

## Series Limited Liability Company the Newest Corporate Entity<sup>1</sup>

A real estate investor, who has multiple rental properties and wants to shield personal assets, generally forms individual entities for each of the properties or constructs a holding company to shield liability. However, a minority of states have enacted a new statutory limited liability company known as a series limited liability company<sup>2</sup>. The Series LLC is a statutory creature whereby the limited liability company is separated into different compartments of assets or “series”, with each series having the ability to have its own members and liabilities that may or may not be the same as other “series” within the Series LLC. Under a series limited liability company each series operates as separate entity with individual names, bank accounts and most importantly liability, whereby, all the assets in one series of a Series LLC are protected from the risks of another series within the same Series LLC. As each state has different filing requirements, Series LLCs are complicated when determining the filing and registration requirements. However, it may be worthwhile to consider Series LLC as you only have to file articles of formation once, making Series LLCs a perfect solution for landlords and real estate investors with multiple rental properties.

The advantages of the Series LLC include reduced startup and administrative costs (typically would have one filing); the incorporator does not have to organize a new limited liability company each time a new investment is organized; one registered agent fee; segregation of assets for liability purposes; and, ability to raise capital at the series level.

The disadvantages of the Series LLC would be the untested nature of the entity (will the court respect the segregation of assets); different state treatment of Series LLC for tax purposes; difficulty in obtaining Federal EIN numbers and bank accounts by series; and, the entity’s unfamiliarity with attorneys, accountants, title companies and lenders.

As Maryland’s Limited Liability Company Act<sup>3</sup> does not contain a Series LLC provision there are questions regarding how the Courts will react to litigation regarding Series LLC. There is no guidance at present whether, for example, the Court will shield the assets of the other series from creditors executing on a judgment against a series within the Series LLC. Another possible matter that could result in litigation would be litigation between members of a series within a Series LLC. One may argue that the

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<sup>2</sup> Alabama, Delaware Del. Code Ann. Titl. 6 Section 18-201 et seq., District of Columbia (District of Columbia provides a Series LLC is treated as separate legal entity), Illinois 805 Ill. Comp. Stat. Anna Section 180/37-40; Iowa Iowa Code Section 490A.305; Kansas; Missouri; Montana; Nevada Nev. Rev. Stat. Ann. Section 86.296; Oklahoma Okla. Stat. titl. 18 Section 2054.4; Tennessee, Tenn. Code Ann. Section 48-249-309; Texas, Tex. Bus. Orgs, Code 101.601; Utah, Utah Code Ann Section 48-2c-606 . It is worth noting that the Revised Uniform Limited Liability Company Act (RULLCA) has not included any provision related to Series LLC in RULLCA.

<sup>3</sup> Md. Code Ann. Corp. & Assn's Section 4A-101 et seq.

organization and formation documents as well as the state of formation of the Series LLC will control the application of law regarding any issues of law. This rationale may work well in matters involving issues between the entity itself and officers, directors and/or members but may not work well when the controversy is between the entity itself and others outside the entity, such as creditors. There is also an alternative view that the law in which the Series LLC is subject to judicial proceedings will control, if there no recognition of the Series LLC entity in that particular jurisdiction.

However, by way of contrast, the Delaware Limited Liability Company Act allows a limited liability company to organize one or more series within a LLC, each series with different members, and with different assets, business purposes and/or investment objectives. The statute further states that the debts, liabilities and expenses of a specific series is only enforceable against that particular series within the Series LLC and does not transfer or otherwise permit collection against other series within the Series LLC.

Of course, when dealing with a new type of entity there will be concern and questions from different entities with business relationships with the series, including the series' lender. For example, failure to properly form your Series LLC and/or publicize your Series LLC may result in not having your loan funded by a financial institution. For example, arguably only Illinois, Kansas and Missouri require the filing of a public record to form a series within the Series LLC<sup>4</sup> and that the series legal existence begins with the filing of the certificate of designation or the articles of organization. Montana requires that the operating agreement for each series within the Series LLC must be filed with the state<sup>5</sup>. As noted, Series LLCs registered in states other than Illinois, Kansas and Missouri are not "registered organizations" as used under Article 9<sup>6</sup>.

The new entity may also cause lender concerns under Article 9 of the Uniform Commercial Code as to whether a series within a Series LLC can be a "debtor" under Article 9<sup>7</sup>. For example under the Delaware LLC Act the assets can be held under the name of the series, the Series LLC, a nominee or otherwise<sup>8</sup>. Some states, that have enacted series limited liability company statutory language, provide that the series must be treated as a separate legal entity provided said series is set forth in the articles of organization of the master limited liability company<sup>9</sup>. However, on a positive note, those states that have recognized the Series LLC have expressly given the Series LLC the authority to contract with others and authority to sue and be sued in the series own name<sup>10</sup>.

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<sup>4</sup> 805 Ill. Comp. Stat 190/37-40(d); Kan. Stat. Ann Section 17-76, 143(d); Mo. Ann. Stat. Section 347.186(4).

<sup>5</sup> Mont. Code Ann. Section 35-8-202.

<sup>6</sup> U.C.C. Section 9-102(a) (71).

<sup>7</sup> See UCC Section 1-201(b) (25) definition of organization; UCC Section 1-201(b) (27) definition of a person.

<sup>8</sup> Del. Code Ann. Tit. 6, Section 18-215.

<sup>9</sup> Ind. Code Section 23-18.1-4-4(a); 805 Ill. Comp. Stat. Ann 180/37-40(b); Iowa Code Ann. Section 489.1201(7); Kan. Stat. Ann. Section 17-76.143(b); Mo. Ann. Stat. Section 347.186.2(4); and U.C.A. 1953 Section 48-3a-1201(6).

<sup>10</sup> Del. Code Ann. tit. 6, Section 18-215(c); D.C. Code Section 29-802.06; 805 Ill. Comp. Stat 190/37-40(b); Ind. Code Ann. Section 23-18.1-4-4(a); Kan. Stat. Ann Section 17-76, 143(b); Mo. Ann. Stat. Section 347.186.2(4); Tex. Bus & Comm. Code Section 101.605(1); Utah Code Ann. Section 48-3a-1201(3)(b).

Similar to how the Series LLC will be treated under the Commercial Code; there is also concern about how the Series LLC will be treated under the Bankruptcy Code. Under the Bankruptcy Code any “person” may file for bankruptcy relief<sup>11</sup>. A person under the Bankruptcy Code has been defined as an individual, partnership or corporation<sup>12</sup>; however it does not include a trust or estate, with the exception of a business trust<sup>13</sup>. LLCs were considered a “person” as the LLC had characteristics of a partnership and a corporation, wherefore the LLC was similar enough to these entities to be considered a “person” for the purposes of filing<sup>14</sup>. Although unclear what the Bankruptcy Court will do when presented with determining whether a Series LLC can file for bankruptcy relief there is a belief that the Bankruptcy Courts in the states that have Series LLC statutes will recognize same<sup>15</sup>.

Despite best efforts to address all possible issues, the states that enacted the Series LLC statutes have still left some issues unanswered that will certainly cause issues moving forward. For example, what happens when: a Series LLC merges into a corporation or a LLC; or, will the assets of a series within a Series LLC be accounted for inside the bankruptcy case of another series inside the same Series LLC; or, if a series is liquidated and dissolved how will the Series LLC treat and handle the claims and assets of the members of the series. Certainly if more states enact Series LLC statutes, or a uniform law is proposed by the National Conference of Commissions on Uniform State Laws, and/or there is the passage of a Limited Liability Company Protected Series Act, some of these issues, as well as others, will be addressed. However, it appears the greatest concern, at present, to business owners and their counsel is how the non-Series LLC states will handle and address the internal liability shield between the individual series, and, in worst case scenarios, what may be the reception of Series LLCs to bankruptcy courts. Third parties’ concern focus on how the U.C.C. will handle these entities and whether title insurance will be available for Series LLCs. Similar to the acceptance of the limited liability companies, there are certainly uses for the Series LLC, which has been recognized by an increasing number of businesses and individuals, whereby all should become familiar with its structure and uses.

Although untested in Maryland, the Series LLC can provide a useful and cost effective tool in effectively separating, organizing and allocating assets and projects within one entity. Each series within a Series LLC has its own separate rights, powers, assets, obligations, business purpose and associates members.

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<sup>11</sup> 11 USC Section 109(a).

<sup>12</sup> 11 USC Section 101(41)

<sup>13</sup> 11 USC Section 101(15)

<sup>14</sup> In re ICLNDS Notes Acquisition LLC, 259 BR 289 (Bankr. N.D. Ohio 2001).

<sup>15</sup> The United States Bankruptcy Court for the Eastern District of Massachusetts (Boston) accepted the filings of Crust Real Estate Series, LLC 917 East Broadway Series, Sole Beneficiary of 917 East Broadway Realty Trust, Case No. 15-12105, Crush Real Estate Series LLC Sole Beneficiary of 427 East Sixty Street Realty Trust, Case No. 15-10237, and Crush Real Estate Series LLC Sole Beneficiary of 427 K Street Realty Trust, Case No. 15-12106. The filings were subsequently dismissed by the Debtor for other reasons without the Court reaching the decision regarding whether the Series LLC is a “person” under the Bankruptcy Code.