



LIABILITY



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The Case for Creditor Protections in Nevada's Series LLC Laws

BY JONATHAN JOEL TEW, ESQ.

Series LLCs can generate consternation and concern among legal and other business-planning professionals. Such a response is reasonable. Series LLCs are in their legal infancy; only about one-third of states have adopted series LLC legislation. Further, series LLCs may present significant operational dangers that standard limited liability companies do not. At this time, it is unclear whether individual series within a company will retain their limited liability in non-series LLC states or in bankruptcy.

Nevertheless, series LLCs are picking up steam. Just last year, the National Conference of Commissioners on Uniform State Laws approved and recommended the enactment of the Uniform Protected Series Act (Uniform Series Act). The prefatory note and comments to the Uniform Series Act make a strong case for the growing popularity of series LLCs – as indicated through filing data and other evidence – and the act's approval may further advance series LLC legislation in non-series LLC states. So why does this matter to Nevada?

The Uniform Series Act was a major undertaking and offers an incredibly comprehensive approach to series LLCs. While a full analysis of the act and how it compares to Nevada's current statute is impossible within the confines of this article, a strong argument can be made that Nevada's series LLC statutes could benefit by adding additional creditor protections like those within the Uniform Series Act. Specifically, Nevada should consider amending NRS Chapter 86 to detail:

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1. How series assets must be accounted for, and
2. When a judgment against a series LLC or series may be enforced against an asset of another series by virtue of deficient accounting or recordkeeping procedures.

Adding such clarity and protection would help Nevada remain competitive in the field of series LLCs by promoting best-practices, reducing uncertainty regarding series operations and discouraging potential misuse of series LLCs. In turn, these benefits should lead to greater investment in Nevada.

Series LLCs in Nevada

Most readers are likely familiar with series LLCs. However, as a brief refresher, series LLCs are a specific type of limited liability company that allow for the segregation of different business operations, assets or interests into independent series within the LLC, each of which is theoretically protected from liability from other series or the series LLC itself.

Nevada adopted series LLC legislation in 2005, becoming one of the first few of states to do so. Until 2017, NRS Chapter 86 provided relatively limited provisions on series LLCs, especially with respect to their formation, operational abilities and limited liability. NRS 86.1255 defined series as a "series of members' interests" having separate rights, powers and duties with respect to property or obligations, or profits and losses associated with property or obligations. NRS 86.296(2) authorized their creation through the articles of organization or operating agreement of the limited liability company. And, NRS 86.296(3) provided how each series could maintain its limited liability by, among other things:

1. Maintaining separate and distinct records for each series, and

2. Holding and accounting for series assets separately from other company and series assets.

Notably, NRS 86.296(3) did not provide much in the way of detail regarding how series assets should be accounted for under the statute.

2017 Amendments

In March 2017, the Assembly Committee on Judiciary met to discuss Assembly Bill (AB) 123, which sought to clarify the power of a series created within a limited liability company. During that process, several legislators expressed concern over potential misuse of series LLCs. In its final, adopted version, AB 123 not only added additional provisions to clarify the scope of a series' operational abilities under NRS Chapter 86, such as the ability to contract, sue and be sued, and hold and dispose of real property, it also added a few provisions to help curb misuse of series LLCs. For example, NRS 86.236 now makes clear that a series is served by serving the registered agent of the umbrella LLC. Additionally, any series that does not include the name of its umbrella LLC is deemed to be doing business under a fictitious business name and is required to register under NRS 602.010. *See* NRS 602.010(3). Thus, AB 123 did add *some* transparency to series and clarity to the service of process.

What AB 123 did not do was add any meaningful detail as to how a series should separately hold and account for its assets and interests to ensure that it maintains its limited liability features. AB 123 inserted

default rules into NRS 86.311, specifying what documentary authorization is needed to bind a series in property transactions. For example, NRS 86.311(2) requires that any transactional document be signed by a manager of a series (if the series is

overseen by managers), a member associated with the series (if the series is managed by members) or (3) a properly authorized agent to be effective. However, NRS 86.311(2) allows a series to change these requirements through its operating agreement.

What the Uniform Series Act Can Tell Us

The Uniform Series Act supports greater creditor protections. One

reason for this is simple; if series LLCs are more accountable and less prone to abuse, the limited liability of individual series is more likely to withstand scrutiny in non-series LLC states and in bankruptcy. At present, there is essentially no meaningful case law from which one can evaluate whether series LLCs will be recognized in non-series LLC states. Additionally, no one knows how series will be treated in bankruptcy. For example, if a series LLC has two series and one series files for bankruptcy, will the other series be pulled into the bankruptcy? How about the umbrella or master LLC? Greater operational predictability and creditor protections will likely help fulfil the promise of series limited liability.

For this reason, Nevada should evaluate and consider adopting certain Uniform Series Act provisions (or the act itself). At a minimum, the Legislature should consider amending NRS Chapter

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86 to add provisions similar to those contained in Sections 301 and 404 of the act. Under the act, only associated assets of a series may be protected from creditor claims against other series or the umbrella LLC. To associate an asset, series records must name the series and describe the asset with sufficient specificity so that a disinterested, reasonable individual can:

1. Identify the asset and distinguish it from other assets of the series, the company and the other protected series of the company;
2. Determine when and from what person the series acquired the asset (or how the asset became an asset of the series); and
3. If the series acquired the asset from another series of the company or the company, determine the consideration paid, the payor and the payee.

If an asset of a particular series is not associated, then any creditor holding

a judgment against the umbrella LLC or another series may seek to enforce that judgment against the non-associated asset under Section 404. Section 404 also authorizes the prejudgment remedy of attachment against non-associated assets, if a creditor has not reduced its claim to judgment and the law of the state (other than the series LLC statute) authorizes such a remedy.

The Uniform Series Act's framework of associating individual assets, *on an asset-by-asset basis*, and allowing for easier access to assets if a series is improperly managed, will likely result in greater operational efficiency, creditor protection and investment. Accordingly, Nevada should consider adding more clear and robust recordkeeping requirements and specific remedies into NRS Chapter 86.

Conclusion

A consistent theme in the legislative history of AB 123 is the goal for Nevada to be competitive. At the same time, that

legislative history demonstrated concern regarding potential misuse of series LLCs. These two noble ends need not be mutually exclusive, as more robust creditor protections and predictability are likely to result in better business practices and more investment in Nevada. Since other states will adopt the Uniform Series Act (Nebraska already has), Nevada should take steps to be at the forefront of series LLC legislation and to be a model for other states. **NL**



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