

Recent Amendments to Delaware’s LLC and LP Acts: Registered Series of LLCs Will Be Permitted Starting in 2019 and LLCs Can Now Divide, among Other Changes

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As recently amended, the Delaware Limited Liability Company Act (the “DLLCA”) now permits, among other things, the “division” of a Delaware limited liability company (“LLC”) into new LLCs and the formation of statutory for-profit LLCs intended to produce public benefits. In addition, beginning August 1, 2019, Delaware LLCs will be able to form “registered series.” While having most of the advantages of LLC series that can currently be established, registered series will also be “registered organizations” under Article 9 of the UCC, with the result that a secured party will be able to perfect security interests in most assets of such series by filing a financing statement in Delaware.

Aside from the amendments relating to registered series of LLCs, all of the amendments discussed below to the DLLCA and the Delaware Revised Uniform Limited Partnership Act (the “DRULPA”) took effect on August 1, 2018.

Registered Series of LLCs

The DLLCA has permitted the establishment of series of LLC members, managers, interests, and assets since 1996. One of the attractive features of LLC series is that if certain statutory conditions are met, the assets associated with a given series are shielded from claims of creditors against other series of the LLC or against the LLC as a whole. 6 *Del. C.* § 18-215(b).

Yet LLC series have created challenges for anyone trying to situate them within the framework of UCC Article 9. A series established under the current DLLCA does not meet the UCC’s definition of “registered organization” because such a series is not formed or organized “by the filing of a public organic record” with the state. UCC § 9-102(a)(71). Thus, it is unlikely that a security interest in the assets of a series can be perfected simply by filing a financing statement in Delaware, as would be the case with assets of a Delaware corporation, LLC, or other registered organization. Instead, one may need to file in the state where the series’ place of business or chief executive office is located, treating the series in the same way one would treat a common law partnership.*

Amendments to the DLLCA, taking effect August 1, 2019, will help resolve the series-perfection issue by enabling Delaware LLCs to form series that will constitute “registered organizations” under Article 9. (For the registered-series amendments, see Delaware Senate Bill 183, 149th General Assembly.) The amendments will distinguish between a “protected series” and a “registered series.” The term “protected series” will be used to refer to a shielded series of the type that can currently be established. “Registered series” will refer to a series formed by the filing of a certificate of registered series with the Delaware Secretary of State. Since a registered series will accordingly be formed “by the filing of a public organic record” with the state, it will be a registered organization under UCC Article 9, and secured parties will therefore be able to perfect security interests in most types of assets owned by a registered series by filing a financing statement with the Delaware Secretary of State.

The certificate of registered series must provide the name of the LLC forming the registered series and the name of the registered series itself.

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The name of a registered series must begin with the full name of the LLC, need not include the word “Series,” and must meet the existing requirement of distinctness from the names of other entities on the records of the Secretary of State. The requirement that the registered series’ name start with the LLC’s name should help ensure that someone searching in Delaware on, for example, the word “borrower” for liens recorded against Borrower LLC will also find liens recorded against any registered series of Borrower LLC, such as Borrower LLC Fund X, Borrower LLC Fund Y, etc. The amendments will also permit the reservation of registered-series names just as the DLLCA already permits the reservation of LLC names. Unlike the certificate of formation for a Delaware LLC, a certificate of registered series will not be required to identify a registered agent in Delaware. Instead, the registered agent of an LLC will also be the registered agent for any registered series formed by the LLC.

A registered series will not necessarily have the asset-shielding characteristics of a protected series. For a registered series to be shielded, it will need to satisfy the same conditions as those currently in place for shielded series, i.e., the records maintained for the series must “account for the assets associated with such series separately from the other assets of the [LLC], or any other series thereof,” plus the LLC’s certificate of formation must provide “[n]otice of the limitation on liabilities” of the series, and the LLC agreement must permit the formation of series. Neither the certificate of formation nor the LLC agreement, however, must refer specifically to *registered* series or to the applicable section of the DLLCA (which will be § 18-218) for the foregoing conditions to be met.

In keeping with a registered series’ status as a registered organization, the amendments will provide for the filing of a certificate of amendment to amend a certificate of registered series and the filing of a certificate of

cancellation to cancel a certificate of registered series after the series has been dissolved and wound up. The Secretary of State will issue—as requested and appropriate—a certificate of good standing for a registered series. The annual Delaware tax on registered series will initially be set at \$75 per series and will be due on June 1, the same date when the annual tax payable by the LLC (currently set at \$300) is due.

Protected series will be able to convert into registered series of the same LLC and vice versa. Also, two or more registered series of the same LLC will be permitted to merge. No series will be permitted to convert or merge under any other provisions of the DLLCA.

LLC Division

The amendments make possible for the first time the “division” of a Delaware LLC into multiple Delaware LLCs and the allocation of assets and liabilities among such LLCs without causing thereby a transfer or distribution for purposes of Delaware law. According to the terminology used in new DLLCA § 18-217, the LLC effecting the division is the “dividing company” and will be the “surviving company” if it survives the division. The LLC or LLCs created in the division are “resulting companies” and, together with the surviving company (if any), are also “division companies.” 6 *Del. C.* § 18-217(a).

To divide, an LLC (the dividing company) must first adopt a plan of division. 6 *Del. C.* § 18-217(g). By default, the plan must be approved by a majority in interest of the dividing company’s members. 6 *Del. C.* § 18-217(c). The plan must set forth how interests in the dividing company will be dealt with in the division (e.g., cashed out, exchanged for other interests, or left outstanding), how the assets and liabilities of the dividing company will be allocated among the division companies, the names of the surviving company (if any) and the resulting companies, and the name and address

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of a “division contact.” 6 *Del. C.* § 18-217(g). The division contact is an individual residing in Delaware or an entity formed under Delaware law that, for six years following the division, will provide to any requesting creditor of the dividing company the name and address of the division company to which the creditor’s claim was allocated under the plan of division. *Id.* If the dividing company will be a surviving company, the plan of division may also effect any amendment to the operating agreement of the dividing company, unless its operating agreement prohibits an amendment specifically in connection with a division, merger, or consolidation. 6 *Del. C.* § 18-217(f).

The division is effectuated by filing with the Delaware Secretary of State a certificate of division containing, among other things, the name of the dividing company, whether the dividing company is a surviving company, the name of each division company, and the name and address of the division contact. 6 *Del. C.* § 18-217(h). When the certificate of division is filed, a certificate of formation must also be filed for each resulting company. *Id.* The operating agreement of each resulting company becomes effective upon the effectiveness of the division. 6 *Del. C.* § 18-217(i).

The effectiveness of the division causes the assets and liabilities of the dividing company to be allocated among the division companies pursuant to the plan of division. 6 *Del. C.* § 18-217(l). The allocation does not constitute a transfer or a distribution for purposes of Delaware law. 6 *Del. C.* § 18-217(l)(8), (m). Likewise, the division does not by default constitute a dissolution of the dividing company even if it is not a surviving company. 6 *Del. C.* § 18-217(d). Instead, when the dividing company is not a surviving company, its existence will merely “cease” upon the division. 6 *Del. C.* § 18-217(l)(1).

In addition to the requirement of a division contact, a number of provisions in Section 18-

217 should help protect creditors of a dividing company. A division “shall not be deemed to affect the personal liability of any person incurred prior to such division with respect to matters arising prior to such division[.]” 6 *Del. C.* § 18-217(b). Also, if the division is judicially found to constitute a fraudulent transfer, then each division company, including by definition the surviving company (if any), “shall be jointly and severally liable on account of such fraudulent transfer notwithstanding the allocations made in the plan of division[.]” 6 *Del. C.* § 18-217(l)(5). Finally, if any liabilities of the dividing company are not allocated under the plan of division, they will be the joint and several liabilities of all the division companies, again including by definition the surviving company (if any). 6 *Del. C.* § 18-217(l)(6).

Division is available to any Delaware LLC formed on or after August 1, 2018, unless the LLC’s operating agreement provides otherwise. For a Delaware LLC formed earlier, division will be deemed to be governed by the provisions of any written agreement to which the LLC is a party (including its operating agreement) that was entered into before August 1, 2018, to the extent that such provisions restrict, condition, or prohibit a merger of the LLC or transfer of its assets. 6 *Del. C.* § 18-217(o).

Use of Blockchain by LLCs and LPs

In 2017, the DGCL was amended to confirm that blockchain (or “distributed database”) technology could be used by corporations to satisfy certain statutory record-keeping and notice requirements. This year, similar amendments have been made to the DLLCA and the DRULPA to provide certainty regarding the use of blockchain and other “networks of electronic databases” by LLCs and LPs. *See, e.g.,* Del. S.B. 183 syn., 149th Gen. Assem. (2018). Specifically, unless the operating agreement provides otherwise, blockchain may now be used by LLC members and managers, or by LP partners, in appointing proxies and in

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providing consent in lieu of voting at a meeting. 6 *Del. C.* §§ 18-302(d), 18-404(d) (LLCs); 6 *Del. C.* §§ 17-302(e), 17-405(d) (LPs).

Blockchain may also be used by an LLC or LP in maintaining its records, provided that the form in which the records are kept “is capable of conversion into written form within a reasonable time.” 6 *Del. C.* § 18-305(d) (LLCs); 6 *Del. C.* § 17-305(c) (LPs).

Statutory Public Benefit LLCs

A new subchapter, Subchapter XII, has been added to the DLLCA to provide express statutory authorization for the formation of public benefit LLCs. 6 *Del. C.* §§ 18-1201 to 18-1208. As with the blockchain amendments just discussed, the amendments authorizing public benefit LLCs follow similar amendments made previously to the DGCL. *See* 8 *Del. C.* §§ 361-368 (enabling the formation of public benefit corporations, originally adopted in 2013).

A public benefit LLC formed under Subchapter XII is termed a “*statutory public benefit*” LLC because Subchapter XII does not provide the exclusive means for “the formation or operation of a limited liability company that is formed or operated for a public benefit (including a limited liability company that is designated as a public benefit limited liability company)[.]” 6 *Del. C.* § 18-1208. Accordingly, a statutory public benefit LLC (an “SPB-LLC”) is a “for-profit” LLC that not only is “intended to produce a public benefit or public benefits and to operate in a responsible and sustainable manner[.]” but also complies with the other requirements of Subchapter XII. 6 *Del. C.* § 18-1202(a).

Unlike a Delaware public benefit corporation, an SPB-LLC need not include in its name any language or abbreviation indicating that it is a public-benefit entity. Its certificate of formation must only state in the heading that the LLC is an SPB-LLC and set forth the specific public benefit or public benefits that the SPB-LLC will promote. *Id.* In addition, the operating

agreement of an SPB-LLC “may not contain any provision inconsistent with” Subchapter XII of the DLLCA. *Id.* The amendments do not set forth any special approvals that must be obtained for an existing LLC to become an SPB-LLC. (By contrast, the DGCL provides in § 363(a) that a non-public-benefit corporation must obtain the approval of two thirds in interest of its stockholders to become a public benefit corporation.) However, an SPB-LLC may not cease to be an SPB-LLC (including by amending its certificate of formation to remove the public-benefit language) without the approval of two-thirds in interest of the members. 6 *Del. C.* § 18-1203.

The definition of “public benefit” for, and the special standards applicable to, an SPB-LLC are similar to those set forth in the DGCL for a public benefit corporation. A public benefit is “a positive effect (or reduction of negative effects) on one or more categories of persons, entities, communities or interests” aside from the SPB-LLC’s members *qua* members. 6 *Del. C.* § 18-1202(b). The persons who manage the SPB-LLC are required to manage it “in a manner that balances the pecuniary interests of the members, the best interests of those materially affected by the [LLC’s] conduct, and the specific public benefit or public benefits set forth in its certificate of formation.” 6 *Del. C.* § 18-1204(a). Two percent in interest of the members may sue the SPB-LLC derivatively to “enforce” the balanced-management requirement, but no member or manager shall have any monetary liability for failing to meet that requirement. 6 *Del. C.* §§ 18-1206, 18-1204(a).

Moreover, in making a decision that implicates the balanced-management requirement, the persons who manage the SPB-LLC will be deemed to have satisfied their fiduciary duties if the decision is informed, disinterested, and “not such that no person of ordinary, sound judgment would approve.” 6 *Del. C.* § 18-1204(b). No

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member or manager of the SPB-LLC shall, “by virtue of the public benefit provisions” in the operating agreement or in Subchapter XII, have a duty to any person on account of an interest in the SPB-LLC’s stated public benefit or an interest “materially affected” by the SPB-LLC’s conduct. *Id.*

SPB-LLCs are subject to reporting requirements similar to those governing Delaware public benefit corporations. The SPB-LLC must provide to its members at least once every two years a report stating the objectives established to promote its stated public benefit, the standards adopted to measure its progress in promoting such public benefit, “[o]bjective factual information based on those standards regarding” its success in meeting its objectives, and an assessment of such success. 6 *Del. C.* § 18-1205.

Other Amendments to the DLLCA and DRULPA

A new section, modeled on DGCL § 284 as amended this year, has been added to the DLLCA to empower the Delaware Court of Chancery to cancel the certificate of formation of an LLC “for abuse or misuse” of the LLC’s “powers, privileges or existence[,]” upon motion of the Delaware Attorney General. 6 *Del. C.* § 18-112(a). The Court of Chancery may also appoint trustees or receivers to wind up the affairs of such an LLC and make other orders respecting its assets, members, and creditors. 6 *Del. C.* § 18-112(b).

The fee for filing a corrected certificate with the Delaware Secretary of State has been changed. When any certificate filed with the Secretary of State under the DLLCA or DRULPA is to be corrected, one may make the correction by filing either a certificate of correction or a corrected version of the erroneous filing. Formerly, the fee for filing a corrected version was the same as the fee for whatever type of filing was being corrected, while the fee for filing a certificate of

correction was \$180 regardless of the type of filing being corrected. Pursuant to the amendment, the fee for a corrected version is now the same as the fee for a certificate of correction. 6 *Del. C.* § 18-211(b) (LLCs); 6 *Del. C.* § 17-213(b) (LPs).

* Continuing the analogy, limited liability partnerships, a subset of general partnerships, are *formed* without the need for any filing with a secretary of state or similar public office, but acquire limited liability features only by way of such a filing. Limited liability partnerships are therefore not registered organizations—their filings are prerequisites not to existence, but rather to the attribute of limited liability. See PERMANENT EDITORIAL BD. FOR THE UNIF. COMMERCIAL CODE, PEB COMMENTARY NO. 17: LIMITED LIABILITY PARTNERSHIPS UNDER THE CHOICE OF LAW RULES OF ARTICLE 9 (June 29, 2012).

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Proposed Amendments to the Delaware LLC Act to Be Effective August 1, 2019

By Eugene A. DiPrinzio

A subcommittee of the Delaware State Bar Association (the “DSBA”) has drafted and proposed for possible consideration and enactment by the Delaware State Legislature, to be effective August 1, 2019, a number of technical amendments to the Delaware LLC Act that are intended to be complementary to the amendments discussed in the preceding article and assist in the implementation of the series amendments adopted in 2018 that will take effect August 1, 2019. The technical amendments as submitted to the DSBA can be summarized, in part, as follows:

- a. Definitional changes to the terms “electronic transmission” and “document” that are intended to establish non-exclusive safe harbor methods when used with electronic transactions consistent with the Delaware Uniform Electronic Transactions Act, The Model Business Corporation Act, and The Electronic Signatures in Global and National Commerce Act.
- b. Requisite ability to distinguish the name of a limited liability company from those of any registered series of a limited partnership formed under other provisions of Delaware law.
- c. Confirmation that a registered agent may resign without appointing a successor registered agent.
- d. Clarification that the Certificate of Formation or Certificate of Registered Series, as applicable, may be amended by filing other documents.
- e. A plan of division may now provide for a contractual appraisal right, and those appraisal rights may be made available in connection with any merger or consolidation in which a registered series is a constituent party along with any division of an LLC.
- f. The allowance of new members to be admitted to a division company at the time of division or merger and technical changes with respect to the use of protected or registered series that may be converted one to another.
- g. Notice that additional fees will be required to be paid to the Delaware Secretary of State for certified documents and clarification as to a protected series or registered series in that one would not be liable for the debts, obligations or liabilities of another solely by reason of a failure to pay annual taxes or one series ceasing to be in good standing.