



Key Similarities and Changes Between ULLCA (2006)(Harmonized 2013) and the Rhode Island Limited Liability Company Act

The Uniform Limited Liability Company Act (ULLCA) and Rhode Island's Limited Liability Company Act are similar in most fundamental concepts and overall statutory architecture. However, the acts differ in regard to governance duties, the agency power of members, definitions of membership, allocation of distributions, finances, and creditor's rights. Enacting H 8116 would clarify Rhode Island's current limited liability company law and fill gaps that have been identified in practice and through litigation. Adopting ULLCA would also facilitate transactional planning by attorneys and businesses and provide much more explicit direction for courts in interpreting and applying limited liability company operating agreements.

Operating Agreement

ULLCA centralizes key provisions regarding the operating agreement and specifically states the operating agreement's relationship to the statutory rules. Sections 7-16.1-105 to 7-16.1-107¹ of H 8116 contain three key provisions dealing with the operating agreement concerning: the scope, functions, and limitations of the operating agreement; the effect of the operating agreement on the LLC and its members; and the effect of the key provisions of the operating agreement on third parties and its relationship to records. Rhode Island's current LLC law scatters provisions relating to the operating agreement throughout the statute. ULLCA specifies that default rules in the act will govern matters not addressed by the operating agreement whereas Rhode Island's current statute does not contain any specific language regarding an operating agreement's relationship to the statutory default rules. § 7-16.1-105(b). Rhode Island's current law also requires an affirmative vote of members entitled to vote, representing a majority of the capital values of all membership interests that have not been assigned, to amend the operating agreement. § 7-16-21. ULLCA requires the unanimous consent of members to amend the operating agreement for a member-managed LLC and a member-managed LLC. § 7-16.1-407(b)(4)(B) and 407(c)(3)(B).

ULLCA provides that the operating agreement may permit non-members, like lenders or non-member managers, to have veto rights over amendments to the operating agreement. § 7-16.1-107(a). It also provides that dissociated member and transferee rights are subject to changes in the operating agreement that occur after the transfer, provided the changes do not impose a new liability on the dissociated member or transferee. § 107(b). Under ULLCA, an LLC is bound by the operating agreement even if it has not manifested assent to the operating agreement. § 106(a). Rhode Island's current LLC law is silent on these matters.

Finally, both statutes expressly authorize sole member LLCs in the operating agreements and permit oral or written operating agreements. § 7-16.1-102(13) and 7-16-2(23).

¹ Rhode Island's Current LLC law is codified at §§ 7-16-1 to 7-16-76. H 8116 would add a new chapter 16.1 to Title 7 and the citations reflect the addition as proposed by the new language. For example, § 7-16.1-103(13) reflects the definition of "operating agreement" as contained in H 8116, whereas § 7-16-23 is that same definition in the current law.

Governance Structure

As far as the governance structure and consent requirements for voting are concerned, ULLCA and Rhode Island's LLC law are similar. Both contain management "templates." Section 407 of H 8116 provides default rules for two types of management structure: member-managed and manager-managed. § 7-16.1-407. Current Rhode Island law also provides that, unless the articles of organization or a written operating agreement provide for management by or under the authority of managers, the LLC shall be managed by the members. § 7-16-14. Both Acts specify that default rules are subject to the operating agreement. § 7-16.1-407(b) – (c) and § 7-16-15.

Under ULLCA, default rules for voting are listed in Section 407. A majority consent of members or managers is required for undertaking matters within the ordinary course of business; however, unanimous consent of members is required for undertaking matters outside ordinary course of business and to amend the operating agreement. §§ 7-16.1-407(b)(3)-(4), 407(c)(1),(3). Rhode Island's current law also requires unanimous consent of members to terminate a member's obligation to make a capital contribution, interim distribution, and grant membership status to an assignee of an interest in the LLC. §§ 7-16-25(d), 28, and 36.

Governance Duties

Current Rhode Island Law and ULLCA differ in regard to governance duties. Under ULLCA, members in a member-managed LLC and managers in a manager-managed LLC owe to LLC and the members a duty of care to refrain from grossly negligent or reckless conduct, intentional misconduct, and knowing violation of law. § 7-16.1-409(c), (i)(1). Under Rhode Island's current law, the manager must act "with the care that an ordinarily prudent person in a similar position would use under the circumstances, and in the manner the manager reasonably believes to be in the best interests of the limited liability company." §§ 7-16-17(a) to 7-16-18(b)(2). ULLCA does not permit an LLC to eliminate the contractual duty of good faith and fair dealing of members. Rhode Island does not have a limitation for the personal liability for a member or manager whose acts or omissions are not in good faith, or which involve intentional misconduct or a knowing violation of the law. §§ 7-16.1-409(d), (i)(3), §7-16-17. ULLCA permits an operating agreement to limit or eliminate aspects of the duties of loyalty, care, and good faith and fair dealing "if not manifestly unreasonable." § 7-16.1-105(c)(6), (d)(3). It also gives an operating agreement the power to limit or eliminate liability for breach of fiduciary duties except for conduct involving bad faith, willful or intentional misconduct, or a knowing violation of law. § 7-16.1-105(c)(7). Rhode Island's LLC law allows the articles of organization or operating agreement to eliminate or limit the personal liability of a manager to the LLC or its members for monetary damages for breach of any duty, but the organizational documents *cannot* eliminate or limit liability for: breach of manager's duty of loyalty; acts or omissions not in good faith; wrongful distributions; and transactions from which the manager received an improper benefit. § 7-16-18.

Agency Power of Members

Rhode Island's LLC law and ULLA also differ in sections regarding the agency power of members. Section 301 of H 8116 specifies that a member is not an agent of the LLC solely by

being a member and the authority of a member or managers to bind an LLC is determined by other law (particularly agency law). § 7-16.1-301. Current statute in Rhode Island uses a statutory apparent authority scheme and does not contain specific provisions relating to a statement of authority or statement of denial. § 7-16-20.

Membership

ULLCA differs from current law in its definition of member. Subsection 11 of Section 102 defines member as, “a person who has become a member of the LLC or was a member when the company became subject to the act and has not dissociated.” § 7-16.1-201(11). Rhode Island currently defines member as, “a person with an ownership interest in a limited liability company with the rights and obligations specified under this chapter.” 7-16-2(20). However, as mentioned above, both permit a limited liability company to have only one member upon formation and members must unanimously consent to granting assignee membership status. § 7-16.1-401, §§ 7-16-5, 36.

Finances

The laws differ in their provisions concerning the allocation of distributions, and express provisions for capital accounts and profits and loss allocations. Both contain similar provisions for limitations on distributions, liability for contributions, liability for improper distributions, and the right to transfer a member’s financial interest. The current default rule in Rhode Island is that distributions and losses are allocated to each member based on the member’s capital value. § 7-16-26 - 27. ULLCA’s default rule is that distributions before dissolution must be in equal shares among members and dissociated members, except to comply with transferee obligations and charging orders. § 7-16.1-404. ULLCA follows both RUPA (1997) (Last Amended 2013) and ULPA (2001) (Last Amended 2013), which Rhode Island enacted last session, by omitting the default rule for allocation of losses. Under ULLCA, distribution rules are sufficient to determine tax allocation of losses.

Both laws provide that distributions will not be allowed if the company would be unable to pay its debts or if the total assets would be less than the total liabilities and any additional amount needed to satisfy preferential rights. § 405, § 7-16-31. Liability for contributions is not excused for death, disability, or other inability to perform. § 7-16.1-403 and § 7-16-25. ULLCA does not change the limitations on distributions that are in current Rhode Island Law: (1) not able to pay the debts as they become due in the ordinary course of business; or (2) total assets less than total liabilities). § 7-16.1-405. Members and managers who consent to an improper distribution may still be personally liable and liability still exists to return the excess distributions by recipients who knew the distribution was improper. § 7-16.1-406. Finally, both laws have similar language reflecting the right of a member to transfer their financial interest in the LLC and protect the “pick-your-partner” principle. § 7-16.1-502 and § 7-16-35.

Dissociation and Dissolution

ULLCA expands on the sections of current Rhode Island law dealing with dissociation and its effects. Rhode Island’s current LLC act does not have specific provisions about dissociation and the effect of this dissociation. Under ULLCA, the default rule gives a member the power to

dissociate; but if the dissociation is wrongful, the member is liable for damages and is still liable for any unpaid contributions or other debts owed to the LLC. § 7-16.1-601. Section § 602 sets forth the causes of disassociation. Once a member has dissociated, the member's right to participate in the management and conduct of the business terminates. § 603. The former member is a mere transferee and has only the right to receive distributions. *Id.* The dissociation does not trigger any distributions; but the former member does receive a proportionate share of future distributions. *Id.*

Both laws provide for dissolution of an LLC. Sections 39 to 45 of the current Rhode Island law list the causes of dissolution, permit judicial dissolution, address winding up, and authorize administrative dissolution by the Secretary of State. § 7-16-39 – 45. However, ULLCA allows for a right of reinstatement within one year if the deficiencies are cured and the current Rhode Island act allows for a right of reinstatement within 10 years if deficiencies are cured. § 7-16.1-709 and § 7-16-43. Current law is also silent as to a court-ordered dissociation of a member. Though both laws address court-ordered dissolution, ULLCA's provisions are more expansive. *Compare* § 7-16.1-701(4) *with* § 7-16-40. Lastly, ULLCA expressly authorizes both direct and derivative lawsuits where the Rhode Island statute contains no express authorization for direct lawsuits. § 7-16.1-801, 7-16-56.

Creditors Rights Against Members and Charging Orders

ULLCA expressly states that charging orders are the exclusive remedy for a judgment creditor of a member or transferee to obtain a member or transferee's financial rights to distributions in subsection h of section 503. This section also makes it clear that a secured creditor will retain all remedies available under Article 9 of the Uniform Commercial Code. While Rhode Island's current act does permit charging orders for judgment creditors of members, it does not contain specific sections on if charging orders are the exclusive remedy, if foreclosure sales are authorized, the effect of a foreclosure sale, and any redemption rights available to a member or LLC.

Reorganization (Domestication, Merger, Interest Exchange, Conversion)

ULLCA offers more extensive provisions concerning reorganization transactions than current Rhode Island law. Section 7-16-59 of current law provides that domestic or foreign LLC may merge or consolidate with or into one or more domestic or foreign LLCs, LPs, or corporations. It also permits one or more LPs or corporations to merge/consolidate with or into any domestic or foreign LLCs. *Id.* Rhode Island only requires a majority vote, not unanimous consent like ULLCA, to approve a reorganization. § 7-16-21(b), § 7-16.1-407(b)(4)(A), (c)(3)(A). Finally, though ULLCA does not contain an express provision concerning appraisal rights, Section 1007 preserves appraisal rights authorized by other law for other entities that are parties to transaction and also authorizes enforcement of contractual appraisal rights in an LLC's operating agreement or the plan of merger, domestication, conversion, or interest exchange.