Banks-Baldwin 2003). This substitution conforms the Kentucky statute to the language of Aronson v. Lewis.

[FN12]. The efficacy of relying upon a review of process has been oft criticized. See, e.g., Leo Herzel & Leo Katz, Smith v. Van Gorkom: The Business of Judging Business Judgment, 41 Bus. Law 1187, 1190 (1986) ("[N]o court will ever succeed in codifying the practices of a careful board. The Smith court's effort to do so was wasted. Bad decisions can be made while observing all the prescribed formalities of Smith; good decisions can be reached without them."). Recall that it was a failure to utilize what the court determined to be necessary procedural safeguards that stripped the Van Gorkom directors of the otherwise available protection of the business judgment rule notwithstanding the manifest advantages of the merger under consideration.

[FN13]. See, e.g., Radol v. Thomas, 772 F.2d 244, 256-57 (6th Cir. 1985); Holland v. Am. Founders Life Ins. Co. of Denver, 376 P.2d 162, 165- 66 (Colo. 1962); Neese v. Brown, 405 S.W.2d 577, 581 (Tenn. 1964). While certainly not resolvable within the confines of this article, and perhaps incapable of resolution at all, there does exist a conceptual disconnect between the business judgment rule as historically applied in corporations and as historically not applied in the general partnership. In the corporation, actual culpability, by application of the business judgment rule, has not existed until a director's breach of the duty of care rose to gross negligence or willful misconduct. This relaxed standard exists in a business entity characterized by limited liability and a separation of management from ownership (effectively stripping the actual owners of any ability to oversee the actions of the day-to-day managers and limiting the ability to oversee the actions of the board), as well as severely constrained information rights. By way of contrast, in the partnership, a form of organization highlighted by unlimited exposure to debts and obligations, the unification of ownership and management, and exceptional information rights, we find there is authority for holding actors liable for violation of a stricter standard of "reasonable care." It is somewhat counter-intuitive that in the organization with the greatest opportunity for fiduciary abuse, namely the corporation, the standard of culpability may be more relaxed than in the partnership, the entity in which there is the highest degree of oversight.

[FN14]. See, e.g., Kaplan v. Centex Corp., 284 A.2d 119, 124 (Del. Ch. 1971).

[FN15]. See, e.g., Smith v. Van Gorkom, 488 A.2d 858, 870-71 (Del. 1985); Aronson v. Lewis, 473 A.2d 805, 812 (Del. 1984); In re Walt Disney Co. Derivative Litig., 825 A.2d 275, 279 (Del. Ch. 2003).

[FN16]. See, e.g., FDIC v. Castetter, 184 F.3d 1040, 1046 (9th Cir. 1999) (applying California law); Aronson, 473 A.2d at 812; M.D. Bldg. Material Co. v. 910 Constr. Venture, 579 N.E.2d 1059, 1065 (Ill. App. 1991) (concluding business judgment rule not available to general partners when charged with self-dealing); Haydinger v. Freedman, No. 98-3045, 2000 U.S. Dist. LEXIS 7924, at *29-*30 (E.D. Pa. June 8, 2000) (same).

[FN17]. See, e.g., FDIC v. Jackson, 133 F.3d 694, 699 (9th Cir. 1998); Katz v. Chevron Corp., 27 Cal. Rptr.2d 681, 689 (Cal. Ct. App. 1994); Aronson, 473 A.2d at 812.

[FN18]. See, e.g., McMullin v. Beran, 765 A.2d 910, 917 (Del. 2000); Cede & Co. v. Technicolor, Inc., 634 A.2d 345, 361 (Del. 1983); Aronson, 473 A.2d at 812.

[FN19]. See, e.g., McMullin, 765 A.2d at 917; Cede & Co., 634 A.2d at 361; Aronson, 473 A.2d at 812.

[FN20]. The American Law Inst., Principles of Corp. Governance: Analysis and Recommendations (1994) [hereinafter ALI-PCG].

[FN21]. Id. § 4.01(c). The standard of care to which this business judgment rule applies, set forth in ALI-PCG § 4.01(a), provides in part:

> A director or officer has a duty to the corporation to perform the director's or officer's functions in good faith, in a manner that he or she reasonably believes to be in the best interests of the corporation, and with the care that an ordinarily prudent person would reasonably be expected to exercise in a like position and under similar circumstances.

For a discussion of the business judgment rule as embodied in the ALI-PCG, see generally Charles Hansen, The Duty of Care, the Business Judgment Rule, and The American Law Institute Corporate Governance Project, 48 Bus. Law. 1355 (1993).

[FN22]. Douglas M. Branson, The Rule That Isn't a Rule-The Business Judgment Rule, 36 Val. U. L. Rev. 631, 635-36 (2002).

[FN23]. Section 8.31 of the MBCA provides:

> (a) A director shall not be liable to the corporation or its shareholders for any decision to take or not to take action, or any failure to take any action, as a director, unless the party asserting liability in a proceeding establishes that:
> (1) any provision in the articles of incorporation authorized by section 2.02(b)(4) or the protection afforded by section 8.61 for action taken in compliance with section 8.62 or 8.63, if interposed as a bar to the proceeding by the director, does not preclude liability; and
> (2) the challenged conduct consisted or was the result of:
>> (i) action not in good faith; or
>> (ii) a decision

(A) which the director did not reasonably believe to be in the best interests of the corporation, or
(B) as to which the director was not informed to an extent the director reasonably believed appropriate in the circumstances; or
(iii) a lack of objectivity due to the director's familial, financial or business relationship with, or a lack of independence due to the director's domination or control by, another person having a material interest in the challenged conduct
(A) which relationship or which domination or control could reasonably be expected to have affected the director's judgment respecting the challenged conduct in a manner adverse to the corporation, and
(B) after a reasonable expectation to such effect has been established, the director shall not have established that the challenged conduct was reasonably believed by the director to be in the best interests of the corporation; or
(iv) a sustained failure of the director to devote attention to ongoing oversight of the business and affairs of the corporation, or a failure to devote timely attention, by making (or causing to be made) appropriate inquiry, when particular facts and circumstances of significant concern materialize that would alert a reasonably attentive director to the need therefor; or
(v) receipt of a financial benefit to which the director was not entitled or any other breach of the director's duties to deal fairly with the corporation and its shareholders that is actionable under applicable law.

MBCA § 8.31.

[FN24]. MBCA 8.31, cmt., Note on the Business Judgment Rule.

[FN25]. See, e.g., 1 Dennis J. Block et al., The Business Judgment Rule-Fiduciary Duties of Corporate Directors 6 (5th ed. 1998), quoting:

> Some have suggested that, within the business judgment standard's broad ambit, a distinction might usefully be drawn between that part which protects directors from personal liability for the decision they make and the part which protects the decision itself from attack. While these two objects of the business judgment standard's protection are different, and judicial review might result in the decision being enjoined but no personal liability (or vice versa), their operative elements are identical (i.e., good faith, disinterest, informed judgment and "best interests"). As a consequence, the courts have not observed any distinction in terminology and have generally followed the practice of referring only to the business judgment rule, whether dealing with personal liability issues or transactional justification matters.

Id. (quoting MBCA § 8.31, cmt., note on the Business Judgment Rule).

[FN26]. See Block et al., supra note 25, at 12-18. See also 3A Fletcher et al., supra note 2, § 1037 (providing similar justifications).

[FN27]. See, e.g., Washington Bancorp v. Said, 812 F. Supp. 1256, 1267- 68 (D.D.C. 1993) ("Courts recognize that even disinterested, well-intentioned, informed directors can make decisions that, in hindsight, [are] improvident."); Air Line Pilots Ass'n v. UAL Corp., 717 F. Supp. 575, 582 (N.D. Ill. 1989), aff'd, 897 F.2d 1394 (7th Cir. 1990) (stating that the business judgment rule "encourages competent individuals to become directors who otherwise might decline for fear of personal liability"); S. Samuel Arsht, The Business Judgment Rule Revisited, 8 Hofstra L. Rev. 93, 97 (1979) ("[P]ersons of reason, intellect and integrity would not serve as directors if the law exacted from them a degree of prescience not possessed by people of ordinary knowledge.").

[FN28]. See, e.g., Resolution Trust Corp. v. Blasdell, 930 F. Supp. 2d 417, 423 (D. Ariz. 1994), stating:

> Directors . . . regularly make complex decisions involving risk, and many such decisions may appear in hind-

> sight to have been made improvidently. . . . [O]ur country's corporate system depends to a degree on the willingness of corporations to take risk. With large sums of money at stake-and the threat of litigation in the event of failure correspondingly high-few directors would recommend ventures involving more than minimal risk.

Id. (citations omitted). See also Air Line Pilots Ass'n, 717 F. Supp. at 582.

> The business judgment rule encourages directors to engage in ventures which have potential for great profit but which may entail some risk. Commonly cited support for this proposition is the speculation that if stricter liability were imposed on directors, the founders of McDonald's Corporation who put $3 million at risk to patent a novel hamburger manufacturing technique might never have made this profitable decision.

Id. (citations omitted). See also Herzel & Katz, supra note 12, at 1189 ("Another thing the court failed to appreciate is the need to help directors be bold. The threat of crushing legal liability will make them too cautious.").

[FN29]. See, e.g., FDIC v. Stahl, 89 F.3d 1510, 1517 (11th Cir. 1996) (quoting Int'l Ins. Co. v. Johns, 874 F.2d 1447, 1458 n.20 (11th Cir. 1989)) ("[D]irectors are, in most cases, more qualified to make business decisions than are judges."); Dodge v. Ford Motor Co., 170 N.W. 668, 684 (Mich. 1919); In re J.P. Stevens & Co. S'holders Litig., 542 A.2d 770, 780 (Del. Ch. 1988).

> Because businessmen and women are correctly perceived as possessing skills, information and judgment not possessed by reviewing courts and because there is great social utility in encouraging the allocation of assets and the evaluation and assumption of economic risk by those with such skill and information, courts have long been reluctant to second-guess such decisions when they appear to have been made in good faith.

Id. (quoting Solash v. Telex Corp., Nos. 9518, 9528 & 9525, 1988 Del. Ch. LEXIS 7, at *21 (Del. Ch. Jan. 19, 1988), reprinted in 13 Del. J. Corp. L. 1250, 1262 (1988)). See also Kamen v. Kemper Fin. Servs., Inc., 908 F.2d 1338, 1343 (7th Cir. 1990), rev'd on other grounds, 500 U.S. 90 (1991), which states: "Managers who make such judgment calls poorly ultimately give way to superior executives; no such mechanism 'selects out' judges who try to make business decisions. In the long run firms are better off when business decisions are made by business specialists, even granting the inevitable errors." A corollary of this rationale is that it preserves judicial resources, a benefit not to the corporation, but to the legal system as a whole.

[FN30]. See, e.g., Michael P. Dooley & E. Norman Veasey, The Role of the Board in Derivative Litigation: Delaware Law and the Current ALI Proposals Compared, 44 Bus. Law. 503, 522 (1989), stating:

> The power to hold to account is the power to interfere and, ultimately, the power to decide. If stockholders are given too easy access to courts, the effect is to transfer decisionmaking power from the board to the stockholders or, more realistically, to one or a few stockholders whose interests may not coincide with those of the larger body of stockholders. By limiting judicial review of board decisions, the business judgment rule preserves the statutory scheme of centralizing authority in the board of directors. In doing so, it also preserves the value of centralized decisionmaking for the stockholders and protects them against unwarranted interference in that process by one of their number. Although it is customary to think of the business judgment rule as protecting directors from stockholders, it ultimately serves the more important function of protecting stockholders from themselves.

See also In re Consumers Power Co. Derivative Litig., 132 F.R.D. 455, 464 (E.D. Mich. 1990) (stating that the business judgment rule "protect[s] the corporation and its stockholders from other stockholders where only the 'duty of care' and not the 'duty of loyalty' is at issue") (citation omitted).

[FN31]. See, e.g., Hilton Hotels Corp. v. ITT Corp., 978 F. Supp. 1342, 1351 (D. Nev. 1997) ("'[O]ne of the justifications for the business judgment rule[] . . . is that unhappy shareholders can always vote the directors out of office.'") (quoting Shoed v. Amerco, 885 F. Supp. 1332, 1340 (D. Nev. 1994)).

[FN32]. See, e.g., Van de Walle v. Unimation, Inc., [1990-1991 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶ 95,834, at 99,030-31 (Del. Ch. Mar. 6, 1991), stating: "[W]here corporate fiduciaries, because of a conflict, are disabled from safeguarding the interests of the stockholders to whom they owe a duty, the Court will furnish compensatory procedural safeguards by imposing upon the fiduciaries an exacting burden of establishing the utmost propriety and fairness of their actions."

[FN33]. See William T. Allen et al., Function Over Form: A Reassessment of Standards of Review in Delaware Corporation Law, 56 Bus. Law. 1287, 1295-96 (2001), reprinted in 26 Del. J. Corp. Law 859, 867-69 (2001), which states:

> A judicial standard of review is a value-laden analytical instrument that reflects fundamental policy judgments. In corporate law, a judicial standard of review is a verbal expression that describes the task a court performs in determining whether action by corporate directors violated their fiduciary duty. Thus, in essential respects, the standard of review defines the freedom of action (or, if you will, deference in the form of freedom from intrusion) that will be accorded the persons who are subject to its reach.
>
> There exists a close, but not perfect, relationship, between the standard by which courts measure director liability (the "standard of review") and the standard of behavior that we normatively expect of directors (the "standard of conduct"). As Professor Melvin Eisenberg expressed this idea in his thoughtful article on corporate standards of review, "[a] standard of conduct states how an actor should conduct a given activity or play a given role. A standard of review states the test a court should apply when it reviews an actor's conduct to determine whether to impose liability or grant injunctive relief." Standards of conduct are sometimes referred to as "conduct rules" that are addressed to corporate directors and officers, whereas standards of review are "decision rules" that are addressed to judges.
>
> In most areas of law, standards of conduct and standards of review tend to conflate and become one and the same, but in corporate law the two standards often diverge. The reasons are rooted in policy interests. First, directors must make decisions in an environment of imperfect information. Second, given the limited investment in publicly held firms that typical corporate directors are able or willing to make, any risk of liability would likely dwarf the incentives for assuming the role. Third, courts are ill-equipped to determine after-the-fact whether a particular business decision was reasonable in the circumstances confronting the corporation.
>
> The interplay of these considerations can be illustrated by considering how judges review board decisions under the business judgment standard. Where the business judgment standard applies, a director will not be held liable for a decision-even one that is unreasonable-that results in a loss to the corporation, so long as the decision is rational. In this review context, the business judgment standard ("rationality") diverges from, and becomes more lenient than, the normative standard of expected conduct ("reasonableness"). The justifications for this divergence have been thoroughly stated elsewhere, and will not be repeated here. Suffice it to say that we endorse a corporate law regime which affords substantial freedom of action to disinterested, well-motivated directors.

Id. (citations omitted).

[FN34]. Id. at 1296, reprinted in 26 Del. J. Corp. L. at 868.

[FN35]. Aronson, 473 A.2d at 812.

[FN36]. See MBCA § 8.31(b)(1) (imposing on a party seeking to hold a director liable for money damages the burden of establishing that the corporation has suffered harm proximately caused by the director's conduct).

[FN37]. Id. § 8.31, cmt. 1.h.

> Under case law, personal liability as well as transactional justification issues will be subject to a fairness standard of judicial review if the plaintiff makes out a credible claim of breach of the duty of loyalty or if the pre-

> sumptions of the business judgment standard (e.g., an informed judgment) are overcome, with the burden of proof shifting from the plaintiff to the defendant.

[FN38]. See supra note 25.

[FN39]. Examples of such provisions include Del. Code Ann. tit. 8 § 102(b)(7) (2001); MBCA §§ 2.02(b)(4), 8.31; Ky. Rev. Stat. Ann. § 271B.8- 300(5)(b) (Banks-Baldwin 2003).

[FN40]. Martin I. Lubaroff & Paul M. Altman, Lubaroff & Altman on Delaware Limited Partnerships § 11.2.4 (2005). See also S. 533, 133d D. Gen. Assembly 2, 5 Del. Laws, ch. 289, §§ 1-2 (1986) (commentary to Section 102(b)(7)) ("This provision would have no effect on the availability of equitable remedies, such as injunction or rescission, for breach of fiduciary duty."); William E. Knepper & Dan A. Bailey, Liability of Corporate Officers and Directors § 7.04, at 217 (4th ed. 1988) ("The commentators agree that the new section [102(b)(7)] does not eliminate or alter a director's fiduciary duty of care."); E. Norman Veasey et al., Delaware Supports Directors With a Three-Legged Stool of Limited Liability, Indemnification, and Insurance, 42 Bus. Law. 399, 403 (1987), which states:

> [S]ection 102(b)(7) does not eliminate the duty of care that is properly imposed upon directors. Directors continue to be charged under Delaware law with a duty of care in the decisionmaking process and in their oversight responsibilities. The duty of care continues to have vitality in remedial contexts as opposed to actions for personal monetary damages against directors as individuals. For example, it will continue to be vitally important in injunction and rescission cases and may well be relevant in elections, proxy contests, resignations, and removal contexts.

Id. Because the provisions in a partnership agreement addressing the liability of a general partner and the indemnification of a general partner are generally provisions that protect a general partner, the question is frequently raised whether or not these provisions are relevant to the fiduciary duty of a general partner. An argument can be made that limitations on a general partner's liability define the scope of the fiduciary duty of the general partner. Where, for example, a partnership agreement provides that a general partner has no liability to a limited partnership or to other partners except with respect to its gross negligence or willful misconduct, it could be argued that the fiduciary duty of the general partner is to act without gross negligence or willful misconduct. To the extent the fiduciary duty of a general partner is defined by such provisions, it is important to make certain that the provisions of a partnership agreement, which arguably relate to a general partner's fiduciary duty, are consistent throughout the partnership agreement. For instance, if one provision in a partnership agreement states or implies that a general partner has a duty to act without negligence, a provision exonerating a general partner from liability for negligence would be inconsistent. The creation of such ambiguities should be avoided.

[FN41]. Unif. P'shp Act (1914) [hereinafter UPA], 6 Pt. I U.L.A. 373 (2001).

[FN42]. Unif. P'shp Act (1997) [hereinafter RUPA], 6 Pt. I U.L.A. 58 (2001). In response to a proposal for updating set forth in UPA Revision Subcommittee of the Committee on Partnerships and Unincorporated Business Organizations, Should the Uniform Partnership be Revised?, 43 Bus. Law. 121 (1987), the UPA was revised and initially released in 1992. The 1992 version was subsequently revised in 1993 and again in 1994. Limited liability partnership provisions were added in 1996, and additional amendments were added in 1997. Through much of its consideration by the National Conference of Commissioners on Uniform State Laws (NCCUSL), it was referred to as the Revised Uniform Partnership Act. In 1994, the "Revised" was dropped. Nonetheless, "Revised Uniform Partnership Act" and "RUPA" have become firmly fixed as the colloquial name of the act, and "RUPA" is in fact used in NCCUSL's prefatory note to the act. All references herein to "RUPA" are to the Uniform Partnership Act (1997).

[FN43]. UPA § 15 provides:

> All partners are liable
>
> (a) Jointly and severally for everything chargeable to the partnership under sections 13 and 14.
>
> (b) Jointly for all other debts and obligations of the partnership; but any partner may enter into a separate obligation to perform a partnership contract.

6 Pt. I U.L.A. 613 (2001).

[FN44]. RUPA § 306(a), 6 Pt. I U.L.A. 117 (2001).

[FN45]. The limited liability partnership (LLP) was devised in Texas in 1991 in an effort to address the vicarious liability among partners for the errors of any individual partner by providing a limited exception to the liability provision of UPA § 15. See, e.g., Alan R. Bromberg & Larry E. Ribstein, Bromberg & Ribstein on Limited Liability Partnerships, the Revised Uniform Limited Partnership Act, and the Uniform Limited Partnership Act (2001) § 1.01(a) (2002 ed.), which states in part:

> The limited liability partnership (LLP) originated in Texas in 1991 to protect against a limited list of torts. It was inspired by the government suits against law and accounting firms that had done work for the freewheeling savings and loan and thrift associations that failed in large and costly numbers in the 1980s along with the collapse of real estate values they had helped to inflate. The suits alleged joint and several liability claims under U.P.A. § 15 for various kinds of malpractice or other tortious misconduct. The claims were against all partners including many who had nothing to do with the failed associations. The suits highlighted the vicarious liability of partners for each other's conduct, a liability that did not exist in other forms of professional organization.

Adoption of similar statutes proceeded with Louisiana in 1992 and Delaware, the District of Columbia and North Carolina in 1993. Id. § 1.01(b). As these further state adoptions advanced, Texas was revising its LLP provisions to address circumstances not anticipated in the admittedly rushed effort to adopt the first statute in 1991. Id. § 1.01(a).

As originally conceived, the LLP would be the entity of choice for professional firms unable to make use of the limited liability company and the limited liability protections afforded thereby. In place thereof, the first LLP statutes provided "partial shield" liability protection. Under these formulations, the partners would be protected from vicarious liability by a modification to the state's adoption of UPA § 15 through a proviso that the partners would not have vicarious liability for claims arising out of some statutory formulation intended to address claims arising in malpractice, malfeasance, or other professional negligence. See, e.g., Ky. Rev. Stat. Ann. § 362.220(2) (Banks-Baldwin 2003) (stating that a partner in an LLP organized in Kentucky was not liable for partnership debts "arising from negligence, malpractice, wrongful acts, or misconduct"). By providing limited liability from such professional claims, the partners were not shielded from claims arising in the ordinary course of business. In effect, vicarious liability was retained with respect to voluntary creditors of the partnership, while vicarious liability was eliminated with respect to involuntary creditors. The scope of the limited liability afforded by the LLP was first expanded in 1994 with Minnesota's adoption of a "full shield" liability shield statute (Minn. Stat. Ann. § 323.14(subd.2) (West 1995) (repealed 1997)), which eliminated vicarious liability regardless of the nature of the claim. The full-shield approach was eventually adopted in RUPA. As of this date, all states have adopted LLP legislation in either a partial shield or full shield format. See Elizabeth G. Hester & Thomas E. Rutledge, Practical Guide to Limited Liability Partnerships, in 5 State Limited Liability Company and Partnership Laws §§ 10.1, 10.2, PGLLP-1 (Elizabeth S. Miller & Arthur J. Jacobson eds., Supp. 2004).

[FN46]. RUPA § 306(c), 6 Pt. I U.L.A. 117, provides:

> An obligation of a partnership incurred while the partnership is a limited liability partnership, whether arising in contract, tort, or otherwise, is solely the obligation of the partnership. A partner is not personally liable, directly or indirectly, by way of contribution or otherwise, for such an obligation solely by reason of being or so acting as a partner. This subsection applies notwithstanding anything inconsistent in the partnership agreement that ex-

> isted immediately before the vote required to become a limited liability partnership under Section 1001(b).

See also Elizabeth S. Miller, Highlights of the Uniform LLP Amendments, PUBOGRAM Newsletter (ABA Section of Business Law), Dec. 1996, available at http://www.abanet.org/buslaw/partners/pubogram/1996_98/11-1highlights.html, reprinted in Prototype LLP Agreement Subcommittee of the Committee on Partnerships and Unincorporated Business Organizations, Prototype Partnership Agreement for a Limited Liability Partnership Formed Under the Uniform Partnership Act (1997), 58 Bus. Law. 689 (2003).

> To counter the erosion of the liability shield that would take place if a partner were required to contribute to satisfy partnership obligations, RUPA section 306(c) provides that a partner in an LLP will not be liable, "directly or indirectly, by way of contribution of otherwise," for a partnership obligation solely by reasons of being a partner. RUPA section 306(c) goes on to provide that inconsistent provisions of the partnership agreement in effect immediately before the vote to become an LLP are not effective with respect to partnership obligations incurred after the partnership becomes an LLP. Thus, previously negotiated contribution provisions that would otherwise require a partner to contribute towards obligations of the partnership arising after the partnership becomes an LLP are "trumped" by the election to become an LLP.

Id. at 690 (footnotes omitted).

[FN47]. See UPA §§ 19-21 (setting forth the statutory underpinnings of the fiduciary nature of the partner relationship). See also UPA §§ 4(3), 9(1); Restatement (Second) of Agency § 13 (1958). UPA § 21, oft cited as the statutory formulation of the fiduciary duties amongst the partners, does not use the term "fiduciary" in its text, but only in its title, stating at subsection (1):

> Every partner must account to the partnership for any benefit, and hold as trustee for it any profits derived by him without the consent of the other partners from any transaction connected with the formation, conduct, or liquidation of the partnership or from any use by him of its property.

UPA § 21(1), 6 Pt. II U.L.A. 194 (2001).

As noted in Official Comment 1 to RUPA § 404, this provision "is structurally different from the UPA which touches only sparingly on a partner's duty of loyalty and leaves any further development of the fiduciary duties of partners to the common law of agency." RUPA § 404, cmt. 1, 6 Pt. I U.L.A. 143 (2001).

[FN48]. Meinhard v. Salmon, 164 N.E. 545, 546 (N.Y.1928). This language, however, has been criticized as overstating partner obligations. See, e.g., Robert W. Hillman, Private Ordering Within Partnerships, 41 U. Miami L. Rev. 425 (1987), which states:

> Although colorful, the judicial rhetoric inevitably overstates the standard of conduct the law actually imposes on partners. If partners truly are fiduciaries, they are a unique species of this group and cannot be subjected to traditional standards applicable to other types of fiduciaries. . . . Partners . . . are always joint owners. . . . Partners are not disinterested trustees, and the likelihood that most partners operate under a "punctilio of an honor the most sensitive" standard is remote.

Id. at 458 (footnotes omitted). Perhaps the better description of the fiduciary duties of the partners in a UPA partnership is that set forth in Latta v. Kilbourn, 150 U.S. 524 (1893), which observed:

> [It is] well settled that one partner cannot, directly or indirectly, use partnership assets for his own benefit; that he cannot in conducting the business of a partnership, take any profit clandestinely for himself; that he cannot carry on the business of the partnership for his private advantage; that he cannot carry on another business in competition or rivalry with that of the firm, thereby depriving it of the benefit of his time, skill, and fidelity, without being accountable to his copartners for any profit that may accrue to him therefrom; that he cannot be permitted to secure for himself that which it is his duty to obtain, if at all, for the firm of which he is a member; nor can he avail himself of knowledge or information, which may be properly regarded as the property of the

> partnership, in the sense that it is available or useful to the firm for any purpose within the scope of the partnership business.

Id. at 541.

[FN49]. The emphasis on the duty of loyalty rather than the duty of care is, of course, in no way unique to the partnership context. Until relatively recently, the corporate law on the fiduciary duties of corporate directors was focused almost entirely upon the duty of loyalty, it being assumed that the duty of care was itself not separately enforceable. See Allen et al., supra note 33, at 1299, reprinted in 26 Del. J. Corp. Law at 872 ("Only toward the end of the twentieth century did Delaware's corporation law first accord 'bite' to the duty of care."); Michele Healy Ubelaker, Director Liability Under the Business Judgment Rule: Fact or Fiction?, 35 Sw. L. J. 775, 789 (1981) ("The modern view [of a corporate director's fiduciary duty] definitely stresses the duty of loyalty, and avoids specific discussion of the parameters of due care.").

[FN50]. See 2 Alan R. Bromberg & Larry E. Ribstein, Bromberg and Ribstein on Partnership § 6.07(f) (2005) (footnote omitted). See also infra notes 119-36 and accompanying text.

[FN51]. Norwood P. Beveridge, Jr., Duty of Care: The Partnership Cases, 15 Okla. City U. L. Rev. 753, 754 (1990).

[FN52]. Bromberg & Ribstein, supra note 50, § 6.07(f).

[FN53]. J. William Callison & Maureen A. Sullivan, Partnership Law and Practice: General and Limited Partnerships § 12.02, at 2-6 to 12-10 (2004).

[FN54]. See also Gerard C. Martin, Duties of Care Under the Revised Uniform Partnership Act, 65 U. Chi. L. Rev. 1307, 1309-10 (1998), which states, "While most courts and scholars agree that partners owe each other some duty of care under the UPA, there are some who argue the partners owe each other no duty of care whatsoever. Additionally, others disagree strongly about what that duty is."

[FN55]. See, e.g., Claire Moore Dickerson, Is It Appropriate to Appropriate Corporate Concepts: Fiduciary Duties and the Revised Uniform Partnership Act, 64 U. Colo. L. Rev. 111 (1993):

> The most fundamental duty owed by partners to one another is a fiduciary duty. Partners may, however, believe that by mutual consent they can restrict or virtually eliminate these mutual obligations. Under current partnership law, this belief is probably mistaken; under most present judicial interpretations of the Uniform Partnership Act (UPA), fiduciary duties are mandatory provisions waivable only with informed consent, on a case-by-case basis.

Id. (footnotes omitted)

[FN56]. See RUPA § 404, 6 Pt. I U.L.A. 143 (2001). Section 404 specifies a partner's duty of loyalty and duty of care and states that these duties are the "only" fiduciary duties that partners owe to the partnership or other partners.

[FN57]. Id. § 404(c), 6 Pt. I U.L.A 143 (2001). In addition, RUPA § 404(d) provides: "A partner shall discharge the duties to the partnership and the other partners under this [Act] or under the partnership agreement and exercise any rights consistently with the obligation of good faith and fair dealing."

[FN58]. See id. §§ 103(a), 103(b)(4), 6 Pt. I U.L.A. 73 (2001) (providing that the relations among the partners and between the partners and the partnership are governed by the partnership agreement, but that the partnership agreement may not unreasonably reduce the duty of care otherwise applicable under Section 404(c) or 603(b)(3)).

[FN59]. RUPA § 404(d) (1991 Draft) provided: "A partner has a duty to act in the conduct of the business of the partnership in a manner which does not constitute gross negligence or willful misconduct. An error in judgment or a failure to use ordinary skill and care does not constitute gross negligence." See also Donald J. Weidner, Three Policy Decisions Animate Revisions of Uniform Partnership Act, 46 Bus. Law. 427, 468 (1991).

[FN60]. Contrast the Texas Revised Partnership Act, which states the duty of care in terms of ordinary care and incorporates a business judgment rule as follows:

> (c) Care. A partner's duty of care to the partnership and the other partners is to act in the conduct and winding up of the partnership business with the care an ordinarily prudent person would exercise in similar circumstances. An error in judgment does not by itself constitute a breach of this duty of care. A partner is presumed to satisfy this duty if the partner acts on an informed basis and in compliance with Subsection (d).

Tex. Rev. Civ. Stat. Ann. art. 6132b-4.04(c) (Vernon Supp. 2003).

Subsection (d) provides:

> (d) Method of Discharge. A partner shall discharge the partner's duties to the partnership and the other partners under this Act or under the partnership agreement, and exercise any rights and powers in the conduct or winding up of the partnership business:
>
> (1) in good faith; and
>
> (2) in a manner the partner reasonably believes to be in the best interest of the partnership.

Id. art. 6132b-4.04(d).

[FN61]. 543 A.2d 348 (Me. 1988).

[FN62]. See infra notes 119-21 and accompanying text.

[FN63]. Cf. Smith v. Van Gorkom, 488 A.2d 858 (Del. 1985); Aronson v. Lewis, 473 A.2d 805 (Del. 1984).

[FN64]. See generally Allan W. Vestal, A Comprehensive Uniform Limited Partnership Act? The Time Has Come, 28 U.C. Davis L. Rev. 1195 (1995) (commenting on the desirability of revising the law of limited partnerships and its separation from the law of general partnerships).

[FN65]. The Uniform Limited Partnership Act (2001) is the successor to the Uniform Limited Partnership Act (1976) with 1985 Amendments. The Uniform Limited Partnership Act (1976) was the successor to the Uniform Limited Partnership Act (1916), often referred to as ULPA. With the 1985 Amendments, the 1976 Uniform Limited Partnership Act is commonly referred to as the Revised Uniform Limited Partnership Act, or RULPA. See ReRULPA Prefatory Note, 6A U.L.A. 2-3 (2003). The uniform act approved in 2001, a comprehensively re-written limited partnership law as contrasted with a mere revision and supplementation, was commonly referred to throughout the drafting process as ReRULPA (the "Revision" of RULPA), and that unofficial acronym is used herein.

[FN66]. ReRULPA §§ 303, 408(c), 6A U.L.A. 46, 62 (2003); see infra notes 75-77 and accompanying text.

[FN67]. ReRULPA § 404(c), 6A U.L.A. 57 (2001).

[FN68]. Compare RULPA § 303, 6A U.L.A. 324 (2003) with ReRULPA § 303, 6A U.L.A. 46 (2003).

[FN69]. Unif. Ltd. P'ship Act (1916), 6A U.L.A. 312 (1995).

[FN70]. RULPA § 403 (amended 1985) provides:

> (a) Except as provided in this [Act] or the partnership agreement, a general partner of a limited partnership has the rights and powers and is subject to the restrictions of a partner in a partnership without limited partners.

> (b) Except as provided in this [Act], a general partner of a limited partnership has the liabilities of a partner in a partnership without limited partners to persons other than the partnership and the other partners. Except as provided in this [Act] or in the partnership agreement, a general partner of a limited partnership has the liabilities of a partner in a partnership without limited partners to the partnership and to the other partners.

RULPA § 403 (amended 1985), 6A U.L.A. 365 (2003).

RULPA § 1105 provides: "In any case not provided for in this [Act] the provisions of the Uniform Partnership Act govern." RULPA (amended 1985), 6A U.L.A. 547 (2003).

[FN71]. See supra note 47 and accompanying text.

[FN72]. See supra notes 56-58 and accompanying text.

[FN73]. See generally Elizabeth S. Miller, Linkage and Delinkage: A Funny Thing Happened to Limited Partnerships When The Revised Uniform Partnership Act Came Along, 37 Suffolk U. L. Rev. 891 (2004) (discussing the "linkage" debate); Larry E. Ribstein, Linking Statutory Forms, 58 Law & Contemp. Probs. 187, 187 (1995) (finding that "[a]lthough linkage has long been an accepted feature of the law of business associations, it creates confusion about the applicable law . . . [and] may cause application of inappropriate rules to linked business forms"); Vestal, supra note 64, at 1196 (stating that "[t]he nexus [between general partnership law and limited partnership law] is no longer clear, the substance is no longer appropriate, and the uniformity (and the associated benefit of stability for limited partnerships) is fast disappearing").

[FN74]. See ReRULPA Prefatory Note, 6A U.L.A. 2-3 (2003) (discussing the drafting committee's rationale for rejecting linkage and drafting a stand-alone statute).

[FN75]. ReRULPA § 408(c), 6A U.L.A. 62 (2003). In addition, ReRULPA § 408(d) provides: "A general partner shall discharge the duties to the partnership and the other partners under this [Act] or under the partnership agreement and exercise any rights consistently with the obligation of good faith and fair dealing." Id.

[FN76]. See RUPA § 404(c), 6 Pt. I U.L.A. 143 (2001).

[FN77]. ReRULPA § 110(b)(6), 6A U.L.A. 24 (2003).

[FN78]. Id. § 305(a), 6A U.L.A. 51.

[FN79]. See id. § 305, cmt., 6A U.L.A. 51.

[FN80]. See supra notes 59-63 and accompanying text.

[FN81]. See generally Robert R. Keatinge et al., The Limited Liability Company: A Study of the Emerging Entity, 47 Bus. Law. 375 (1992) (discussing the LLC as an emerging entity); Larry E. Ribstein, The Emergence of the Limited Liability Company, 51 Bus. Law. 1 (1995) (discussing the rapid growth and acceptance of LLCs).

[FN82]. See Unif. Ltd.Liab. Co. Act (1996), Prefatory Note, 6A U.L.A.554 (2003) [hereinafter ULLCA] ("The allure of the limited liability company is its unique ability to bring together in a single business organization the best features of all other business forms-properly structured, its owners obtain both a corporate-styled liability shield and the pass-through tax benefits of a partnership."). The very first LLC statutes are generally characterized as "bulletproof," in that these statutes provided for minimal flexibility with respect to certain entity characteristics pertinent to the federal tax classification of the LLC and, as those tax classifications regulations were generally interpreted, these statutes would assure partnership classification. There arose a second generation of LLC acts, characterized as "flexible," which provided default rules with respect to those tax classification items that would provide for partnership classification. With the flexibility to modify those default rules, however, came the risk of inadvertent failure to meet the requirements for partnership tax classification of an LLC. The third generation of LLC statutes arose after the adoption of the check-the-box classification regulations effective January 1, 1997. These post-check-the-box statutes have largely eliminated those aspects of the prior statutes that were crafted to meet the pre-check-the-box tax classification test.

[FN83]. See generally 1 Carter G. Bishop & Daniel S. Kleinberger, Limited Liability-Tax and Business Law § 1.01(3) (2003) (describing the evolution of the LLC from Wyoming to all fifty states, the District of Columbia, and the Virgin Islands); 1 Larry E. Ribstein & Robert R. Keatinge, Ribstein and Keatinge on Limited Liability Companies § 1:02, 1-7 to 1-10 (2003) (citing the historical development of LLC in all fifty states); Charles W. Murdock, Limited Liability Companies in the Decade of the 1990s: Legislative and Case Law Developments and Their Implications for the Future, 56 Bus. Law. 499, 499 (2001) (stating "Limited Liability Companies . . . are now authorized by statute in all states").

[FN84]. Am. Bar Ass'n Prototype Ltd. Liab. Co. Act (1992) (ABA Prototype). The ABA Prototype was completed in late 1992, and is reproduced at Ribstein & Keatinge, supra note 83, at App. B.

[FN85]. ULLCA (1996), 6A U.L.A. 553 (2003). ULLCA was completed in 1994, and was revised by 1996 in response to the check-the-box federal income tax classification regulations. See infra note 91 (listing states that have adopted ULLCA).

[FN86]. ULLCA § 409(c), 6A U.L.A. 600 (2003). This language is essentially identical to that set forth in RUPA § 404(c) and ReRULPA § 408(c). ULLCA § 409(d) provides: "A member shall discharge the duties to a member-managed company and the other members under this [Act] or under the operating agreement and exercise any rights consistently with the obligation of good faith and fair dealing." 6A U.L.A. 600.

[FN87]. ULLCA § 409(h)(2), 6A U.L.A. 601 (2003).

[FN88]. ULLCA § 103(b)(3), 6A U.L.A. 567 (2003).

[FN89]. ABA Prototype § 402(A). See also Ky. Rev. Stat. Ann. § 275.170(1) (Michie 2003) (adopting ABA Prototype § 402(A)).

[FN90]. The commentary to Section 402(A) of the ABA Prototype states:

> Subsection (A) sets forth the gross negligence standard of care for those participating in management. This is similar to the standard commonly applied to corporate directors, managing partners, or general partners of limited partnerships. In general, as long as managers avoid self-interested and grossly negligent conduct, their actions are protected by the business judgment rule. With respect to general partnerships, see RUPA §404(d).
>
> Although the duty of care has been formulated in similar terms for managers of all types of firms, as noted above there are important differences among firms that may result in variations in applying the general standard. The duty of care may be lower in a general partnership because the partners' individual liability makes it likely not only that managing partners will manage carefully, but that non-managing partners will at least take an active interest in management. At the other end of the spectrum, limited partners or shareholders in a publicly-traded corporation may not participate in management and may rely more heavily on the fiduciary duties of the general partners or directors. LLCs have members with limited liability, but can be expected to be closely held because management rights are not freely transferable, and therefore may lie between the two extremes. Moreover, there will be differences among LLCs. It is likely that the precise boundaries of the duty will be left

to develop by case law and operating agreement rather than by statutory provision.

Id. (emphasis added).

[FN91]. Alabama, Hawaii, Illinois, Montana, South Carolina, South Dakota, Vermont, and West Virginia have adopted ULLCA along with the Virgin Islands. ULLCA Table of Jurisdictions Wherein Act Has Been Adopted, 6A U.L.A. 553 (2003).

[FN92]. Ala. Code § 10-12-21(g), (k)(2) (2003); Haw. Rev. Stat. Ann. § 428-409(c) (Michie 2004); 805 Ill. Comp. Stat. Ann. 180/15-3(c) (West 2002); Mont. Code. Ann. § 35-8-310(3) (2003); S.C. Code Ann. § 33-44- 409(c) (Law. Co-op. Supp. 2003); S.D. Codified Laws § 47-34A-409(c) (Michie 2000); W. Va. Code Ann. § 31B-4-409(c) (Michie 2003). Vermont substituted an MBCA-based formulation of the duty of care. Vt. Stat. Ann. tit. 11, § 3059(c) (2003).

[FN93]. See Fla. Stat. Ann. § 608.4225(b) (West Supp. 2004); Or. Rev. Stat. § 63.155(3) (2003). The Colorado LLC act was recently amended to adopt the ULLCA formulation of the duty of care. Colo. Rev. Stat. § 7-80- 404(2) (as amended effective July 1, 2004). Prior to July 1, 2004, Colorado followed the MBCA model. See Colo. Rev. Stat. § 7-80-406(1) (2003). The California LLC act provides that LLC managers and managing members have the same fiduciary duties as general partners. Cal. Corp. Code § 17153 (West Supp. 2004). Since California has adopted RUPA, the result is a duty of care like that found in ULLCA.

[FN94]. Wis. Stat. Ann. § 183.0402(b), (d) (West 2002). Even a criminal violation would not violate the standard of conduct set by the statute if the member or manager had "no reasonable cause to believe the conduct was unlawful." Id. § 183.0402(b).

[FN95]. MBCA § 8.30(a) (1984). Section 8.30(a) formerly read as follows:

(a) A director shall discharge his duties as a director, including his duties as a member of a committee:

(1) in good faith;

(2) with the care an ordinarily prudent person in a like position would exercise under similar circumstances; and

(3) in a manner he reasonably believes to be in the best interests of the corporation.

Former Section 8.30(a) of the MBCA has been rewritten and divided into subsections (a) and (b). The current provisions read as follows:

(a) Each member of the board of directors, when discharging the duties of a director, shall act: (1) in good faith, and (2) in a manner the director reasonably believes to be in the best interests of the corporation.

(b) The members of the board of directors or a committee of the board, when becoming informed in connection with their decisionmaking function or devoting attention to their oversight function, shall discharge their duties with the care that a person in a like position would reasonably believe appropriate under similar circumstances.

MBCA § 8.30(a)-(b).

[FN96]. Alaska Stat. § 10.50.135(a) (Michie 2004); Conn. Gen. Stat. Ann. § 34-141(a) (West 2002); Ga. Code Ann. § 14-11-305(1) (2003); Iowa Code Ann. § 490A.706(1) (West 2003); La. Rev. Stat. Ann. § 12:1314(A)(1) (West 2003); Me. Rev. Stat. Ann. tit. 31, § 652(1) (West 2003); Mich. Comp. Laws Ann. § 450.4404(1) (West 2003); Minn. Stat. Ann. §§ 322B.663(1), 322B.69 (West 2004); Miss. Code Ann. § 79-29- 402(1) (2003); Mo. Ann. Stat. § 347.088.1 (West 2001); N.Y. Ltd. Liab. Co. Law § 409(a) (McKinney 2005); N.C. Gen. Stat. § 57C-3-22(b) (2003); N.D. Cent. Code § 10-32-86(1) (Supp. 2003); Ohio Rev. Code Ann. § 1705.29(B) (West 2003); Okla. Stat. Ann. tit. 18, § 2016(1) (West 1999); R.I. Gen. Laws § 7-16-17(a) (2002); Tenn. Code Ann. §§ 48-239-115(a), 48-240-102(b), 48-241-111(a) (2003); Vt. Stat. Ann tit. 11, § 3059(c) (1997). All of these statutes also include provisions entitling managers and managing members to rely on specified types of information and reports. Alaska Stat. § 10.50.135(a) (Michie 2004); Conn. Gen.

Stat. Ann. § 34-141(b) (West 2002); Ga. Code Ann. § 14-11-305(2) (2003); Iowa Code Ann. § 490A.706(2) (West 2003); La. Rev. Stat. Ann. § 12:1314(A)(2) (West 2003); Me. Rev. Stat. Ann. tit. 31, § 657 (West 2003); Mich. Comp. Laws Ann. § 450.4404(2) (West 2003); Minn. Stat. Ann. § 322B.663(2) (West 2004); Miss. Code Ann. § 79-29-402 (2) (2003); Mo. Ann. Stat. § 347.090 (West 2001); N.Y. Ltd. Liab. Co. Law § 409(b) (McKinney 2005); N.C. Gen. Stat. § 57C-3-22(b) (2003); N.D. Cent. Code § 10-32-86(2) (2003); Ohio Rev. Code Ann. § 1705.30 (West 2003); Okla. Stat. Ann. tit. 18, § 2016(2) (West 1999); R.I. Gen. Laws § 7-16-17(b) (2002); Tenn. Code Ann. §§ 48-239- 115(b), 48-240-102(c), 48-241-111(b) (2003); Vt. Stat. Ann. tit. 11, § 3059(i) (1999). The Louisiana statute goes on to provide that, notwithstanding the statutory duty of care imposed, a member or manager shall not be personally liable to the limited liability company or its members for monetary damages unless the member or manager acted in a grossly negligent manner or engaged in conduct demonstrating a greater disregard for the duty of care than gross negligence, including intentional tortious conduct or intentional breach of the duty of loyalty. La. Rev. Stat. Ann. § 12:1314(B) (West 2003). "Gross negligence" is defined in the statute as "reckless disregard of or carelessness amounting to indifference to the best interests of the limited liability company or the members thereof." Id. § 12:1314(C).

[FN97]. The Georgia statute merely requires that the belief be "in good faith" rather than "reasonable." Ga. Code Ann. § 14-11-305(1) (2003). The Maine statute requires only that managers and members act "with a view to the interests of the limited liability company." Me. Rev. Stat. Ann. tit. 31, § 652(1) (West 2003). The Iowa statute simply states that duties must be discharged "in a manner the manager believes to be in the best interests of the limited liability company." Iowa Code Ann. § 490A.706(1) (West 2003). The New York statute does not include any language along these lines.

[FN98]. Va. Code Ann. § 13.1-1024.1 (Michie 1999).

[FN99]. See Ark. Code Ann. § 4-32-402(1) (Michie 2001); Idaho Code § 53-622(1) (Michie 2000); Ind. Code Ann. §§ 23-18-4-2(a) to -4-10 (Michie 1999); Ky. Rev. Stat. Ann. § 275.170(1) (Michie 2003); N.H. Rev. Stat. Ann. § 304-C:31(IV), (V) (1995); N.J. Stat. Ann. §§ 42:2B-26, 42:2B-30 (West. Supp. 2003); N.M. Stat. Ann. § 53-19-16(B) (Michie 2003); Utah Code Ann. 48-2c-807(1) (2002); Wash. Rev. Code Ann. § 25.15.155(1) (West Supp. 2004). A number of these provisions are modeled quite closely or verbatim after the ABA Prototype.

[FN100]. These states are Arizona, Delaware, District of Columbia, Kansas, Maryland, Massachusetts, Nebraska, Nevada, Pennsylvania, Texas, and Wyoming. See Ribstein & Keatinge, supra note 83, app. 9-4, at 9-62 to 9-63 (charting the duty of care in LLC statutes).

[FN101]. For example, some of these state statutes include provisions protecting members and managers who rely in good faith on reports and information. See Del. Code Ann. tit. 6, § 18-406 (2001); Kan. Stat. Ann. § 17-7697 (2003); Mass. Gen. Laws Ann. ch. 156C, § 11 (West 2002). In addition, provisions authorizing the expansion or restriction of duties, or the limitation or elimination of liability for breach of a duty, imply the existence of traditional fiduciary duties. See Del. Code Ann. tit. 6, § 18- 1101(c) (2003); D.C. Code Ann. § 29-1020(a) (2004); Mass. Gen. Laws Ann. ch. 156C, §§ 8(b), 63(b) (West 2002); Tex. Rev. Civ. Stat. Ann. art. 1528n-2.20(B) (Vernon 2002).

[FN102]. See Ribstein & Keatinge, supra note 83, app. 9-6, at 9-68 to 9-69 (categorizing the approaches toward waiver of fiduciary duties in the state LLC statutes).

[FN103]. ULLCA § 103(b)(3), 6A U.L.A. 567. See also Fla. Stat. Ann. §§ 608.423(1), (2)(c) (West 2002); Haw. Rev. Stat. §§ 428-103(a)- (b) (2004); S.C. Code Ann. § 33-44-103(a)-(b) (Law. Co-op. Supp. 2003).

[FN104]. E.g., Iowa Code Ann. § 490A.707 (West 1999); Mich. Comp. Laws Ann. § 450.4407 (West 2001); N.Y. Ltd. Liab. Co. Law § 417 (McKinney 2005); N.D. Cent. Code § 10-32-86(5) (Supp. 2003); R.I. Gen. Laws § 7-16-18 (1999);

Va. Code Ann. § 13.1-1025 (Michie 1999).

[FN105]. See, e.g., Conn. Gen. Stat. Ann. § 34-143(1) (West 2002); Del. Code Ann tit. 6, § 18-1101(c), (e) (2003); Ky. Rev. Stat. Ann. § 275.180(1) (Michie 2003); Mass. Gen. Laws Ann. ch. 156C, § 63(b) (West 2002); Tex. Rev. Civ. Stat. Ann. art. 1528n-2.20(B) (Vernon 2002).

[FN106]. Del. Code Ann. tit. 6, § 18-1101(c) (2004) (emphasis added). The limited liability company agreement may not, however, eliminate the implied contractual covenant of good faith and fair dealing. Id. Prior to August 1, 2004, this provision stated that the fiduciary duties of a member or manager could be "expanded or restricted" by the operating agreement. The Delaware Supreme Court had indicated in dicta that similar language in the Delaware limited partnership statute did not authorize the elimination of a general partner's fiduciary duties, pointing to the absence of such express authorization in the statute. Gotham Partners, L.P. v. Hallwood Realty Partners, L.P., 817 A.2d 160, 167-68 (Del. 2002). In response to this opinion, the Delaware legislature amended both the limited partnership and limited liability company acts to expressly permit elimination of fiduciary duties. 2004 Del. Laws ch. 275 (H.B. 411) (eff. Aug. 1, 2004). See also Del. Code Ann. tit. 6, § 18-1101(e) (2004) (providing that a limited liability company agreement may limit or eliminate any and all liabilities of a member of manager for breach of contract and breach of fiduciary duty, except that a "limited liability company agreement may not limit or eliminate liability for an act or omission that constitutes a bad faith violation of the implied contractual covenant of good faith and fair dealing"). See also Allan G. Donn, Contractual Modification of Fiduciary Duties for Delaware Unincorporated Business Entities, 7 J. Passthrough Entities 21 (Nov./Dec. 2004); Paul M. Altman et al., Contractually Defining Duties of General Partners in Delaware Limited Partnerships, 19 Pubogram Newsletter (ABA Section of Business Law) 8 (July 2002).

[FN107]. ULLCA § 409(c), 6A U.L.A. 600 (2003); see also supra notes 85-89 and accompanying text.

[FN108]. As in the case of RUPA, it does not appear appropriate to further relax the standard of liability under the auspices of the business judgment rule since the statute appears to align the standard of care and the standard of liability. See supra notes 59-63 and accompanying text.

[FN109]. Supra notes 89-90 and accompanying text.

[FN110]. See, e.g., generally Credentials Plus, LLC v. Claderone, 230 F. Supp. 2d 890 (N.D. Ind. 2002) (stating members of LLCs owe a duty of loyalty and finding the duty was breached by an individual's competition with the LLC); Blackmore Partners, L.P. v. Link Energy LLC, 864 A.2d 80 (Del. Ch. 2004) (holding pleadings were sufficient to support an inference of disloyal conduct on the part of LLC managers who approved a sale of the LLC's assets that rendered the equity units worthless); Metro Communications Corp., BVI v. Advanced Mobilecomm Techs., Inc., 854 A.2d 121 (Del. Ch. 2004) (finding pleadings were sufficient to state claims against LLC managers for common law fraud and breach of fiduciary duties of loyalty and disclosure in connection with a bribery scheme leading to the collapse of the LLC); Solar Cells, Inc. v. True North Partners, LLC, No. 19,477, 2002 Del. Ch. LEXIS 38 (Del. Ch. Apr. 25, 2002) (granting injunctive relief based on reasonable probability the plaintiff member would prevail on its breach of duty of loyalty claim against the other member in connection with a squeeze-down merger); VGS, Inc. v. Castiel, No. 17,995, 2000 Del. Ch. LEXIS 122 (Del. Ch. Aug. 31, 2000), aff'd, 781 A.2d 696 (Del. 2001) (finding LLC managers breached their duty of loyalty by secretly orchestrating a squeeze-down merger of the LLC); Anest v. Audino, 773 N.E.2d 202 (Ill. App. 2002) (holding an LLC member breached his fiduciary duty to the other member by diverting a business opportunity of the LLC); Bio-Septic Sys., LLC v. Weiss, 60 P.3d 943 (Mont. 2002) (finding no breach of fiduciary duty where an LLC member received compensation as an independent contractor); TIC Holdings, LLC v. HR Software Acquisitions Group, Inc., 750 N.Y.S.2d 425 (N.Y. Sup. 2002), aff'd, 755 N.Y.S.2d 19 (N.Y. A.D. 1 Dept. 2003) (finding LLC manager was not entitled to summary judgment based on release provisions in the LLC operating agreement because the alleged breaches of fiduciary duty involved misconduct that cannot be released by such provisions); Jundt v. Jurassic Res. Dev., N. Am., L.L.C., 656 N.W.2d 15 (N.D. 2003) (holding that defendant LLC members did not violate their fiduciary duties by allegedly diverting business opportunities); McConnell v. Hunt Sport Enters., 725 N.E.2d 1193 (Ohio App. 1999) (concluding LLC members did not breach their duty of loyalty by competing with the LLC because the LLC operating agreement permitted members to compete); Flippo v. CSC Assocs. III, L.L.C., 547 S.E.2d 216 (Va. 2001) (finding LLC member breached his fiduciary duties by acting in his own interest and the statutory business judgment rule was inapplicable).

[FN111]. In a typical partnership, where partners participate in management and have equal liability for partnership obligations, the partners have the incentive and the power to monitor the partnership business, and a good faith standard is appropriate. See Susan Saab Fortney, Professional Responsibility and Liability Issues Related to Limited Liability Law Partnerships, 39 S. Tex. L. Rev. 399, 419-22 (1998); Susan Saab Fortney, Seeking Shelter in the Minefield of Unintended Consequences-The Traps of Limited Liability Law Firms, 54 Wash. & Lee L. Rev. 717, 751-52 (1997).

[FN112]. Stephen B. Presser, Thwarting the Killing of the Corporation: Limited Liability, Democracy, and Economics, 87 Nw. U.L. Rev. 148, 158 (1992):

> First [Easterbrook and Fischel] observe that if there were unlimited shareholder liability, shareholders would find it necessary to monitor closely the activities of their corporations in order to escape liability, and that the high cost of this monitoring would itself discourage investment. Further, they argue, the need for increased monitoring would render uneconomic their favored strategy of diversified investing, which now seems to attract risk-averse capital. Limited liability decreases the need for shareholder monitoring, since less is at risk, they claim, and thereby "makes diversification and passivity a more rational strategy and so potentially reduces the costs of operating the corporation."

Id. (quoting Frank H. Easterbrook & Daniel R. Fischel, The Economic Structure of Corporate Law 42 (1991) (footnotes omitted)).

[FN113]. The exceptions to this rule were the large accounting and legal partnerships that continued to operate in that format for a variety of reasons, including long held prejudices against the practice of the learned professions other than through the general partnership form, tax disincentives to practicing as a professional service corporation after that form became available in the 1960s, and rules of professional regulation that precluded or eliminated many of the benefits of other business forms. Recent years have seen the adoption of the limited liability partnership and the limited liability company as an alternative to the traditional partnership. See generally Robert W. Hillman, Organizational Choices of Professional Service Firms: An Empirical Study, 58 Bus.Law. 1387, 1389-95 (2003) (discussing various different business entities available to professional services firms and the benefits associated with the newer entities such as LLCs and LLPs); Thomas E. Rutledge, The Place (If Any) of the Professional Structure in Entity Rationalization, 58 Bus. Law. 1413, 1419-23 (Aug. 2003) (same).

[FN114]. Note, however, that this limitation is not complete. RUPA § 301, which vests in each partner apparent agency authority on behalf of the partnership in its ordinary course of business, will continue to limit the size of general partnerships as promoters seek to limit (control) agency.

[FN115]. For example, to date courts have shown a general reluctance to pierce the veil of the limited liability company (see cases collected in Elizabeth S. Miller, The First Decade of LLC and LLP Case Law: A Survey of Cases Dealing with Registered Limited Liability Partnerships and Limited Liability Companies, which appears in the program materials for "Partnerships and LLCs-Important Case Law Developments 2004" (American Bar Association, August 2004)), a reluctance that appropriately parallels the reluctance of courts to pierce the corporate veil. There are any number of other areas where the courts may be invited to analogize or borrow from the corporate context when an LLC statute fails to provide guidance. For example, absent statutory authorization, courts have differed as to whether LLC members may bring a derivative action. See generally Weber v. King, 110 F. Supp. 2d 124 (E.D. N.Y. 2000) (recognizing common law right to bring derivative action even though the New York LLC statute does not expressly permit such actions); Schindler v. Niche Media Holdings, LLC, 772 N.Y.S.2d 781 (N.Y. Sup. Ct. 2003) (holding that the New York LLC statute does not permit derivative actions because it contains no provision authorizing such actions).

An example of a questionable application of corporate norms in the LLC context appears in Geresy v. Dommert, No. 243,468, 2004 Mich. App. LEXIS 1397 (Mich. App. June 3, 2004) (unpublished decision), where the operating agreement provided that each of the members agreed to be personally liable for one-fifth of certain obligations and to sign guarantees. Id. at *5-*6. One of the members signed the operating agreement on behalf of the LLC, and all five members signed the operating agreement under the heading "members." Id. at * 15. The court held that the members could not be held liable because "they had signed the operating agreement only once, rather than twice, which indicated that they had signed only as members and not as individuals." Id. The court relied upon the general rule that "'an individual stockholder or officer is not liable for his corporation's engagements unless he signs individually, and where individual responsibility is demanded the nearly universal practice is that an officer signs twice-once as an officer and again as an individual.'" Id. (citation omitted).

[FN116]. See supra notes 1-3 and accompanying text.

[FN117]. RUPA § 404(c), 6 Pt. I U.L.A. 143 (2001).

[FN118]. ReRULPA § 408(c), 6A U.L.A. 62 (2003).

[FN119]. 543 A.2d 348 (Me. 1988).

[FN120]. The Maine Supreme Court stated that the trial court's delineation of fiduciary obligations accurately described the duties of care and loyalty owed under Maine law by the corporate director to the corporation and its shareholders, as well as the duties of a partner to the partnership and his fellow partners. Those duties were described as follows:

> (1) To act with that degree of diligence, care and skill which ordinarily prudent persons would exercise under similar circumstances in like positions;
> (2) To discharge the duties affecting their relationship in good faith with a view to furthering the interests of one another as to the matters within the scope of the relationship;
> (3) To disclose and not withhold from one another relevant information affecting the status and affairs of the relationship;
> (4) To not use their position, influence or knowledge respecting the affairs and organization that are subject to the relationship to gain any special privilege or advantage over the other person or persons involved in the relationship.

Id. at 352.

[FN121]. The Maine Supreme Court concluded that the trial court incorrectly instructed the jury by misstating the business judgment rule. Id. at 353. In doing so, the court stated:

> Having already stated that defendants owed [their co-partner] four specific fiduciary duties, including the duty of due care, the presiding justice told the jury that the business judgment rule would come into play only if the defendants had not otherwise violated the duty of due care. Thus the justice left open to the jury to find a breach of fiduciary duty by defendants on a showing merely that they had failed "[t]o act with that degree of diligence,

> care and skill which ordinarily prudent persons would exercise under similar circumstances in like positions." That is not the law.
>
> Many courts, including our own, have long recognized that it falls outside the proper judicial domain to inquire into and second-guess the prudence of particular business decisions honestly reached by those entrusted with the authority to determine what course of action best advances the well-being of the enterprise. . . .
>
> Thus the business judgment rule will insulate from a finding of liability the informed business decisions made by [the acting partners] unless [the other partners] [are] able to show that their allegedly harmful conduct was primarily motivated by fraud or bad faith. . . .
>
> The jury instruction in this case did not give [the acting partners] the benefit of the business judgment rule to which by law they are entitled. It erroneously permitted the jury to assess the ordinary prudence of defendants' business decisions, a function denied to judicial tribunals. The jury should have been told that for it to conclude that defendants in fact violated their fiduciary obligations . . ., it must find that the predominating motive for their conduct was fraud or bad faith.

Id. at 353-54 (citations omitted).

[FN122]. Bane v. Ferguson, 890 F.2d 11, 14 (7th Cir. 1989) (finding no precedent in Illinois or elsewhere for imposing tort liability on careless managers for the financial consequences of the collapse of the firm).

[FN123]. Wirum & Cash Architects v. Cash, 837 P.2d 692, 702 (Alaska 1992) (stating that partners are not generally liable to the partnership for "failure to use ordinary skill and care in the supervision and management of business because harm to the partnership is frequently outweighed by the need to give the partner sufficient leeway to exercise discretion on behalf of the partnership") (quoting Alan R. Bromberg & Larry E. Ribstein, Bromberg and Ribstein on Partnership § 6.07(f), at 6.85-.86 (1992)).

[FN124]. ARTRA Group Inc. v. Salomon Bros. Holding Co., 680 N.E.2d 769, 773 (Ill. App. 1997) (stating that the "exercise of poor business judgment does not [alone] constitute a breach of a fiduciary duty" and indicating that some type of intentional or willful disregard of duty would be required to impose liability) (citations omitted).

[FN125]. Borys v. Rudd, 566 N.E.2d 310, 316 (Ill. App. 1990) (stating that "partnership losses occasioned by a partner's poor judgment or mistakes of judgment will be borne by the partnership so long as the decision does not involve fraud, illegality, or conflict of interest").

[FN126]. Stuart Silver Assocs. Inc. v. Baco Dev. Corp., 665 N.Y.S.2d 415, 418 (N.Y. App. Div. 1997) (stating that the business judgment rule shielded the general partners from liability for an unwise investment scheme in the absence of bad faith, a conflict of interest, or personal bias).

[FN127]. Duffy v. Piazza Constr. Inc., 815 P.2d 267, 268-69 (Wash. App. 1991) (stating that there is generally no liability on the part of a partner for negligence in the management of the partnership and that it is only actionable when there is a breach of trust).

[FN128]. Grider v. Boston Co., 773 S.W.2d 338, 342 (Tex. App. 1989) (stating that the judgment used in making business decisions will be respected by the courts in the absence of a clear abuse of discretion).

[FN129]. Cates v. Int'l Tel. & Tel. Corp., 756 F.2d 1161, 1178-79 (5th Cir. 1985) (stating that there were no grounds to interfere with the majority partner's decision not to bring suit on behalf of the partnership where there was no allegation that the majority partner was guilty of any fraud or misconduct or that he was even unwise in refusing to consent to the suit).

[FN130]. In re Boston Celtics Ltd. P'ship S'holders Litig., No. 16,511, 1999 Del. Ch. LEXIS 166, at *12 (Del. Ch. Aug. 6, 1999). See also Seaford Funding Ltd. P'ship v. M&M Assocs. II, L.P., 672 A.2d 66, 70 (Del. Ch. 1995) ("When limited partners make demand and the general partner refuses to pursue the action after informed consideration and in good faith, the business judgment rule comes into play.") (citation omitted).

[FN131]. Dean v. Dick, No. 16,566, 1999 Del. Ch. LEXIS 121, at *15 (Del. Ch. June 10, 1999).

[FN132]. Shlomchik v. Richmond 103 Equities Co., 662 F. Supp. 365, 373- 74 (S.D.N.Y. 1986) (finding no failure on the part of the general partners to fulfill their obligation to make a business judgment in the exercise of good faith and reasonable diligence under the existing circumstances); Seaford Funding Ltd. P'ship, 672 A.2d at 70.

[FN133]. Wyler v. Feuer, 149 Cal. Rptr. 626, 633 (Cal. Ct. App. 1979) (stating that the good faith business judgment and management of a general partner need only satisfy the standard of care demanded of an ordinarily prudent person and will not be scrutinized by the courts with the "cold clarity of hindsight").

[FN134]. Master Garage Inc. v. Bugdanowitz, 690 P.2d 879, 882 (Colo. Ct. App. 1984) (dismissing claim for breach of fiduciary duty because partner's action constituted a business judgment); Lehrberg v. Felopulos, 248 N.E.2d 648, 653 (Mass. 1969) (finding that the general partners' decision was made in the exercise of business judgment as to what was best for the partnership and was a decision that could reasonably be made by a partner with the power to act); Jackson v. Marshall, 537 S.E.2d 232, 236 (N.C. App. 2000) (holding that the duties of a general partner are similar to the duties of a corporate director and that the general partner's duty to the limited partners is to discharge his responsibilities according to the business judgment rule); See also Opus Corp. v. Int'l Bus. Mach. Corp., 141 F.3d 1261, 1267-68 (8th Cir. 1998) (applying business judgment rule standard articulated by the partners in the limited partnership agreement). The business judgment rule has not been applied when the court determined that the partner breached the partnership agreement. See generally Fisher v. Hampton, 118 Cal. Rptr. 811 (Cal. Ct. App. 1975) (holding that the general partner breached the partnership agreement by refusing to comply with an express provision contained therein); Wallner v. Parry Prof'l Bldg., Ltd., 27 Cal. Rptr. 2d 834, 839 (Cal. Ct. App. 1994) (holding that limited partner may bring a derivative suit on the grounds of an alleged breach of the partnership agreement); Roper v. Thomas, 298 S.E.2d 424 (N.C. Ct. App. 1982), rev. denied, 302 S.E.2d 244 (N.C. 1983) (holding that the business judgment rule did not protect the general partner where the general partner breached the partnership agreement); Shinn v. Thrust IV, Inc., 786 P.2d 285 (Wash. Ct. App. 1990) (same).

[FN135]. Henkels & McCoy, Inc. v. Adochio, 138 F.3d 491, 502 (3d Cir. 1998).

[FN136]. Callison & Sullivan, supra note 53, § 12.02, at 12-5 to 12-6 (footnotes omitted).

[FN137]. Froelich v. Erickson, 96 F. Supp. 2d 507, 520 (D. Md. 2000), aff'd sub nom., Froelich v. Senior Campus Living LLC, 5 Fed. Appx. 287 (4th Cir. 2001). The limited liability company was structured with corporate features such as a "board of directors" and classes of "preferred" and "common" interests. The Fourth Circuit Court of Appeals further addressed the application of the business judgment rule in this case in Froelich v. Senior Campus Living, LLC, 355 F.3d 802 (4th Cir. 2004). Stretching the rule beyond recognition was the Maryland case of LGB Group, LLC v. Booty, in which the business judgment rule was held to protect the decision of an LLC's members to amend the operating agreement. LGB Group, LLC v. Booty, Nos. CAL 03-00088, CAE 02-00408 & CAL 03-08305, 2004 WL 1058958, at *11-*12 (Md. Cir. Ct. Jan. 28, 2004).

[FN138]. No. 17,995, 2000 Del. Ch. LEXIS 122 (Del. Ch. Aug. 31, 2000), aff'd, 781 A.2d 696 (Del. 2001).

[FN139]. Id. at *15-*16. See also the cursory opinion in the Delaware case of Stern v. LF Capital Partners, LLC that implies, but does not clearly state, that the business judgment rule would protect decisions made by what may have been the LLC's managers. Stern v. LF Capital Partners, LLC, No. 19,218, 2003 Del. Ch. LEXIS 30, at *3 (Del. Ch. Mar. 12, 2003). In Blackmore Partners, L.P. v. Link Energy LLC, the Delaware Court of Chancery held that Revlon duties apply in the LLC context and that a provision in the LLC operating agreement eliminating liability for breach of the duty of care would not protect the managers from disloyal or intentional misconduct. Blackmore Partners, L.P. v. Link Energy LLC, 864 A.2d 80 (Del. Ch. 2004).

[FN140]. VGS, Inc., 2000 Del. Ch. LEXIS 122, at *15-*16.

[FN141]. 123 F. Supp. 2d 1254, 1260 (D. Kan. 2000) (stating that Kansas courts have a long history of looking to Delaware decisions involving corporation law).

[FN142]. Id. (characterizing the Delaware business judgment rule as presupposing "that the 'directors act on an informed basis and in the honest belief [that] they acted in the best interest of the corporation'") (quoting Krim v. ProNet, Inc., 744 A.2d 523, 527 (Del. Ch. 1999)).

[FN143]. See DeBold v. Case (In re Tri-River Trading LLC), 317 B.R. 65, 74 (Bankr. E.D. Mo. 2004) (noting that the Missouri LLC statute requires that "'[a]n authorized person shall discharge his duty . . . in good faith, with the care a corporate officer would exercise under similar circumstances, in the manner he reasonably believes to be in the best interests of the limited liability company,"' and concluding that an LLC member's withdrawal of financial support, which led the LLC to experience significant financial losses, breached the statutory fiduciary duty) (quoting Mo. Rev. Stat. § 347.088 (2003)); In re Provenza, 316 B.R. 225, 230 (Bankr. E.D. La. 2003) (reciting the statutory fiduciary duties and standard of liability under the Louisiana LLC act, and commenting that courts employ "at minimum, a gross negligence standard and the business judgment rule" under the Louisiana LLC statute, in reaching its conclusion that an LLC member/manager's alleged failure to disclose certain financial difficulties did not amount to a breach of fiduciary duty and that an exculpatory provision in the articles of organization relieved the member of liability even if the action amounted to a breach of fiduciary duty to the LLC or its members). In an unpublished California case, the California Court of Appeal concluded that a managing member's failure to seek additional capital (which was needed in order to close the purchase of property sought by the LLC) constituted gross negligence, noting parenthetically that the business judgment rule defense was unavailable. Denevi v. Green Valley Corp., Nos. H024089, H024292, H024293, H024374 & H025206, 2005 Cal. App. Unpub. LEXIS 578, at *24-*25 (Cal. App. 6 Dist. Jan. 21, 2005). The operating agreement in that case absolved the managing member from liability for any loss or damage unless it resulted from "'fraud, deceit, gross negligence, reckless or intentional misconduct, or a knowing violation of law."' Id. at *9. The standard in the operating agreement was thus similar to the default standard under the California LLC statute, which incorporates by reference the standard of care specified in the California Revised Uniform Partnership Act. See supra note 93. That standard limits the duty of care to refraining from engaging in grossly negligent or reckless conduct, intentional misconduct, or a knowing violation of law. Cal. Corp. Code § 16404 (West Supp. 2004). In Flippo v. CSC Associates III, LLC, the Virginia Supreme Court stated that an LLC "manager, like a corporate director, is required to discharge his duties in accordance with his 'good faith business judgment . . . [in] the best interests of the . . . [LLC]."' Flippo v. CSC Assocs. III, LLC, 547 S.E.2d 216, 221 (Va. 2001). The court acknowledged that the Virginia LLC statute protects managers "from liability in the exercise of that . . . judgment under certain circumstances." Id. The court concluded, however, that the manager was not protected in relying on advice of counsel in connection with the transaction in question because the advice was sought in the member's personal capacity for his own personal interests. Id. at 222. In essence, the transaction in question breached the manager's duty of loyalty. Id. Thus, the court did not need to discuss the standard of care and the standard of liability under the statutory duty of care provisions. Id. at 221-22.

[FN144]. No. E2003-02124-COA-R3-CV, 2004 Tenn. App. LEXIS 507, at *4 (Tenn. Ct. App. Aug. 5, 2004).

[FN145]. Id. at *19-*21.

[FN146]. This statement is made subject to the discussion below regarding contractual modification of the duty of care. The partners or members are, of course, generally free to agree regarding the standard of conduct and standard of liability that will apply in their relationship under these statutes.

[FN147]. See, e.g., Martin, supra note 54, at 1329-30 (explaining that adoption of the gross negligence standard of care in RUPA applies to both the standard of conduct and the standard of review, eliminating any necessity for the application of a separate business judgment rule).

[FN148]. Nos. 99-20287 & 00-6064, 2001 Bankr. LEXIS 1033 (Bankr. D. Idaho Mar. 19, 2001).

[FN149]. Id. at *34 (footnotes omitted).

[FN150]. See generally Jack B. Jacobs, Entity Rationalization: A Judge's Perspective, 58 Bus. Law. 1043 (2003) (presented at Entity Rationalization Symposium, University of Maryland College of Law, Nov. 1, 2002) (describing the Delaware Court of Chancery's growing challenges in dealing with governance issues for alternative business entities).

[FN151]. See id. at 1044-45, which states:

> [T]hose entity forms [LP, LLP, LLC or Business Trust] are, by statute, to be governed by contract rules, customized in the organizational instrument of the entity in question and limited only by the express prohibitions of the entity enabling statute. Indeed, the alternative entity statutes contemplate that fiduciary duty principles may be displaced, to a greater or lesser degree, by contract.

[FN152]. Id. at 1045.

[FN153]. Id.

[FN154]. See, e.g., RUPA § 103(b)(4), 6 Pt. I U.L.A. 73 (2001) (permitting a reasonable reduction in the standards of care set forth in RUPA §§ 404(c) and 603(b)(3)).

[FN155]. This fact situation was faced in UPA partnerships, and by means of linkage in RULPA limited partnerships, which sought to incorporate a contractually defined (and limited) standard of care.

[FN156]. These scenarios in graphic form are:

Scenario	Statutory Standard of Care	Modification of Standard Expressly Allowed	Agreement Provides Modified Standard of Care
1	/	/	/
2	/		/

3 /

4 / /

5 /

6 [/]

[FN157]. See, e.g., RUPA §§ 103(b)(4), 404(c)

[FN158]. This is not to say, however, that it is either simple or appropriate to modify statutory or common law fiduciary duties. As observed in Murdock:

> In order to draft an adequate shareholders' agreement in the corporate context, or operating agreement in the LLC context, which would provide the types of protection that fiduciary duties provide on a default basis, one could expect an attorney's fee in the range of $10,000 or more, at least in the Chicagoland area. One of the reasons for this high cost is the difficulty in drafting such an agreement. Because we are dealing with a relationship, we need to anticipate problems that may not arise until years down the line. If one were to examine the litigated cases, one would find that many of the cases involve problems that have arisen a decade or more after the organization of the business. This is because, over time, situations change. Personality differences may arise, someone may go through an ego shattering divorce, a spoiled child may enter the business, or the financial misfortunes of one member may lead him or her to make demands that are unacceptable to other members.

Murdock, supra note 83, at 528-29 & n.161 (citing Battaglia v. Battaglia, 596 N.E.2d 712, 719 (Ill. App. Ct. 1992), appeal denied, 602 N.E.2d 446 (Ill. 1992) (involving brothers that had worked together for forty years); In re Kemp & Beatley, Inc., 473 N.E.2d 1173, 1176 (N.Y. 1984) (involving plaintiffs that had worked for the business for thirty-five and forty-two years, respectively); Pedro v. Pedro, 489 N.W.2d 798, 803 (Minn. Ct. App. 1992) (involving a plaintiff that had been employed for forty-five years and the defendant brothers employed for thirty-four and fifty years, respectively)).

[FN159]. We assume for this discussion that the contractual modification is within the limits set by the statute. See, e.g., RUPA § 103(b)(4); ReRULPA § 110(b)(6).

[FN160]. Note that some LLC acts do not provide for a standard of care, but do recognize the primacy of the operating agreement as controlling the relationship among the members. See, e.g., Ky. Rev. Stat. Ann. § 275.003 (Michie 2002) ("It shall be the policy of the General Assembly through this chapter to give maximum effect to the principles of freedom of contract and the enforceability of operating agreements.").

[FN161]. Egregious abuses may be addressed by resort to principles of good faith and fair dealing and, in the face of a modification of the standard of care, a judicial determination that the modification lacked the specificity necessary to sanction the subject conduct.

[FN162]. See supra notes 146-47 and accompanying text.

[FN163]. See McLendon v. McLendon, 862 S.W.2d 662, 676-77 (Tex. App.1993) (holding the parties' agreement to modify the general partners' duties enforceable); Grider v. Boston Co., 773 S.W.2d 338, 342-43 (Tex. App. 1989) (same); see also R.S.M., Inc. v. Alliance Capital Mgmt. Holdings, L.P., 790 A.2d 478, 499 & n.33 (Del. Ch. 2001) (discussing the extent of contractual modification of fiduciary duties in the partnership agreement); Sonet v. Timber Co., L.P., 722 A.2d 319, 324 & n.12 (Del. Ch. 1998) (same).

[FN164]. See supra note 160.

[FN165]. We should always make this assumption in all cases in which the parties define an applicable standard of care.

[FN166]. See, e.g., Froelich v. Erickson, 96 F. Supp. 2d 507, 520 (D. Md. 2000), aff'd sub nom., Froelich v. Senior Campus Living LLC, 5 Fed. Appx. 287 (4th Cir. 2001).

[FN167]. Whether the participants had a common understanding of that standard of care is open to dispute.

[FN168]. As Professor Ribstein described:

> Fiduciary duties are a specific type of contractual term, namely a duty of unselfishness, which applies in the absence of contrary agreement in the particular case where an "owner" who controls and derives the residual benefit from property delegates open-ended management power over property to a "manager." . . . In such a relationship the fiduciary has the incentive to use control to enrich herself rather than the owner, and the owner's most effective protection is to subject the manager to a limited ex post duty focusing on whether the manager has engaged in self-dealing.
>
> Although others have described fiduciary duties along similar lines, they usually do not clarify why the property manager needs to be constrained by the strong fiduciary duty. In other words, while it is apparent that the property owner would not delegate control over his property without demanding some protection, it is not clear why the benefits of the particular protection provided for in fiduciary law outweigh the costs. The short answer is that the fiduciary's discretion cannot readily be constrained by devices other than fiduciary duties without undermining the owner's objectives in delegating control.

Larry E. Ribstein, The Structure of the Fiduciary Relationship, at http:// home.law.uiuc.edu/~ribstein/structureofthefiduciaryrelationship9.doc, at 8-9 (Nov. 23, 2003 Draft) (footnotes omitted)

[FN169]. Of course, where the business judgment rule has been expressly incorporated in a statute, this statement is inapposite, and the business judgment rule should be applied unless the parties have expressly elected out of it in the organic documents. In addition, in those instances where the statutory formulation of the duty of care in an LLC or partnership statute is based on the former MBCA model (i.e., an MBCA-based standard of care without explicit provisions embodying the business judgment rule), courts will likely view the business judgment rule as an implicit feature of the formulation, and application of the business judgment rule arguably best reflects the intent underlying adoption of such a corporate model. See supra notes 95-96 and accompanying text; see Tex. Rev. Civ. Stat. Ann. art. 6132b-4.04(c) (quoted in supra note 60). In the case of those statutes that are silent with respect to the duty of care, the courts might follow any of several courses, all of which can be found in prior case law: articulation of a standard of care and a standard of review/ liability that are contiguous; articulation of a standard of care subject to a relaxed standard of review/liability (as reflected in the business judgment rule); or articulation of a standard of review/liability without specifying the standard of care itself. Inasmuch as each of these approaches may well (as they have in the past) ultimately reflect a reluctance to impose liability short of gross negligence or similarly culpable conduct, the difference in approaches may be more theoretical than practical.

[FN170]. See supra note 57.

[FN171]. See Bayless Manning, Reflections and Practical Tips on Life in the Boardroom After Van Gorkom, 41 Bus. Law. 1, 1 (1985) ("The day-to-day evolution of the business judgment rule in the Delaware court continues to be the best law game in town.").

[FN172]. See Bayless Manning, The Business Judgment Rule and the Director's Duty of Attention: Time for Reality, 39 Bus. Law. 1477 (1984).

> A while back, the solonic custodians of the Model Business Corporation Act (MBCA), the ABA's Committee on Corporate Laws, struggled through three years of debate to arrive at a formulation of the director's duty of care. . . . Over the past three years, this same ABA committee has been engaged in an overall revamping of the entire Model Act. In the course of that exercise, the committee tried again to grapple with the elements of the business judgment rule in a new section 8.30. After no less than ten drafts and literally hundreds of man-hours of struggle, the effort was again abandoned, and it was decided, faute de mieux, to retain old section 35 and not seek to go further. Substantially all of the battle raged over the subject traditionally called the directors' duty of care.

Id. at 1478-79 (footnotes omitted).

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***355 SERIES LLCs**: THE LOAVES AND FISHES OF SUBCHAPTER K

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***359 Table of Contents**

*361 I. Background

Limited liability companies have long been recognized as a preferred vehicle to combine the best of the tax world and the business world. [FN1] They afford limited liability protection to their members, but flow-through treatment for federal income tax purposes, all without the more cumbersome administrative requirements of limited partnerships. [FN2] It was only a question of time, therefore, before the business and legal communities would seek still greater flexibility to businesses choosing this new and popular form of legal enterprise.

Now, along come **series LLCs**, adding to the advantages of using an LLC the opportunity to form a single entity under state law but allow the entity's members to segregate the liabilities, control, and profit sharing of one business conducted by the LLC from another business conducted by the same LLC.

In a nutshell, a **series LLC** [FN3] is a special form of LLC that provides for the establishment of designated series within the LLC applicable to specified assets or operations, each with a separate business purpose or investment objective. [FN4] In a **series LLC**, the debts, liabilities, and obligations relating to one series are enforceable only against the assets of that series and not against the assets of the LLC generally or the assets of any other series. [FN5]

To date, only seven states -- Delaware, Iowa, Oklahoma, Illinois, Nevada, Utah, and Tennessee -- have adopted **series LLC** statutes, but several others have similar legislation under consideration. Even in those states that have adopted legislation, many questions remain unanswered concerning the new type of entity, such as:

- Will each series be treated as a separate person for federal bankruptcy purposes? [FN6]
- ***362** Will the courts be more liberal in allowing a creditor to pierce the corporate veil of one series with respect to the liabilities of another series in the same LLC?
- Will an LLC with several series that are conducting businesses in different states be entitled to the protections of its state of formation when pressed by creditors in another state? [FN7]

Also unexplored to date is the degree to which the members of an LLC formed under a nonseries state statute can achieve series-type protections through their certificate of formation or articles of organization or through their LLC agreement, if creditors are put on proper notice.

While these issues may be better left to the corporate bar, the appearance of **series LLCs** raises important questions also as to the taxation of these new entities for federal income tax purposes. [FN8] Those questions include:

- What is the proper classification of a **series LLC** for federal income tax purposes?
- What are the ramifications for an LLC and its members from forming a **series LLC** and from operating in **series LLC** form?
- Can **series LLCs** function in the world of subchapter K, or are new rules needed?

The following discussion is divided into five parts. Part II provides an overview of the provisions of several state laws that allow the creation of **series LLCs**. Part III highlights what the state statutes do not do. Part IV explores the appropriate tax classification of **series LLCs** under current federal law. Part V discusses some ancillary issues that may put taxpayers at risk when using the new entity -- absent guidance from the IRS as to how it intends to treat **series LLCs**. Finally, Part VI considers the world without **series LLC** statutes and whether ***363** they are really necessary to achieve separate entity status for different interests in an LLC.

II. The Framework: A Look at the State Laws

A. Delaware

Delaware was the first state to adopt **series LLC** legislation. [FN9] Section 18-215 of the Delaware Limited Liability Company Act [FN10] allows an LLC agreement to establish one or more designated series of members, managers, or LLC interests, each having separate rights, powers, or duties with respect to specified property or obligations of the LLC, or with respect to profits and losses associated with specified property or obligations of the LLC. [FN11] Each series also may have a separate business purpose or investment objective. [FN12]

Under the Delaware statute, the debts, liabilities, obligations, and expenses incurred, contracted for, or otherwise existing with respect to a designated series will be enforceable only against the assets of that series, and not against the assets of the LLC generally or any other series, as long as three conditions are met: (1) separate and distinct records are maintained for the series, the assets associated with the series are held in those separate and distinct records (directly or indirectly, including through a nominee or otherwise), and the assets of the series are accounted for in those records separately from other assets of the LLC or any other series (what we might call the "separateness" test); (2) the LLC agreement provides for the foregoing; and (3) notice of the limitation on liabilities of a series is set forth in the certificate of formation of the LLC. [FN13] There is no requirement that any specific series of the LLC be referenced in the notice. [FN14]

Section 18-215 of the Delaware Act provides also that an LLC agreement may provide for separate governance and procedural rules for classes or groups of members or managers associated with each series of the LLC. Thus, for example, the agreement ***364** may designate the relative rights, powers, and duties of each series; [FN15] make provisions for the future creation of additional classes or groups associated with the series; [FN16] and provide for taking any action, including amending the LLC agreement, without the vote or approval of any member or manager or class or group of members or managers. [FN17] The agreement also may provide that any member or class or group of members associated with a particular series have no voting rights, [FN18] and may grant to all or some identified members or managers, or a specified class or group of the members or managers associated with a series, the right to vote separately or with all or any class or group of the members or managers associated with the series on any matter. [FN19] Voting by members or managers associated with a series may be on a per capita, number, financial interest, class, group, or any other basis. [FN20]

Other elements of the Delaware statute that contribute to the separate nature of each series include (1) a provision that an event that causes a manager to cease to be a manager with respect to one series will not, in itself, cause the manager to cease to be a manager of the LLC with respect to any other series, [FN21] (2) a provision that allows a series to be terminated and its affairs wound up without causing the dissolution of the LLC, [FN22] and (3) a provision that generally limits distributions with respect to any series to the fair market value of the assets of the series in excess of liabilities associated with the series. [FN23]

B. Iowa

Iowa followed shortly after Delaware in adopting provisions permitting **series LLCs**, and, perhaps for that reason, its statute basically tracks the Delaware statute. [FN24] The statutes do differ in minor respects, however. For example, a series of an Iowa LLC may be terminated by its members only if all members of the series consent, while a series of a Delaware LLC may be terminated by members associated with the series who own more than two-thirds of the then-current percentage or other interest in the profits of the series.

***365 C. Illinois**

The Illinois series statute [FN25] became effective August 16, 2005. It is similar to the Delaware statute, but includes some additional (and important) details not found in the Delaware statute, which was enacted almost a decade before. For example, the Illinois statute states that each series with limited liability may, in its own name, contract, hold title to assets, grant security interests, sue and be sued, and otherwise conduct business and exercise the powers of an LLC under the Illinois LLC Act. [FN26] Each series creates its own existence by filing a separate certificate of designation. [FN27] Perhaps most importantly, the statute provides that a series will be treated as a separate entity to the extent set forth in the articles of organization of the LLC. [FN28]

In an additional distinction from Delaware, the Illinois statute addresses to some extent the tax status of a series, something no other state has chosen to do, at least by statute. [FN29] It provides that an LLC and any of its series may elect to consolidate their operations as a single taxpayer "to the extent permitted under applicable law." [FN30] The series also may elect to work cooperatively, elect to contract jointly, or elect to be treated as a single business for purposes of qualification to do business in Illinois or any other state. [FN31] Any such election will not affect the limitation of liability set forth in the statute, except to the extent that a series has specifically accepted joint liability by contract. [FN32]

While the Delaware statute refers only to "designated series" of members, interests, and so on, the Illinois statute requires that the name of any series with limited liability contain the entire name of the LLC and, as a further attribute of separateness, that it be distinguishable from the names of the other series set forth in the articles of organization of the LLC. [FN33] Also, if it is different from the LLC generally, the certificate of designation for each series must list the names of the members if the series is member managed, or the names of the managers if the series ***366** is manager managed. [FN34] Thus, owners of an Illinois **series LLC** seeking confidentiality will want to be certain their LLC is manager managed, to avoid disclosing the names of the individual members.

D. Nevada

Adopted in the same year as the Illinois statute, the series provisions of Nevada law are scattered throughout the LLC statute rather than concentrated in one or two sections. [FN35] Among other things, the Nevada statute allows the articles of organization or operating agreement of an LLC to create one or more series of members, or to vest in one or more members or managers of the LLC or in other persons the authority to create one or more series of members, including -- without limitation -- rights, powers, and duties senior to existing series of members. [FN36] A Nevada **series LLC** also may designate different voting rights for members associated with one series from those of another series, or provide no voting rights for a series at all, [FN37] and may designate separate powers, rights, or duties for a series with respect to specified property or obligations of the LLC or profits and losses associated with specified property or obligations. [FN38] Each series may have a separate business purpose or investment objective. [FN39]

The debts, liabilities, obligations, and expenses incurred, contracted for, or otherwise existing with respect to a particular series of a Nevada LLC are enforceable against the assets of that series only, and not against the assets of the LLC generally or any other series if, as in Delaware, the series satisfies the separateness test -- that is, separate and distinct records are maintained for the series and the assets associated with the series are held and accounted for separately from the other assets of the LLC and any other series, and the articles include a statement to that effect, together with a statement setting forth the relative rights, powers, and duties of the series, or indicating that the relative rights, powers, and duties of the ***367** series will be set forth in the operating agreement or established as provided in the operating agreement. [FN40]

Supporting the separate identify of each series, the Nevada statute prohibits a distribution of profits and contributions of a series if, after giving the distribution effect, the LLC would not be able to pay the debts of the series from assets of the series as those debts become due in the usual course of business [FN41] or if, except as otherwise specifically permitted by the articles of organization, the total assets of the series would be less than the sum of the total liabilities of the series. [FN42]

Nevada has managed to make **series LLCs** a moneymaker as well. The initial filing fee for an LLC is $75, but Nevada requires a separate filing (and fee) for each series. Additional fees apply for annual filings, with the annual filing fee of $125 applied to each series.

E. Oklahoma

Oklahoma is another more recent addition to the family of states approving **series LLCs**. Like the Iowa statute, the Oklahoma statute [FN43] is based largely on the Delaware statute, frequently parroting its provisions. The Oklahoma statute, like Delaware's, authorizes persons winding up the affairs of a series to take all actions with respect to the series permitted under the general LLC dissolution and winding-up provisions of Oklahoma law. [FN44]

F. Utah

Enacted in 2006, Utah's **series LLC** statute [FN45] provides generally that the operating agreement may establish or provide for the establishment of one or more designated series of members, managers, or interests in the LLC having separate rights, powers, or duties with respect to some property or obligations of the LLC or profits and losses associated with some property or obligations. [FN46]

***368** To limit the liabilities of a series solely to the assets of that series, a Utah **series LLC** must comply with requirements substantially similar to those in effect in Delaware. [FN47] Like the Illinois law, the new Utah law makes clear that a series may contract on its own behalf and in its own name, [FN48] but it does not go as far as to provide, as does Illinois, that the series will be treated as a separate entity. [FN49] Finally, the statute requires a foreign LLC with series registering to do business in Utah to indicate on its application for authority that it has series and to identify which of the protections found in section 48-2c-606 apply to its series. [FN50] If different protections found in the Utah statute apply to different series, the application for authority must identify the protections that apply to each existing series and the protections that will apply to later-created series. [FN51]

G. Tennessee

With its addition of series provisions to its LLC statute in 2006, Tennessee became the most recent state to recognize **series LLCs**. The Tennessee statute [FN52] provides generally that LLC documents may establish, or provide for the establishment of, one or more designated series of members, holders, managers, directors, membership interests, or financial rights having separate rights, powers, or duties, with respect to specified property or obligations of the LLC or with respect to profits and losses associated with specified property or obligations. Any such series may have a separate business purpose or investment objective.

To establish its separateness, an individual series of a Tennessee LLC must maintain separate and distinct records and, subject to compliance with the statute, must limit the debts, liabilities, obligations, and expenses incurred with respect to a particular series to the assets of that series only. [FN53]

The Tennessee statute contemplates the registration in Tennessee of **series LLCs** from other jurisdictions. [FN54] Although the statute calls for a foreign **series LLC** to reflect in its ***369** Tennessee registration the fact of its separate series and their separate rights, powers, and duties with respect to specified property or obligations of the foreign LLC or profits and losses associated with the specified property or obligations, the only consequence of failing to do so appears to be a loss of statutory liability protection for one series against the liabilities of another series.

H. Republic of the Marshall Islands

Those who are interested in the benefits of a **series LLC** offshore may want to explore the laws of the Republic of the Marshall Islands (RMI), which authorize **series LLCs**. [FN55] The RMI statute is modeled after Delaware's statute. At least one author has suggested that an RMI LLC might be used to provide an economical framework allowing clients access to international investment programs not available to U.S. persons. [FN56]

III. What the State Statutes Do Not Do

While the statutes in Delaware, Illinois, Iowa, Oklahoma, Nevada, Utah, and Tennessee all clearly segregate the liabilities of one series from another series of the same LLC (unless segregation is voluntarily waived), [FN57] only the Illinois statute states affirmatively that a series is a separate entity distinct from other series of the LLC. [FN58] The Illinois statute goes further than any other to imbue each series with independent powers and authority, providing that, in addition to their specifically stated powers and authorities, each series may "otherwise conduct business and exercise the powers of a limited liability company under the [LLC] Act." [FN59] Still, some important attributes of separate entity status are missing from all the **series LLC** statutes. For example, as noted in one treatise on LLCs: [FN60]

***370** • while in each of the states an LLC may sue or be sued in its own name, only in Illinois may a separate series sue or be sued in its own name; [FN61]

• while most of the states allow an LLC to merge or consolidate with another taxable entity, [FN62] thereby (apparently) sweeping along with it each series, none allows separately for a series to merge or consolidate with another legal entity;

• while other business entities generally may convert to an LLC in each state, [FN63] none allows a series to convert to another type of business entity; and

• while each of the states allows an LLC formed under the laws of another state to domesticate in its jurisdiction, [FN64] none allows a series of a foreign LLC to do so absent domestication by the entire LLC.

Thus, while most of the statutes provide a great deal of separateness among the series of an LLC formed -- their jurisdictions -- perhaps with the exception of Illinois, they do not take the more definitive step of confirming, even as a matter of state law, that each series is to be treated as a separate legal entity for other purposes.

IV. Federal Tax Classification of Series LLCs

Those who take little comfort from state law concerning the tax classification of **series LLCs** [FN65] will find an equally uncertain climate under federal law. [FN66] To date, neither Congress, the courts, nor the IRS has provided any guidance directly on point as to how **series LLCs** should be treated for federal income tax purposes. There is helpful precedent in a number of other areas, however, that provides a preview of how the IRS may treat **series LLCs**. Those are discussed below.

***371** What are the choices? Depending on how one looks at **series LLCs**, they might be taxed in one of three ways:

• The LLC, despite its separate series, could be taxable as a single entity for federal income tax purposes, much like a limited partnership with different classes of members. See Figure 1. Although at first blush one might resist this classification in light of the care with which the various state statutes spell out the separate rights and obligations of each series, under none of the statutes is separateness universal.

Figure 1. Series as Part of a Single Entity

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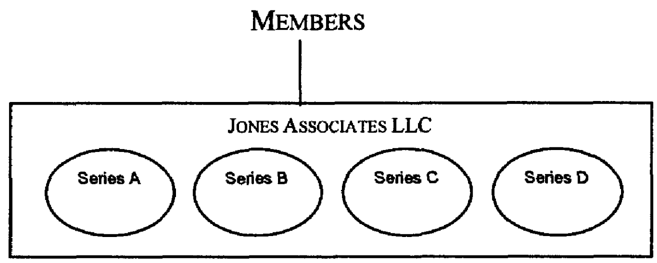

• Alternatively, each series could be treated as a disregarded entity, the sole owner of which is the LLC of which it is a part. See Figure 2. If this approach were followed, all of the creditor and similar protections provided by state statute would remain intact, but the federal classification of the activities of the LLC conducted through its several series would not be affected; that is, the respective series (at least absent a check-the-box election) would be classified as disregarded entities and the aggregate businesses would be taxable as a single partnership under subchapter K.

***372 Figure 2. Series as Disregarded Entities With a Single Owner**

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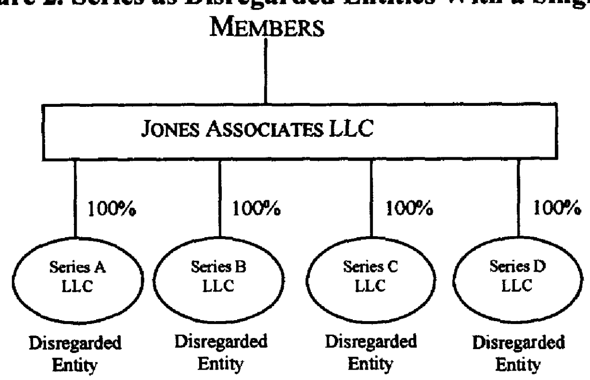

• Finally, each series could be taxable as a separate entity owned directly by the series' members. See Figure 3.

Figure 3. Series as Separate Taxable Entities Owned by Individual Members

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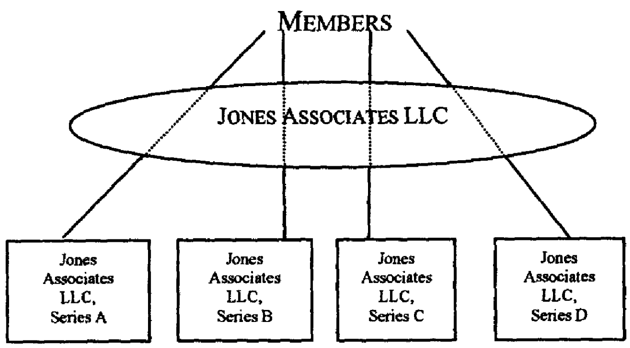

A. The Federal Entity Classification Regulations

The logical starting point for determining the proper federal tax classification for **series LLCs** is the entity classification rules in reg. section 301.7701-1 et seq. In effect since 1997, the rules replace the factual classification rules in effect for many ***373** decades that based an enterprise's tax classification generally on whether it possessed more corporate characteristics than noncorporate characteristics.

For an enterprise to be eligible to elect classification under the regulations, it must pass three tests:

- it must constitute an entity within the meaning of reg. section 301.7701-1(a);
- it must constitute a business entity within the meaning of reg. section 301.7701-2(a); and
- it must not be a per se corporation.

Unfortunately, the regulations provide little guidance as to what attributes or characteristics of an enterprise are relevant for determining whether it meets the first of the tests, that of entity status. Reg. section 301.7701-1(a)(2) states only in general terms that a joint venture or other contractual arrangement may create a separate entity for federal tax purposes if the participants carry on a trade, business, financial operation, or venture and divide the profits therefrom.

The courts and the IRS have been more helpful. They generally have treated an organization -- whether established under state law or simply by contract among its owners -- as a separate entity if the organization changes the legal and economic relationship between the owners and their assets. [FN67] Under that standard, whether a single series of an LLC will constitute a separate entity for tax purposes will depend on whether the governing statute or the contractual arrangement among the participants, for example, the LLC's articles of organization or operating agreement, alters the members' rights with respect to the assets held by the series in which they participate. Although a review of any of the current LLC statutes suggests this is the case for multiple participants in a series, the conclusion is not so apparent if the LLC itself is deemed to be the owner of each series. [FN68] In that case, there would be only one owner, so the ***374** legal and economic relationship between that single owner and the series assets would seem not to be changed by formation of the series. If each series, however, is considered to be owned by the members of the series designated in the LLC's certificate of formation or operating agreement, [FN69] the requisite change in the members' legal and economic relationship clearly would occur.

As noted, a series also must constitute a business entity under reg. section 301.7701-2(a) to be eligible to elect separate status. A business entity for this purpose is any entity recognized for federal tax purposes (including an entity with a single owner that may be disregarded as an entity separate from its owner under reg. section 301.7701-3) that is not properly classified as a trust [FN70] or otherwise subject to special treatment under the

IRC. [FN71]

The distinction between a trust and other entities has been the subject of two U.S. Supreme Court cases that continue to be recognized today as the seminal decisions on the subject. Each focuses on the business purpose of the entity.

In *Morrissey v. Commissioner*, [FN72] the Court was called on to distinguish a trust from an association. In concluding that the entity in question was taxable as an association, the Court noted that the purpose of a trust generally is to hold and conserve a particular property, while the purpose of an association is to provide a vehicle for conducting business and sharing gains from that business.

A somewhat similar analysis led the Court in *Commissioner v. Culbertson* [FN73] to conclude that an entity was taxable as a partnership for federal tax purposes. According to the court, a partnership must be respected if "the parties in good faith and acting with a business purpose intended to join together in the present conduct of the enterprise." [FN74]

***375** In light of *Morrissey* and *Culbertson*, an LLC series should have less trouble meeting the second requirement of the regulations. When a series carries on a separate business, the series should constitute a separate business entity, both under *Morrissey* and *Culbertson* and under reg. section 301.7701-2, as long as the members owning the series carry on a trade, business, financial operation, or venture and divide the profits therefrom. To use the words of Justice Frankfurter in his concurring opinion in *Culbertson*, when parties "are in the same business boat, although they may have varying rewards and varied responsibilities, they do not cease to be in it when the tax collector appears." [FN75] Pending the issuance of any clear administrative confirmation, the most appropriate test of business entity status under the regulations therefore may be to analyze each series under *Morrissey* and *Culbertson*. If it meets both factors established by those cases, it should constitute a separate business entity for federal income tax purposes. [FN76]

Other factors not mentioned in the regulations may play a role as well in the tax classification of a series, although they more often are viewed simply as evidence of the parties' intent to create a separate entity. These include:

- maintaining adequate capitalization for the series separate from other series;
- filing a fictitious business name statement for the series in the proper local offices where it owns property or carries on business;
- maintaining a separate bank account for the series;
- signing all documents in a manner that distinguishes the series from other series; and
- acting in an arm's-length manner when dealing with other series.

***376 B. Other Authority**

The case for recognizing each series of an LLC as a separate entity for federal tax purposes may receive its strongest boost from relatively long-standing precedents established by the IRS and the courts in other areas. One of these is Delaware statutory trusts. [FN77]

Beginning as early as 1949, the Tax Court held that each series of a Delaware statutory trust may be regarded as a separate taxpayer. [FN78] In *National Securities*, each of the petitioners was an open-end investment trust taxable federally as a regulated investment company whose shareholders were entitled at any time, at their option, to surrender their shares for redemption and to receive their proportionate share of the underlying assets of the trust and its net earnings at the date of surrender. During the tax period before the Court, each of the petitioners, incident to the redemption of its shares, made distributions of net earnings to its shareholders and included the sums as dividends paid in the computation of its basic surtax credit.

The Court held that the accumulated net earnings distributed by the taxpayers during the tax year on the redemption of shares were not preferential dividends within the meaning of section 27(h) of the 1939 code, and that the taxpayers were entitled to include the sums as dividends paid in determining their basic surtax credit under sections 362(b) and 27(b)(1) of that code. To arrive at that conclusion, the Court determined as well that each series of the RIC effectively constituted a separate entity for federal income tax purposes.

The *National Securities* decision was followed shortly by Rev. Rul. 55-416, [FN79] in which the IRS reached a similar conclusion, albeit on slightly different facts. In the ruling, the taxpayer requested advice as to whether amounts paid to shareholders of a RIC representing their proportionate part of net income received or receivable up to the surrender of their shares for redemption should be included in determining ***377** whether the RIC had distributed to its shareholders as taxable dividends at least 90 percent of its net income for the tax year for the purpose of determining whether the company could obtain the benefits provided in section 362(b) of the 1939 code. The trust agreement in question provided that regular and extra cash dividends received and earned interest received in respect of trust property would become payable to the shareholders of record on particular dates. It also provided that profits realized on the sale of underlying assets could be distributed from time to time. Although the facts in Rev. Rul. 55-416 were somewhat different from those in *National Securities*, the IRS concluded that "the principles laid down in the [*National Securities*] case are equally applicable." *National Securities* and Rev. Rul. 55-416 have formed the basis for a number of private letter rulings issued since their promulgation. [FN80] Those private letter rulings focus on two principal features. In each case, the redeeming holder is limited to the assets of the series in which he participates and may share in the income solely of that series, and payment of expenses, charges, liabilities, and other obligations of each series is limited to the assets of that series.

A second area in which the IRS has applied similar principles to find separate entity status for different economic interests can be seen in GCM 39211 (Apr. 13, 1984). There, the IRS was asked to consider whether three investment funds formed as a single Massachusetts business trust consisted of one or three separate unincorporated associations taxable as corporations under section 7701(a)(3).

The declaration of trust in GCM 39211 authorized the establishment of the funds as separate investment portfolios, each of which would be represented by a separate series of shares of beneficial interest. The trust was registered with the SEC under the Investment Company Act of 1940 as a no-load, diversified, open-end investment company.

The interest of any shareholder of a fund in the trust was limited to the net assets of that fund and did not extend to the ***378** assets of the trust generally, and the holder of each share of beneficial interest in a particular fund was entitled to a pro rata share of dividends and net realized capital gain distributions of that fund only. Also, the rights of the holders of beneficial interest in a particular fund were limited in redemption and liquidation or termination to the assets of that fund.

The declaration of trust provided that the liability of each fund would be restricted to the assets of that fund. It also included other special rules segregating the interests, providing for the payment of expenses attributable to a fund solely out of the assets of that fund and for voting all shares by individual series in the election of trustees, the termination of the trust, and the amendment of the trust. An exception to this special voting rule applied when required by the 1940 act, when shares would be voted in the aggregate and not by individual series.

In concluding that each fund was a separate entity for federal tax purposes, the IRS cited *National Securities*, noting that while the issue was not directly before the court, the Tax Court and the IRS had "tacitly endorsed the position that a single trust consisting of separate series can be classified as multiple taxpayers." It is also significant that the IRS reached that conclusion even though some activities of the respective series of the business trust were joint rather than separate -- although it noted that the circumstances of joint activities were "extremely limited." Finally, what perhaps may be the closest authority supporting separate entity treatment of classes, series, or related interests in a subchapter K context is a ruling that appears to have escaped the attention of most commentators. In Rev. Rul. 55-39, [FN81] the taxpayer was a general partner of a firm consisting of both limited partners and general partners. The limited partners were entitled to a fixed return on their capital contributions, plus an additional contingent return dependent on net earnings. Except as modified by a special provision affecting the taxpayer, the general partners were entitled to interest at the rate of 6 percent on their capital accounts. ***379** Thereafter, the general partners shared all gains and losses in varying percentages.

Under a special provision in the partnership agreement, the taxpayer was allowed to direct that the amounts in his capital account be invested, in whole or in part, in securities of his selection, with a purchase price being charged to his capital account alone, thereby reducing the balance in his capital account on which the interest referenced above would be computed. The taxpayer's capital account was credited with any dividends, interest, or other distributions received by the firm with respect to the securities in his account, and the increase or decrease in the value of those securities was solely for his account.

Although the taxpayer could direct the sale of any securities in his capital account and the proceeds would be credited to that account, the partnership agreement provided that the securities would "become and remain the property of the partnership and . . . be deemed part of the capital" contributed by the taxpayer. Those and other provisions of the partnership agreement made clear that any securities purchased for the taxpayer's account would be treated as partnership property regarding the claims of creditors.

How did the IRS view this unusual arrangement? It concluded that the securities became the property of the taxpayer when they were acquired for him by the partnership. When the partnership acquired the securities, it in effect distributed cash to the taxpayer in the amount of the cost of the securities purchased. A later distribution of the securities to the taxpayer was not a distribution of partnership property and had no federal income tax consequences. Accordingly, for the purpose of determining basis and computing holding period, the taxpayer was deemed to acquire the securities when they were purchased for his account and at a cost equal to the purchase price.

***380** Further, because the partnership agreement permitted withdrawal of contributed capital without diminution of the taxpayer's participation rights in gains or losses, the IRS concluded that withdrawals of contributed capital under the agreement were not in payment for or liquidation of part of the taxpayer's interest in the partnership. An investment of his contributed capital in securities of his own choice, and for his own account, was in effect the withdrawal of that capital from the firm and an investment by the taxpayer in the securities purchased, resulting in a reduction in the basis of his partnership interest.

Thus, it appears that the partners in Rev. Rul. 55-39 were able to segregate the assets of the partnership allocated to the taxpayer without the aid of any statute simply by the terms of their partnership agreement. In the words of the IRS:

> Where, as here, the agreement provides that certain property is acquired and held for the account of a particular partner, and all of the incidents of ownership, including the right to be credited with all income and profits therefrom and all rights of control, are in him, such property cannot qualify as jointly owned property.

Rev. Rul. 55-39 has not been cited by the IRS in any later ruling.

V. Ancillary Issues

The tax classification of a **series LLC** is not an academic exercise. It may have significant consequences throughout the code, both to the LLC and the owners of its series. The problem is not that these consequences are particularly adverse depending on classification, but rather the inability of taxpayers using **series LLCs** to plan effectively without greater certainty as to what rules will apply. There are numerous examples.

*381 A. Tax Elections

In many places throughout the code, the taxpayer is allowed to make an election. In the case of a **series LLC**, who can or must file the election? Is it the individual series, each of which can file a different election, or the LLC itself? For example:

• A business entity other than a per se corporation with more than one member may elect to be taxable either as a partnership or as a corporation. [FN82] For a **series LLC**, can each series make a separate election if it desires to be classified other than by default for federal income tax purposes?

• Can each series elect a different tax year, [FN83] or is the tax year elected by the LLC itself binding on each series?

• Like the selection of a tax year, and depending on the particular circumstances, can one series of an LLC be on a different method of accounting [FN84] than another, or will the activities of all series be aggregated for purposes of making eligibility determinations for cash versus accrual method? Will the activities of one series taint those of another for purposes of making this determination, for example, if one series has inventory?

• Sections 771 through 777 provide special rules for large partnerships that elect to be treated as such. To be eligible to file the election, the number of persons who were members of the partnership in the preceding tax year must equal or exceed 100, [FN85] and the partnership must elect the application of large partnership rules. [FN86] For purposes of determining whether a **series LLC** has at least 100 members, should one count the members of all of the series, or must a determination of eligibility be based on the number of members in each series? Who files the election?

***382** • Who is eligible to make an election under section 754? [FN87] If the election is made, what assets are subject to the election? [FN88]

The foregoing is only a brief list. Also, an LLC (or series) taxable as a partnership may make an election regarding:

• the use of straight-line or another method of computing depreciation; [FN89]

• amortization of pollution control facilities; [FN90]

• deduction of research or experimental expenditures; [FN91]

• expensing some depreciable business assets; [FN92]

• expensing intangible drilling and development costs of oil and gas wells; [FN93]

• reporting income from installment sales on other than the installment basis; [FN94]

• use of the last-in, first-out inventory method; [FN95]

• deferral of gain on an exchange of like-kind property [FN96] and identification of the replacement property in a deferred exchange; [FN97]

• deferral of gain on involuntarily converted property; [FN98]

• the use of a simplified dollar-value LIFO method; [FN99] and

• application of rules to futures and forward contracts. [FN100]

Each of these elections has important substantive tax consequences and, if not properly made, may be invalid. For example, the IRS has consistently taken the position that to be eligible to defer gain under section 1033 with respect to an involuntary conversion of property, the election to defer must be made by the appropriate taxpayer. Thus, when a partnership divided into two partnerships following an involuntary conversion of property, the IRS applied that principle to rule that both of the new partnerships were continuations of the former partnership and each was an appropriate taxpayer for purposes of the section 1033(a)(2)(A) election. [FN101] The courts have generally supported the IRS in that position. [FN102]

***383 B. Attribution and Related-Party Determinations**

Section 707(b) disallows losses from sales or exchanges of property (other than an interest in the partnership), directly or indirectly, between a partnership and a person owning, directly or indirectly, more than 50 percent of the capital interest, or the profits interest, in “such partnership,” or two partnerships in which the same persons own, directly or indirectly, more than 50 percent of the capital interests or profit interests.

For purposes of determining common ownership, the ownership of a capital or profits interest in a partnership is determined in accordance with the rules for constructive ownership of stock provided in section 267(c) other than paragraph (3) of that section. [FN103] Under section 267(c), stock owned, directly or indirectly, by or for a partnership is considered as being owned proportionately by or for its partners. What is the partnership and who are its partners for purposes of applying these rules in the context of a **series LLC**?

> **Example:** World **Series LLC** is a Delaware LLC with three series: Series A, Series B, and Series C, each representing one-third of the capital and profits of the LLC. Mr. G owns 100 percent of the capital and profits interests in Series A, 30 percent of the capital and profits interests in Series B, and 30 percent of the capital and profits interests in Series C. The remaining interests in each series are owned by unrelated persons. World **Series LLC** sells to Mr. G at a loss an asset owned by Series C. Is the loss disallowed by section 707(b)? Similarly, what if Mr. G owns 100 percent of the capital and profits interests in Series A, but only 10 percent of the capital and profits interests in Series B and 10 percent of the capital and profits interests in Series C, and Series A sells an asset to Mr. G at a loss?

The answer to those questions depends on how each series of World **Series LLC** is classified for federal income tax ***384** purposes. If each series constitutes a separate entity, the loss on the sale by Series C to Mr. G should be allowed, because Mr. G, who does not own more than 50 percent of Series C, is unrelated to Series C for purposes of section 707(b). However, if Series A, Series B, and Series C are classified as a single entity for federal income tax purposes, the loss will be disallowed under section 707(b), because Mr. G owns 53.34 percent of the total LLC interests (100 percent of Series A plus 30 percent of Series B and 30 percent of Series C).

C. Termination of a Partnership

A partnership will be considered terminated if no part of any business, financial operation, or venture of the partnership continues to be carried on by any of its partners in a partnership, [FN104] or within 12 months there is a sale or exchange of 50 percent or more of the total interest in partnership capital and profits. [FN105] The question is whether a sale or exchange of 50 percent or more of the total interest in a single series would affect the continuation only of that series or also of the remaining series, as to which no sale or exchange of interest occurs.

> **Example:** Real Estate LLC is a Delaware **series LLC** with three series of interests, Series A, Series B, and Series C. Each series owns a separate apartment complex, and each series is owned in equal thirds by Messrs. A and B and Ms. C. Messrs. A and B transfer their interests in Series A to Mr. D. Thus, after the transfer, Series A is owned 66-2/3 percent by Mr. D and 33-1/3 percent by Ms. C, so there has been a sale or exchange of 50 percent or more in the total interest in the capital and profits of Series A, but there has not been a sale or exchange of 50 percent or more of the total interests in the LLC's capital and profits. What, if anything, terminates?
>
> ***385 Example:** Assume the same ownership of the Real Estate LLC Series A, Series B, and Series C interests as in the foregoing example. Each of Messrs. A and B and Ms. C transfers to Mr. D 15 percentage points of his or her one-third interest in Series A, 15 percentage points of his or her one-third interest in Series B and all of his or her interest in Series C. After the transfer, Mr. D owns 45 percent of the interests in Series A and Series B, and all of the interests in Series C, which means that 63.3 percent of the total interests in the LLC's capital and profits (45 percent of Series A, 45 percent of Series B, and 100 percent of Series C) has been transferred to Mr. D.

Again, the question is what terminates? If the LLC is a single entity, Mr. D's acquisition of 63-2/3 percent of the total LLC interests clearly would result in a termination. If each series is a separate entity, however, the threshold change of ownership has occurred only with respect to series C.

D. Allocation of Nonrecourse Liabilities

A partnership liability is considered to be a recourse liability to the extent any partner or partners (or any person related to a partner or partners) bears the economic risk of loss for the liability. [FN106] If no partner or related person bears the economic risk of loss for a partnership liability, the liability will be deemed to be a nonrecourse liability of the partnership. [FN107] Subject to some special rules that may apply, [FN108] nonrecourse liabilities of a partnership are shared by its partners in accordance with the partners' shares of partnership profits.

In contrast to a limited partnership, in which the general partner always will be deemed to bear the risk of loss with respect to any general liability of the partnership (absent nonrecourse language in the appropriate credit instrument), the liabilities of an LLC always will be nonrecourse unless an individual member or manager has agreed to bear the risk of ***386** loss. How will those rules be applied in the context of a **series LLC**?

Example: Chicago LLC is a **series LLC** formed under Illinois law with three series: Series A, Series B, and Series C. Series A is owned by Mr. P, who has a basis of $10,000 in his LLC interest. Series B is owned by Ms. Q, who has a basis of $20,000 in her LLC interest. Series C is owned by Mr. R., who has a basis of $50,000 in his LLC interest. Series A borrows $100,000 from Lender Y secured exclusively (on a nonrecourse basis) by the assets used in the business of Series A. Shortly after borrowing the $100,000, Chicago LLC makes a distribution of $25,000 to each of Messrs. P and R and Ms. Q out of assets of his or her series.

If Chicago LLC is a single entity (and assuming equal profit-sharing percentages by all members), no member will recognize gain from the distribution under section 731, because the amount of money distributed to each ($25,000) will not exceed his or her adjusted basis in the LLC immediately before the distribution (Mr. P will have a basis of $43,333, Ms. Q will have a basis of $53,333, and Mr. R will have a basis of $83,333). In contrast, if each series is a separate entity for subchapter K purposes, Mr. P still will recognize no gain (basis of $110,000 and a distribution of $25,000), Mr. R likewise will recognize no gain (basis of $50,000 and a distribution of $25,000), but Ms. Q will recognize a gain of $5,000 (basis of $20,000 and a distribution of $25,000).

A more complex analysis will apply if the series are deemed to be separate entities and the funds distributed to Ms. Q and Mr. R are derived from the proceeds of the borrowing by Series A. [FN109]

***387 E. Forming a Series LLC** for a New Business

Section 721 provides that no gain or loss will be recognized by a partnership or any of its partners for a contribution of property to the partnership in exchange for an interest in the partnership. Thus, if Mr. A and Ms. B join together to transfer appreciated assets to a new LLC in which each will have a 50 percent interest, neither Mr. A nor Ms. B will recognize any gain from the transfer if the partnership does not assume any liabilities in connection with the transfer. It does not matter that the assets transferred to the LLC by Mr. A and Ms. B differ significantly (for example, Mr. A transfers the assets of a pickle packing business and Ms. B transfers the assets of a fishing business). [FN110]

But what if Mr. A and Ms. B want to keep separate the liabilities of the two businesses to be operated by the new LLC and therefore they form a **series LLC** to operate them? Assume, for example, Mr. A transfers the pickle packing assets to Pickled Fish LLC, Series A, and Ms. B transfers the assets of the fishing business to Pickled Fish LLC, Series B. Is the result the same?

Depending on the tax classification of the series, Mr. A and Ms. B may be in for an unpleasant surprise. If each series is treated as a separate taxable entity, Mr. A and Ms. B will each be deemed to have swapped one-half of his or her interest in each business for one-half the interest in the other's business, causing each to recognize gain on any appreciation in the assets deemed to have been transferred. [FN111]

F. Converting an Existing LLC to a Series LLC

Assuming each series of an LLC is treated as a separate legal entity for federal income tax purposes, the conversion of an existing LLC to a **series LLC** will constitute a division of the LLC under section 708(b)(2)(B) and reg. section 1.708-1(d)(1). Any series whose members had more than a 50 percent interest ***388** in capital and profits of the preexisting LLC will be considered a continuation of the preexisting LLC. [FN112]

For any series comprised of members who had a 50 percent or less interest in capital and profits of the preexisting LLC, the new series will be treated as a new partnership. [FN113] If none of the series meets the 50 percent test, the original LLC will be deemed to have been terminated. [FN114] When a transfer of assets is made by an existing LLC to several new series, the existing LLC will be deemed for tax purposes to have transferred the assets to the new series in the “assets over” form and thereafter to have liquidated by distributing the member interests in the new series to the existing LLC's members. [FN115]

The IRS takes the position that a partnership division exists only if at least two partners from the prior partnership are partners in each resulting partnership. [FN116] Accordingly, if a preexisting LLC converts to a **series LLC** with three series, Series A, Series B, and Series C, with each series owned by one of the former members of the preexisting LLC, the conversion *may* be treated as a liquidation of the LLC rather than a division, since each series of the LLC will be a disregarded entity for tax purposes, unless it “checks the box.” The conditional qualification on this conclusion is due to the fact that the IRS may treat the individual members of the three disregarded entities themselves as a partnership for federal income tax purposes.

Obviously, to achieve the benefits of any statute regarding limited liability protection vis-á-vis another series, the members of the preexisting LLC would have to sort out various liabilities with creditors or notify those creditors of the conversion.

Depending on the nature and extent of the appreciation in the assets of the LLC, any one of the members in this scenario may be deemed to have received a distribution of section 704(c) property contributed by another (the interest of the new series ***389** will be treated under the section 704 regulations as substitute section 704(c) property), [FN117] with the result that the contributing member may be required to recognize a portion of his or her built-in gain. Gain also may have to be recognized under section 737, because a member contributing section 704(c) property would receive from the LLC property (an interest in the other series) other than the contributing member's own section 704(c) property. [FN118]

Thus, the same tax trap may await Mr. B and Ms. C in the Pickled Fish LLC scenario outlined above if they contribute the assets first to a “plain vanilla” LLC and after an appropriate period create a separate series for each business. The creation of the series may be treated as a partnership division under section 708.

G. Interseries Transfers

Like several of the preceding examples, interseries transfers of assets of a **series LLC** may have significantly different tax consequences depending on the tax classification of the series.

> **Example:** Manufacturing LLC consists of two series, Series A and Series B. Series A and Series B are owned identically by Mr. A and Ms. B. Series A units represent an interest in a computer manufacturing business. Series B units represent an interest in a television production business. During the year, several assets of the computer manufacturing business are transferred without consideration for use in the television production business.

If each of Series A and Series B is treated as a separate partnership for subchapter K purposes, the transfer of assets from one series to the other series may cause the transferring series, and hence Mr. A and Ms. B, to recognize gain, depending on various factors, including Mr. A's and Ms. B's bases in their interests in the transferring series. [FN119]

*390 VI. Common Law Series LLCs

The foregoing analysis prompts one more question concerning **series LLCs**, which is whether a **series LLC** statute is necessary to achieve separate tax classification for each series of an LLC or whether the same result can be achieved in a jurisdiction with no series statute simply through careful drafting of the LLC's certificate of formation, articles of organization, and LLC agreement. Admittedly, one might draw significant comfort from several provisions in the statutes, but are they really necessary for tax classification purposes?

Most of the statutes go a long way in providing attributes that contribute to separate treatment. Almost all, for example, provide that none of the debts, liabilities, obligations, and expenses that are incurred, contracted for, or otherwise existing with respect to one series will be enforceable against the assets of another series. All also provide for the creation of interests having separate rights, powers, and duties with respect to specified property or obligations, and for profits and losses associated with specified property or obligations to be allocated separately. Most allow any series to be terminated and its affairs wound up without causing the dissolution of the LLC itself.

As noted, the Illinois statute goes even further. It specifies that each series with limited liability may contract, hold title to assets, grant security interests, sue and be sued, and otherwise conduct business and exercise the powers of an LLC under the Illinois act, all in its own name. It also authorizes “consolidation” of the operations of several series “to the extent permitted under applicable law,” and provides that two or more series may elect to contract jointly or elect to be treated as a single business for qualification purposes to do business in Illinois or any other state without affecting the limitations of liability set forth in the statute.

***391** But is it the presence of these provisions in the statutes, or simply the legal relationship they create among the series -- a relationship that it should be possible to create by contract even absent the statute, for example, through the LLC's certificate of formation or articles of organization and LLC agreement -- that is most important from a tax perspective? After all, there was nothing in the Massachusetts business trust in GCM 39211 or in the partnership agreement in Rev. Rul. 55-39 that relied on statutory provisions to accord separate tax status to different portions of their investment portfolios. Accordingly, while most practitioners, if given the choice, would still opt for statutory limitations on liability while achieving the desired separate tax status of a series, in cases in which liability can be controlled by contract, [FN120] it should be possible *for federal income tax purposes* to achieve separate entity status for each of several interests within a single LLC through careful drafting of the LLC's certificate of formation and articles of organization or limited liability company agreement. [FN121]

VII. Conclusions

Despite the growing number of states that have enacted **series LLC** statutes, their use is inhibited by the lack of definitive guidance on how these new entities should be taxed. The IRS is clearly aware of the issue, but has chosen to be silent to date. [FN122]

Pending the issuance of clearer guidance, practitioners desiring to treat an LLC's series as separate taxable entities for federal income tax purposes should do all they can to imbue each series with separate status. Whether formed and operated under one of the **series LLC** statutes or simply by agreement, the LLC should adhere strictly to the requirements spelled out in the statutes for segregating the assets of one series from those of another, for example, the explicit creation of separate series, the maintenance of separate and distinct records, holding and separate accounting of assets of each series and, where required, appropriate naming of the series. A separate ***392** employer identification number should be obtained for each series and a separate tax return should be filed for each. Finally, as with the case of multiple corporations operated by common owners, those using a **series LLC** should be certain to respect in all contracts, correspondence, business cards, and so on the separate identity of each series of the LLC. Whether that will carry the day in each instance remains uncertain, but even absent definitive guidance from the IRS, there is clear authority to support this result.

[FN1]. *See*, *e.g.*, Robinson, *Federal Income Taxation of Real Estate* (6th Ed. 1998) at para. 8-02[1] [e]. ("In the past, limited partnerships were used as vehicles for raising equity capital for real estate ventures. Their attraction is that they combine the limited liability feature of an investment in corporate stock with the tax advantages of a partnership. . . . Their allure as investment vehicles has diminished, however, with the advent of LLCs . . . that offer these same advantages.") The introduction of single-member LLCs with the adoption of the entity classification rules in reg. section 1.7701-1 et seq. provided still more planning opportunities for businesses domestically and internationally. *See*, *e.g.*, Schinner, "IRS Rulings Expand Opportunities for Using Single-Member LLCs on 1031 Exchanges," 88 *Journal of Taxation* 286 (May 1998); Bryant, "Check-the-Box Regulations Focus Attention on Planning Possibilities With Single-Member LLCs," 4 *Journal of Limited Liability Companies* 46 (Fall 1997); Lowell, "International Use of LLCs and the 'Check-the-Box' Proposal," 2 *Journal of Limited Liability Companies* 57 (Fall 1995).

[FN2]. Limited liability for individual partners of a limited partnership can be achieved generally by using a corporation or other limited liability entity to serve as general partner, but doing so requires separate registrations and filings for both entities under state law, as well as multiple tax returns at the federal and state level. Many hedge funds and private equity funds nevertheless continue to favor the limited partnership format, apparently due to its long-standing familiarity to investors.

[FN3]. Some people refer to a **series LLC** as a cell LLC or a mini-LLC.

[FN4]. **Series LLCs**, as a general rule, are creatures of state law, *but see* the discussion *infra* regarding the creation of a **series LLC** by contract or agreement.

[FN5]. *See*, *e.g.*, Del. Code Ann. tit. 6, section 18-215.

[FN6]. An LLC is a corporation for purposes of the U.S. Bankruptcy Code, 11 U.S.C. section 101(9), and hence a person, 11 U.S.C. section 101(41), eligible for relief under chapters 7 (liquidation) and 11 (reorganization) of the Bankruptcy Code. 11 U.S.C. section 109(b) and (d). *See* 2 *Collier on Bankruptcy* (15th ed. revised) (hereinafter "Collier") at para. 101.09. Whether a single series of a **series LLC** would itself constitute a corporation and hence a person for purposes of bankruptcy eligibility is a question of first impression. Bankruptcy courts likely would look first to the degree of separateness conferred on a designated series by the law of the **series LLC's** state of incorporation. The court may be inclined to presume rebuttably that a designated series of a **series LLC** is a separate corporation for purposes of the Bankruptcy Code and may rely on the bankruptcy doctrine of substantive consolidation if necessary to remedy abuse. Substantive consolidation is the equitable doctrine whereby corporate entities are disregarded to create a single pool of assets and a single body of creditors when related but ostensibly separate affiliates have been operated as a single entity.

[FN7]. At least one state permits a foreign LLC to identify, on its application for authority to do business in the state, which of the protections accorded series under the state statute apply to the series. *See* Utah Code Ann. section 48-2c-606. Still, the separate series of a foreign LLC may not be accorded all of the same protections offered by the LLC's home state.

[FN8]. *See*, *e.g.*, Gerson, "**Series LLC** Tax Issues: Limited Liability Companies," 35(7) *The Tax Adviser* 416 (2004); Cuff, "**Series LLCs** and the Abolition of the Tax System," *Tax Law and Estate Planning Course Handbook Series*, Practising Law Institute (June 2004) (*reprinted from Business Entities*, vol. 2, no. 1, Warren Gorham & Lamont (Jan./Feb. 2000); Charles T. Terry and Derek D. Samz, "An Initial Inquiry Into the Federal Tax Classification of Series Limited Liability Companies," *Tax Notes*, Mar. 6, 2006, p. 1093, *Doc 2006-3770, 2006 TNT 44-40*. For a discussion of state income tax issues regarding **series LLCs**, see McLoughlin and Ely, "**Series LLCs**: Many State Tax Questions Are Raised but Few Answers Are Yet Available," *Business Entities* (WG&L) Jan./Feb. 2007.

[FN9]. The Delaware Limited Liability Company Act was amended in 1996 to add series provisions. *See* Del. Code Ann. tit. 6, section 18-215.

[FN10]. Del. Code Ann. tit. 6, section 8-101 et seq.

[FN11]. Del. Code Ann. tit. 6, section 18-215(a).

[FN12]. *Id*.

[FN13]. Del. Code Ann. tit. 6, section 18-215(b).

[FN14]. *Id*.

[FN15]. Del. Code Ann. tit. 6, section 18-215(d).

[FN16]. *Id*.

[FN17]. *Id*.

[FN18]. *Id*.

[FN19]. Del. Code Ann. tit. 6, section 18-215(e). Unless the LLC agreement of a Delaware **series LLC** provides otherwise, the management of a series is vested in the members associated with that series in proportion to their then-current percentage interests in the series. Del. Code Ann. tit. 6, 18-215(f).

[FN20]. Del. Code Ann. tit. 6, section 18-215(e).

[FN21]. Del. Code Ann. tit. 6, section 18-215(f).

[FN22]. Del. Code Ann. tit. 6, section 18-215(j). However, a dissolution of the **series LLC** itself will result automatically in the dissolution of each of its series; that is, a series cannot survive on its own without the **series LLC**.

[FN23]. Del. Code Ann. tit. 6, section 18-215(h). For purposes of this limitation, the term "distribution" does not include amounts constituting reasonable compensation for current or past series or reasonable payments made in the ordinary course of business under a bona fide retirement plan or other benefits program.

[FN24]. *See* Iowa Code section 490A.305, adopted in 1997; *compare* Del. Code Ann. tit. 6, section 18-215.

[FN25]. 805 ILCS section 180/37-40.

[FN26]. 805 ILCS section 180/37-40(b).

[FN27]. 805 ILCS section 180/37-40(d).

[FN28]. *See* 805 ILCS section 180/37-40(b).

[FN29]. Three states have discussed in administrative rulings the tax classification of **series LLCs**. *See infra* note 65.

[FN30]. *See* 805 ILCS section 180/37-40(b). The statute leaves unclear whether the "applicable law" referred to here is state law or both state law and federal law, for example, the IRC.

[FN31]. Although the provisions of 805 ILCS section 180/37-40(b) suggest that an Illinois LLC with multiple series qualifying to do business in another state may elect to be treated as a single business for purposes of that state's registration, at least one state requires separate registration of each series doing business there, regardless of its jurisdiction of formation. *See* "Ask the Advocate," State of California Franchise Tax Board, Mar./Apr. 2006, *Tax News*. ("Our current position is that each series in a **series LLC** is considered a separate LLC and must file its own Form 568 Liability Company Return of Income and separate LLC annual tax and fee if it is registered or doing business in California.") This position by the FTB is consistent with its more recent statement that it will recognize a **series LLC** as a separate business entity, subject to some conditions. *See* discussion at *infra* note 65. Both the Illinois statute and the position of the California FTB suggest also that a single series may register to do business as an LLC in California, even if the **series LLC** itself does not (or is not required to) register.

[FN32]. 805 ILCS section 180/37-40(b).

[FN33]. 805 ILCS section 180/37-40(c).

[FN34]. 805 ILCS section 180/37-40(d).

[FN35]. *See* Nev. Rev. Stat. section 86.011 et seq.

[FN36]. Nev. Rev. Stat. section 86.296(1).

[FN37]. *Id.*

[FN38]. Nev. Rev. Stat. section 86.296(2).

[FN39]. *Id.*

[FN40]. Nev. Rev. Stat. section 86.296(3).

[FN41]. Nev. Rev. Stat. section 86.343(2)(a).

[FN42]. Nev. Rev. Stat. section 86.343(2)(b).

[FN43]. 18 Okla. St. Ann., section 20544.4.

[FN44]. *See* 18 Okla. St. Ann. section 2054.4(k).

[FN45]. Utah Code Ann. section 48-2c-606 et seq.

[FN46]. Utah Code Ann. section 48-2c-606(1)(a).

[FN47]. *See* Utah Code Ann. section 48-2c-606(3); *compare* Del. Code Ann. tit. 6, section 18-215(b).

[FN48]. *See* Utah Code Ann. section 48-2c-606(5).

[FN49]. *Compare with* 805 ILCS section 180/37-40(b).

[FN50]. Utah Code Ann. section 48-2c-616.

[FN51]. *Id.*

[FN52]. Tenn. Code Ann. section 48-249-309 et seq.

[FN53]. Tenn. Code Ann. section 48-249-309(b).

[FN54]. Tenn. Code Ann. section 48-249-309(i).

[FN55]. *See* Limited Liability Company Act of 1996, as amended by P.L. 2000-14, section 79.

[FN56]. *See* A. Aaron, Invest Offshore (Offshore Investing blog) at http://www.investoffshore.com/blog/2006/11/the_incredible_series_llc.php (Nov. 15, 2006).

[FN57]. *See*, *e.g.*, 18 Okla. St. Ann., section 2054.4(c).

[FN58]. *See* 805 ILCS section 180/37-40(b).

[FN59]. *Id.*

[FN60]. Bishop and Kleinberger, *Limited Liability Companies: Tax and Business Law* (WG&L 1994) at para. 2.11[2].

[FN61]. *See* 805 ILCS, section 180/37-40(b).

[FN62]. *See*, *e.g.*, Del. Code Ann. tit. 6 section 18-209.

[FN63]. *See*, *e.g.*, Del. Code Ann. tit. 8, section 266.

[FN64]. *See*, *e.g.*, Del. Code Ann. tit. 6, section 18-902.

[FN65]. Although the state tax authorities of at least three states have expressed their views on **series LLCs**, taxpayers' ability to rely on these interpretations is questionable. Delaware, for example, has ruled informally that it will treat all series of an LLC under the first of these scenarios, that is, as branches or divisions of their owner. *See* Del. Dept. of Fin., Informal Ruling, Sept. 16, 2002. According to the Department of Finance, because all of the interests with respect to the series are owned by a single entity (the LLC), those series will be treated as branches or divisions of their owner, like how a single-member LLC is treated. The department ruled further that transfers among series would be disregarded for purposes of Delaware taxation -- including transfer taxes -- because they have the same owner and the separate series are merely bookkeeping segregations of assets and liabilities. New York has reached a contrary result, ruling that each series will be treated as a separate partnership. *See* Advisory Opinion of the State of New York Commissioner of Taxation and Finance, TSB-A-98(8)I (Sept. 4, 1998). There is some ambiguity in the advisory opinion's rulings, but this appears to be the conclusion intended. Most recently, California has indicated that at least until the IRS decides to classify **series LLCs** as something else, it will recognize each series as a separate business entity if it meets some requirements. To quote the FTB:

> The classification of an eligible business entity for California tax purposes shall be the same as the classification of the entity for federal tax purposes. Currently, the IRS has not provided any guidance on whether a series within a Delaware **Series LLC** (*e.g., most common **Series LLC**)* is a separate entity or part of a single **Series LLC** entity. *The Franchise Tax Board has taken the position that a series within the **Series LLC** will be considered a separate business entity if: (1) the holders of interests in that series are limited to the assets of that series upon redemption, liquidation, or termination, and may share in the income only of that series; and (2) under state law, the payment of the expenses, charges, and liabilities of that series is limited to assets of that series. Each series that is a separate business entity and registered or doing business in California must file their own California tax return, pay the annual tax, and may be subject to a fee based on total annual income.*

[emphasis in original] California FTB 689 (Rev. 02-2007).

[FN66]. Regardless of the state law under which a **series LLC** is formed, federal tax law, not state tax law, will apply to determine the proper classification of the entity for federal income tax purposes. Reg. section 301.7701-1(a)(1).

[FN67]. *See, e.g., Bergford v. Commissioner,* 12 F.3d 166, *Doc 94-368, 93 TNT 264-10* (9th Cir. 1993) (arrangement between owners of computer equipment and manager of sale-leaseback program to finance, purchase, lease, and remarket equipment classified as a partnership); *Bussing v. Commissioner*, 89 T.C. 1050 (1987) (purported sale of computer equipment and indirect leaseback classified as a partnership); and *Alhouse v. Commissioner,* T.C. Memo. 1991-652 (venture for leasing equipment under a comprehensive leasing program classified as a partnership). *See also* TAM 7951006 (complex arrangement among co-owners of undivided interests in a pipeline classified as a partnership); and LTR 7919065 (agreement among corporation, municipalities, and cooperatives to share ownership and generating output at cost of a nuclear generating plant classified as a partnership).

[FN68]. *See* Figure 2.

[FN69]. *See* Figure 3.

[FN70]. Reg. section 301.7701-4.

[FN71]. A domestic business entity with two or more members will be classified for federal tax purposes as either a corporation or a partnership. A business entity with only one owner will be classified as a corporation or as a disregarded entity. Reg. section 301.7701-3(b).

[FN72]. 296 U.S. 344 (1935).

[FN73]. 337 U.S. 733 (1949).

[FN74]. *Id.* at 742. *Compare* reg. section 301.7701-4(a) (a trust formed to take title to property for the purpose of protecting or conserving it for the beneficiaries will be classified as a trust) and reg. section 301.7701-4(b) (an entity formed as a trust as a device to carry on a profit-making business that normally would have been carried on through a business organization will be classified as a corporation or partnership under the IRC).

[FN75]. 337 U.S. at 754 (1949).

[FN76]. *See* Gerson, *supra* note 8.

[FN77]. *See* Delaware Code Ann., tit. 12, section 3801(a).

[FN78]. *See National Securities Series-Industrial Stocks Series v. Commissioner*, 13 T.C. 884 (1949), *acq*. 1950-1 C.B. 4.

[FN79]. 1955-1 C.B. 416.

[FN80]. *See*, *e.g.*, LTR 9819002, *Doc 98-14482, 98 TNT 90-46* (May 8, 1998). In light of the weight *National Securities* is accorded in these rulings, it is surprising how little it really says on this issue. Still, that has not prevented (or discouraged) the IRS from relying on it to find separate entity status for each series of statutory trusts, where it seems to gloss over any shortcomings in the decision. A good example is the following excerpt from LTR 9819002, which is representative of many similar rulings:

> Although the classification of the entities in [*National Securities*] was not an issue, the court *assumed* in its opinion that each of the several series created under a single trust instrument was a separate taxpayer. Rev. Rul. 55-416 . . . repeats the Tax Court's *tacit* characterization of the series funds as separate taxpayers. [Emphasis added.]

[FN81]. 1955-1 C.B. 403.

[FN82]. Reg. section 301.7701-2(a).

[FN83]. *See* sections 441 and 442. Unless indicated otherwise, all section references are to the Internal Revenue Code of 1986, as amended.

[FN84]. *See* section 446.

[FN85]. *See* section 775.

[FN86]. *Id.*

[FN87]. *See* section 754; reg. section 1.754-1(b).

[FN88]. *See* section 755; reg. section 1.755-1.

[FN89]. *See* section 168.

[FN90]. *See* section 169.

[FN91]. *See* section 174.

[FN92]. *See* section 179; reg. sections 1.179-1 through 1.179-5.

[FN93]. *See* section 263(c).

[FN94]. *See* section 453.

[FN95]. *See* section 472.

[FN96]. *See* section 1031.

[FN97]. *See* reg. section 1.1031(k)-1(c).

[FN98]. *See* section 1033.

[FN99]. *See* section 474.

[FN100]. IR News Release 82-13 (Jan. 22, 1982).

[FN101]. *See* LTR 8244124 (Aug. 9, 1982).

[FN102]. *See, e.g.*, *Demirjian v. Commissioner*, 54 T.C. 1691 (1970), *aff'd*, 457 F.2d 1 (3d Cir. 1972); *Myers v. United States*, 72-2 USTC (S.D. Cal. 1972); *Varner v. Commissioner*, T.C. Memo. 1973-27, 32 TCM 97.

[FN103]. *See* section 707(b)(3).

[FN104]. Section 708(b)(1)(A).

[FN105]. Section 708(b)(1)(B).

[FN106]. Reg. section 1.752-1(a)(1).

[FN107]. Reg. section 1.752-1(a)(2).

[FN108]. *See, e.g.*, reg. section 1.752-3(a).

[FN109]. *See* discussion at note 119, *infra*.

[FN110]. Reg. section 1.721-1.

[FN111]. Rev. Rul. 99-5, 1999-1 C.B. 434, *Doc 1999-2045, 1999 TNT 10-6*.

[FN112]. Reg. section 1.708-1(d)(1).

[FN113]. *Id.*

[FN114]. *Id.*

[FN115]. Reg. section 1.708-1(d)(3).

[FN116]. T.D. 8925, *Doc 2001-645, 2001 TNT 3-9* (Jan. 4, 2001).

[FN117]. Reg. section 1.704-3(a)(8)(i).

[FN118]. Reg. section 1.737-1.

[FN119]. The IRS likely would view such a transfer as a distribution of the transferred assets to Mr. A and Ms. B, followed by a contribution of the distributed assets to the other series. Note also that such a transfer may violate the separateness requirements of state law applicable to the LLC. *See, e.g.*, Del. Code Ann. tit. 6, section 18-215(b).

[FN120]. Consider, for example, the following relatively standard nonrecourse language found in a real estate financing, modified slightly (in italics) to apply instead to a single series of a **series LLC**:

> Notwithstanding anything to the contrary contained herein, any claim based on or in respect of any liability of the Borrower under this Loan Agreement or any other Loan Document shall be enforced only against the *assets of Borrower Series A*, and not against any other assets, properties or funds of the Borrower *generally or as the assets, properties or funds of any series of the Borrower other than Series A* or against its *or their* direct or indirect officers, directors, members, partners, shareholders, or other beneficial owners thereof, employees, representatives and agents and each of their permitted successors and assigns.

It is less likely such an LLC could protect assets in one series from creditors of another series when the creditor's claim arises in tort.

[FN121]. *But see* California Franchise Tax Board FTB 689, note 65 *supra*, in which the Franchise Tax Board indicates that it will recognize a series within a **series LLC** as a separate business entity only if, among other things, *under state law* the payment of the expenses, charges, and liabilities of that series is limited to assets of the series. Based on the federal authorities cited above, there is no reason to believe such state law protection is required for separate federal tax classification.

[FN122]. At least as early as August 2004, the issue was presented to the Treasury Department in private correspondence in which a practitioner suggested there was an "urgent need for guidance in this evolving area." *See Doc 2004-18367, 2004 TNT 181-23*. More recently, a panel at the American Bar Association Section of Taxation Sales, Exchanges, and Basis Committee meeting held in San Diego on Feb. 4, 2006, discussed the uncertainty of this area and the need for governmental guidance. There has been no response from Treasury.

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