



Tax and Accounting Center

Estates, Gifts and Trusts Journal
2010
09/09/2010
ARTICLES

35 *Estates, Gifts and Trusts Journal* 233

***Olmstead*: Right Result, Wrong Reason**

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INTRODUCTION

Florida's Supreme Court held in *Olmstead v. Federal Trade Commission*¹ that a court may order a judgment debtor to surrender all right, title and interest in the debtor's single-member limited liability company ("LLC"), organized under Florida law, to satisfy an outstanding judgment. The Florida Supreme Court said: "[s]pecifically, we conclude that there is no reasonable basis for inferring that the provision authorizing the use of charging orders under section 608.433 (4) establishes the sole remedy for a judgment creditor against a judgment debtor's interest in single-member LLC."²

¹ 2010 Fla. LEXIS 990, 35 Fla. L. Weekly S 357 (Fla. June 24, 2010).

² *Id.* at *17-18.

This article summarizes the majority and minority opinions in *Olmstead* and explains why multimember LLCs may also be vulnerable to attack. To assist the reader and limit confusion, an explanation of basic terms such as charging order and exclusive remedy is provided. Since Florida's next legislative session will begin in March 2011 (assuming no special session is called), even if legislation is enacted in 2011, by the time the governor signs it into law the effective date would probably be July 1, 2011, or later. It is possible that any new law will be applied retroactively, but due to uncertainty as to whether or when legislation will be enacted, members of Florida LLCs may want to take action now as described below. Earlier attempts by several Florida Bar committees over recent years to provide exclusive remedy protection for LLCs have met opposition and never reached the Florida Legislature. Any state that has disparity in its creditor remedies for LLCs and partnerships could face similar challenges; the so-called "warning bell" has sounded to consider whether exclusive remedy and foreclosure restrictions should be uniform. This article suggests new legislation that would make charging orders the exclusive remedy for LLCs and prohibit other remedies such as foreclosure. Many states such as Delaware do not differentiate between charging order protection for single-member and multimember LLCs.³ Among the alternatives, the Florida Legislature could provide charging order protection to: (i) single-member LLCs as well as multimember LLCs (as provided under Wyoming law);⁴ (ii) all LLCs, without specific reference to single-member or multimember LLCs (as provided under Delaware law);⁵ or (iii) only multimember LLCs (to conform Florida statutes to the *Olmstead* decision). Based upon the uncertainty resulting from *Olmstead*, legislative clarification is necessary as soon as possible.

³ 6 Del. C. §18-703:

(a) On application by a judgment creditor of a member or of a member's assignee, a court having jurisdiction may charge the limited liability company interest of the judgment debtor to satisfy the judgment. To the extent so charged, the judgment creditor has only the right to receive any distribution or distributions to which the judgment debtor would otherwise have been entitled in respect of such limited liability company interest.

(b) A charging order constitutes a lien on the judgment debtor's limited liability company interest.

(c) This chapter does not deprive a member or member's assignee of a right under exemption laws with respect to the judgment debtor's limited liability company interest.

(d) The entry of a charging order is the exclusive remedy by which a judgment creditor of a member or of a member's assignee may satisfy a judgment out of the judgment debtor's limited liability company interest.

(e) No creditor of a member or of a member's assignee shall have any right to obtain possession of, or otherwise exercise legal or equitable remedies with respect to, the property of the limited liability company.

⁴ Wyo. Stat. §17-29-503(e) ("A limited liability company or one (1) or more members whose transferable interests are not subject to the charging order may pay to the judgment creditor the full amount due under the judgment and thereby succeed to the rights of the judgment creditor, including the charging order").

(g) This section provides the exclusive remedy by which a person seeking to enforce a judgment against a judgment debtor, including any judgment debtor who may be the sole member, dissociated member or transferee, may, in the capacity of the judgment creditor, satisfy the judgment from the judgment debtor's transferable interest or from the assets of the limited liability company. Other remedies, including foreclosure on the judgment debtor's limited liability interest and a court order for directions, accounts and inquiries that the judgment debtor might have made are not available to the judgment creditor attempting to satisfy a judgment out of the judgment debtor's interest in the limited liability company and may not be ordered by the court.

⁵ 6 Del. C. §18-703, above note 3.

OLMSTEAD COULD RENDER FLORIDA (AND POSSIBLY OTHER STATE) MULTIMEMBER LLCs VULNERABLE

That the Florida Supreme Court held that a single-member LLC was not provided charging order protection was not a surprise. The majority opinion referred to *In re Albright* ⁶ where a Colorado Bankruptcy Court rejected the argument that a bankruptcy trustee should be entitled to only a charging order with respect to a debtor's ownership of a single-member LLC. It held: "[b]ecause there are no other members in the LLC, the entire membership interest passed to the bankruptcy estate." ⁷

⁶ 291 B.R. 538 (D. Colo. 2003).

⁷ *Id.* at 540.

As discussed below, the Florida Supreme Court's reasoning in *Olmstead* could apply equally to multimember LLCs. The majority opinion states: "[o]n its face, the charging order provision establishes a *nonexclusive* remedial mechanism. There is no express provision in the statutory text providing that the charging order is the only remedy that can be utilized with respect to a judgment debtor's membership interest in an LLC." (Emphasis added.) ⁸

⁸ *Olmstead*, 2010 Fla. LEXIS 990, 35 Fla. L. Weekly S 357 at *13. (Emphasis added.)

Judge Lewis' dissenting opinion creates even greater concern for members of multimember Florida LLCs. Judge Lewis wrote:

[T]he principles used [by the majority] to ignore the LLC statutory language under the current factual circumstances apply with equal force to multimember LLC entities and, in essence, today's decision crushes a very important element for all LLCs in Florida. If the remedies available under the LLC Act do not apply here because the phrase "exclusive remedy" is not present, the same theories apply to multimember LLCs and render the assets of all LLCs vulnerable. ⁹

⁹ *Id.* at *20.

Judge Lewis continued:

By relying on an inapplicable statute [Florida's Revised Uniform Limited Partnership Act of 2005 and the Revised Uniform Partnership Act of 1995], the majority ignores the plain language of the LLC Act and the other restrictions of the statute, which universally apply the use of the charging order to judgment creditors of all LLCs, regardless of the composition of the membership. The majority opinion now eliminates the charging order remedy for multimember LLCs under its theory of "nonexclusivity" which is a disaster for those entities. ¹⁰

¹⁰ *Olmstead*, 2010 Fla. LEXIS 990, 35 Fla. L. Weekly S 357 at *36-37. The dissent may be overly alarming in concluding that *Olmstead's* majority opinion also eliminates the exclusive charging order protection for members of multimember LLCs. However, the fact that Judge Lewis so concluded in his minority opinion provides creditor attorneys reason to explore this possibility.

UNDERSTANDING ESSENTIAL TERMS

While this article is not intended to be a comprehensive analysis of charging orders, it is helpful to provide a general understanding of the essential terms that are the subject of the *Olmstead* case, such as what a charging order is, and how some states have specifically legislated to provide clarity within the law to avoid *Olmstead*-type litigation. Generally, "[a] charging order is a statutory procedure whereby a creditor of an individual member can satisfy its claim from the member's interest in the limited liability company as a protection of the other partners of the partnership or other members of the LLC." ¹¹ Both the Uniform Limited Partnership Act and the Revised Uniform Limited Liability Company Act, drafted by the National Conference of Commissioners on Uniform State Laws, provide for charging orders and specifically permit foreclosure. ¹² Judge Lewis' dissenting opinion provides the following historical summary of charging orders:

¹¹ *Black's Law Dictionary* 266 (9th ed. 2009).

¹² *See Rev. Unif. Ltd. Liab. Co. Act* §503(c) (2006)
Upon a showing that distributions under a charging order will not pay the judgment debt within a reasonable time, the court may foreclose the lien and order the sale of the transferable interest. The purchaser at the foreclosure sale obtains only the transferable interest, does not thereby become a member, and is subject to Section 502.

Unif. Ltd. P'ship Act §703(b) (2001)

A charging order constitutes a lien on the judgment debtor's transferable interest. The court may order a foreclosure upon the interest subject to the charging order at any time. The purchaser at the foreclosure sale has the rights of a transferee.

See also Fla. Stat. §620.1703, below note 14 (indicating Florida's approach to charging orders and limited partnerships); Fla. Stat. §608.433, below note 16 (indicating Florida's approach to charging orders and LLCs). In both cases Florida did not adopt the express authority for a foreclosure remedy as provided in the uniform laws.

The language of the charging order provision in the Revised Uniform Limited Partnership Act (1976), as amended in 1985, is virtually identical to that used in the Uniform Limited Liability Company Act, as well as in the Florida LLC Act.... The Uniform Limited Partnership Act of 2001 significantly changed this provision by explicitly allowing execution upon a judgment debtor's partnership interest.... However, the Florida Partnership [Revised Uniform Limited Partnership] Act provides that a charging order is the exclusive remedy for judgment creditors (stating the charging order provision provides the "exclusive remedy by which a judgment creditor of a partner or partner's transferee may satisfy a judgment out of the judgment debtor's interest in the limited partnership or transferable interest"). ¹³

¹³ *Olmstead*, 2010 Fla. LEXIS 990, 35 Fla. L. Weekly S 357 at *35-36.

The charging order discussion provided in *Olmstead* falls short in explaining the "disconnect" of Florida law on the treatment of charging orders under Florida's Revised Uniform Limited Partnership Act of 2005, ¹⁴ Florida's Revised Uniform Partnership Act of 1995, ¹⁵ and Florida's Limited Liability Company Act. ¹⁶

Section 620.1703 of Florida's Revised Uniform Limited Partnership Act of 2005 states that a charging order is the exclusive remedy by which a judgment creditor of a partner may satisfy a judgment and provides that other remedies, including (but not limited to) foreclosure on the partner's interest in the limited partnership, are not available and may not be ordered by a court.¹⁷ Florida Bar members with different areas of specialty worked on the drafting of the Florida Revised Uniform Limited Partnership Act of 2005. Based upon my review at that time of various state laws, I proposed that the drafting committee include the "exclusive remedy" and foreclosure prohibition provisions that were enacted. These provisions were based in significant part on the Alaska Uniform Limited Partnership Act.¹⁸ A Summary and Report submitted to describe the proposal to enact the Florida Revised Uniform Limited Partnership Act of 2005 stated:

¹⁴ Fla. Stat. §620.1703, subsection (1), for Florida Limited Partnerships, states:
On application to a court of competent jurisdiction by any judgment creditor of a partner or transferee, the court may charge the partnership interest of the partner or transferable interest of a transferee with payment of the unsatisfied amount of the judgment with interest. To the extent so charged, the judgment creditor has only the rights of a transferee of the partnership interest.

Subsection (3) states:

This section provides the exclusive remedy which a judgment creditor of a partner or transferee may use to satisfy a judgment out of the judgment debtor's interest in the limited partnership or transferable interest. Other remedies, including foreclosure on the partner's interest in the limited partnership or a transferee's transferable interest and a court order for directions, accounts, and inquiries that the debtor general or limited partner might have made, are not available to the judgment creditor attempting to satisfy the judgment out of the judgment debtor's interest in the limited partnership and may not be ordered by a court.

¹⁵ Fla. Stat. §620.8504 for Partnerships other than Limited Partnerships, states:
(1) Upon application by a judgment creditor of a partner or of a partner's transferee, a court having jurisdiction may charge the transferable interest of the judgment debtor to satisfy the judgment. The court may appoint a receiver of the share of the distributions due or to become due to the judgment debtor in respect of the partnership and make all other orders, directions, accounts, and inquiries the judgment debtor might have made or which the circumstances of the case may require.
(2) A charging order constitutes a lien on the judgment debtor's transferable interest in the partnership. The court may order a foreclosure of the interest subject to the charging order at any time. The purchaser at the foreclosure sale has the rights of a transferee.
(3) At any time before foreclosure, an interest charged may be redeemed:
(a) By the judgment debtor;
(b) With property other than partnership property, by one or more of the other partners; or
(c) With partnership property, by one or more of the other partners with the consent of all of the partners whose interests are not so charged.
(4) This act does not deprive a partner of a right under exemption laws with respect to the partner's interest in the partnership.
(5) This section provides the exclusive remedy by which a judgment creditor of a partner or partner's transferee may satisfy a judgment out of the judgment debtor's transferable interest in the partnership.

¹⁶ Fla. Stat. §608.433, subsection (4), for Limited Liability Companies, states:
On application to a court of competent jurisdiction by any judgment creditor of a member, the court may charge the limited liability company membership interest of the member with payment of the unsatisfied amount of the judgment with interest. To the extent so charged, the judgment creditor has only the rights of an assignee of such interest. This chapter does not deprive any member of the benefit of any exemption laws applicable to the member's interest.

¹⁷ Fla. Stat. §620.1703(3), above note 14.

¹⁸ Alaska Stat. §32.11.340(b)
This section provides the exclusive remedy that a judgment creditor of a general or limited partner or of the general or limited partner's assignee may use to satisfy a

judgment out of the judgment debtor's interest in the partnership. Other remedies, including foreclosure on the general or limited partner's partnership interest and a court order for directions, accounts, and inquiries that the debtor general or limited partner might have made, are not available to the judgment creditor attempting to satisfy the judgment out of the judgment debtor's interest in the limited partnership and may not be ordered by a court.

See also Alaska Stat. §10.50.380 (dealing with LLCs)

(c) This section provides the exclusive remedy that a judgment creditor of a member or a member's assignee may use to satisfy a judgment out of the judgment debtor's interest in the limited liability company. Other remedies, including foreclosure on the member's limited liability company interest and a court order for directions, accounts, and inquiries that the debtor member might have made, are not available to the judgment creditor attempting to satisfy a judgment out of the judgment debtor's interest in the limited liability company and may not be ordered by a court.

Drafting Committee changed the uniform act provisions to further clarify the rights of judgment creditors and to emphasize that the charging lien is the exclusive remedy by which a judgment creditor of a partner may satisfy a judgment out of the judgment debtor's interest in the partnership; the supplemental language also clarifies that other remedies (including but not limited to foreclosure on the partner's interest) are not available and may not be ordered by a court. ¹⁹

¹⁹ *Summary and Report: Florida Revised Uniform Limited Partnership Act (2005) and Amendments to Other Florida Business Entity Statutes 8* (Fla. 2005), http://www.floridatlawyers.org/pdf/Summary_report_Bill595.pdf.

The exclusive remedy and foreclosure prohibition language described above was included in the Florida Revised Uniform Limited Partnership Act of 2005 affirming existing Florida case law, holding that a creditor of a partner could only pursue a charging order against that partner's interest in the partnership and could not pursue foreclosure against such interest. ²⁰

²⁰ *In re Stocks*, 110 B.R. 65 (Bankr. N.D. Fla. 1989); *Givens v. National Loan Investors L.P.*, 724 So. 2d 610 (Fla. 5th DCA 1998).

It should be noted that the Florida Revised Uniform Limited Partnership Act of 2005 and the Alaska Uniform Limited Partnership Act both state that the charging order provides the "exclusive remedy" of a judgment creditor. ²¹ Florida's Act states "which a judgment creditor of a partner... may use to satisfy a judgment out of the judgment debtor's interest in a limited partnership." ²² The Alaska Uniform Limited Partnership Act is almost identical to the Florida Act but Alaska's states "that a judgment creditor of a *general or a limited partner*... may use to satisfy a judgment..." ²³ Both the Alaska and Florida Acts state that the charging order provides the exclusive remedy which a judgment creditor of a partner (both general and limited partners) may use to satisfy a judgment out of the judgment debtor's interest in a limited partnership. Florida's Act uses the word "partner" while Alaska's refers to a general or limited partner. The Florida Act does not reference specifically to a general or limited partner because partner is defined in §620.1102 (13) as a limited or general partner. ²⁴

²¹ Alaska Stat. §32.11.340(b), above note 18; Fla. Stat. §620.1703, above note 14.

²² Fla. Stat. §620.1703, above note 14.

²³ Alaska Stat. §32.11.340(b), above note 18 (emphasis added).

²⁴ Fla. Stat. §620.1102(13).

Where an individual serves as general partner of a Florida limited partnership, such individual's creditors would be limited to a charging order against his or her general partnership interest. However, if the general partner of a Florida limited partnership is a single-member LLC owned by an individual debtor, then the debtor would not be protected by §620.1703(3) as that section only provides the exclusive

remedy protection to a judgment creditor of a partner.²⁵ Where the general partner of a limited partnership is an LLC, the creditors of the LLC members are not creditors of the partnership. As such, the LLC member's creditors would be subject to the charging order provisions of §608.433 of Florida's Limited Liability Company Act. Based upon *Olmstead*, no charging order protection is available to the sole member of an LLC. Accordingly, under *Olmstead*, an individual general partner of a Florida limited partnership who has creditors is protected under §620.1703(3), whereas an LLC general partner of a Florida limited partnership whose sole member may be an individual who has creditors, would not be protected by §620.1703.²⁶

²⁵ Fla. Stat. §620.1703, above note 14.

²⁶ It should be noted that if the individual general partner becomes a debtor in bankruptcy or executes an assignment for the benefit of creditors, the general partner would be dissociated from the limited partnership as a general partner. See Fla. Stat. §620.1603(6). In such event if there is no other general partner, all of the limited partners may consent to continue the partnership and admit at least one general partner. However, if the individual general partner is also a limited partner, the requirement to obtain the consent of "all" the limited partners is unlikely to be satisfied. Therefore, it may still be preferable to use an LLC as a general partner provided the LLC is created in a jurisdiction where charging orders are the exclusive remedy.

A well drafted limited partnership agreement will: (i) restrict an LLC general partner from conveying its membership interests, without the consent of the limited partners; and/or (ii) provide that a charging order against a member of the general partner LLC will cause the LLC to be disassociated from the limited partnership as a general partner. Both alternatives will avoid the creditor from becoming a member of an LLC that is the sole general partner of a limited partnership, and thereby gaining control of the LLC general partner. Until legislative action is taken to resolve the exclusive remedy issue created by the *Olmstead* decision, owning a general partnership interest directly may be better than owning said general partnership interest indirectly through an LLC. However, tax and other issues may render individual ownership of a general partnership interest in a Florida limited partnership less desirable than ownership through an LLC. Florida limited partnerships having a Florida LLC general partner may benefit from restructuring, described below (such as moving the situs of the LLC to a state where a charging order is the exclusive remedy against the owner of an LLC). As of August 19, 2010, eight states have exclusive remedy language and prohibition of foreclosure as part of their LLC Acts and/or Limited Partnership Acts.²⁷

²⁷ See Alaska Stat. §10.50.380; N.J. Stat. §42:2B-45; 18 Okl. St. §2034; S.D. Codified Laws §47-34A-504; Tex. Business Organizations Code §101.112; Wyo. Stat. §17-29-503, for LLC states Alaska, New Jersey, Oklahoma, South Dakota, Texas, and Wyoming. See LP Code of Ala. 10-9C-703; Alaska Stat. §32.11.340; Fla. Stat. 620.1703; S.D. Codified Laws §48-7-703; Tex. Business Organizations Code 153.256, for LP Act states Alabama, Alaska, Florida, South Dakota, Texas. Note, while some states do not have exclusive remedy and foreclosure prohibition in their LLC statutes, court decisions in such states (including Delaware) have interpreted state law to provide such protection. See below note 40, for articles providing a summary of each state's charging order provisions; below note 35, for articles by various authors relating to charging orders and state statutory language.

PRIOR ATTEMPT TO CREATE CONTINUITY BETWEEN CHARGING ORDER PROTECTION FOR LLCs AND PARTNERSHIPS WAS UNSUCCESSFUL

In 2007, the Asset Preservation Committee of the Real Property, Probate and Trust Law Section of the Florida Bar attempted to introduce exclusive remedy and prohibition against foreclosure language provisions, almost identical to those in §620.1703 of the Florida Revised Uniform Limited Partnership Act of 2005, for LLCs and Florida general partnerships.²⁸ The proposal was supported by the Executive Counsel of the Real Property, Probate and Trust Law Section of the Florida Bar.²⁹ The explanation attached to the Legislative Position Request Form included a section entitled: "Extension of Charging Lien Limitation and Foreclosure Prohibition Against Partner and Member Interests in Other Partnerships and in Limited Liability Companies." The "White Paper" attached to the Florida Bar's "Legislative Position Request Form" describing the proposed legislation stated:

²⁸ See Legislative Position Request Form Submitted By Real Property, Probate & Trust Law Section, Jan. 5, 2006, available at http://www.rpptl.org/Content/Committees/LegislativeReview/Creditor's_remedies_against_LP_and_LLLP_Interests.pdf [hereinafter

Legislative Position].

²⁹ *Id.*

The same policy concerns that caused the adoption of the limited remedy of a charging lien and prohibition of foreclosure apply equally to partner interests in general partnerships and in limited liability partnerships and member interests in limited liability companies. Accordingly, the proposed legislation would extend those features to the general and limited liability partnership and limited liability company statutes. ³⁰

³⁰ Legislative Position, above note 28.

The proposal was withdrawn when opposition to the policy being extended was expressed by those representing creditors, and this issue was never considered by the Florida Legislature. Based upon discussions with the Florida Bar's Chapter 608 LLC Drafting Task Force Chair Louis T. M. Conti and committee member Richard Comiter, in addition to the above described proposal initiated by the Florida Bar's Asset Protection Subcommittee, the Business Law Section Drafting Committee in 2006 proposed Amendments to the LLC Act that initially included "exclusive remedy" language to the LLC Act. The Business Law Section also decided not to proceed to the Florida Legislature in order to assure that other non controversial revisions to the LLC Act would be enacted.

INCONSISTENT TREATMENT FOR LIMITED PARTNERSHIPS, GENERAL PARTNERSHIPS, AND LLCs MAY HAVE CAUSED CONFUSION IN THE MAJORITY OPINION

One significant reason provided in the *Olmstead* majority opinion supporting its conclusion was that Florida's Revised Uniform Limited Partnership Act of 2005 specifically provided that a charging order is the exclusive remedy and foreclosure is not an available remedy, and the Revised Uniform Partnership Act of 1995 specifically provided that the remedies described in §620.8504 were exclusive, but no such exclusive language was provided in the Florida Limited Liability Company Act. ³¹ The majority opinion said:

³¹ *Olmstead*, 2010 Fla. LEXIS 990, 35 Fla. L. Weekly S 357 at *15-16.

In this regard, the charging order provision in the LLC Act stands in stark contrast to the charging order provisions in both the Florida Revised Uniform Partnership Act and the Florida Revised Uniform Limited Partnership Act.... [and] [a]lthough the core language of the charging order provisions in each of the three statutes is strikingly similar, the absence of an exclusive remedy provision set the LLC Act apart from the other two statutes. ³²

³² *Id.*

Based upon the disparity between the LLC and limited partnership law, the majority opinion states: "[w]here the legislature has inserted a provision in only one of two statutes that deal with closely related subject matter, it is reasonable to infer that the failure to include that provision in the other statute was deliberate rather than inadvertent." ³³ That might be a reasonable inference, but the justices did not have access to nor were they aware of the real story. For example, as discussed above, Florida's Legislature never had the opportunity to determine whether LLCs should have the same charging order exclusive remedy provisions as were enacted as part of the Florida Revised Uniform Limited Partnership Act of 2005. Had the 2006 legislative proposal from the Real Property, Probate and Trust Law Section or similar proposals from the Business or Tax Law Sections of the Florida Bar, that would provide charging order exclusive remedy protection for LLCs as described above, been put before the Florida Legislature, the majority opinion would have been correct, assuming the charging order protection was not provided to members of single-member LLCs by the Florida Legislature after due consideration. However, because the above described legislative proposals were never submitted to the Florida Legislature, the majority's conclusion is misguided because the omission of exclusive remedy language in the LLC statute was never considered.

³³ *Id.* at *15.

OLMSTEAD DECISION COULD HAVE NATIONAL CONSEQUENCES

There is confusion in the courts and among practitioners throughout the United States on whether charging orders are the exclusive remedy based upon applicable state law.³⁴ In recent years, a number of articles have been written suggesting the best states to form limited partnerships and LLCs, taking into account asset protection.³⁵ Since legislation is continually changing on a statewide basis, many recent articles may already be outdated. For example, Wyoming and Texas enacted protective charging order laws in 2010³⁶ and 2009³⁷ respectively.

³⁴ See *Nigri v. Lotz*, 453 S.E. 2d 780 (Ga. Ct. App. 1995) (explaining that under the Georgia Limited Partnership statute, a financial interest of a limited partner could be reached by garnishment as well as by a charging order, where the Georgia statute did not contain exclusivity language).

³⁵ See Merric, Comer, & Monasky, "Forum Shopping for Favorable FLP and LLC Law: 2010 LLC Asset Protection Planning Table" (Steve Leimberg's Asset Protection Planning Newsletter #154) May 25, 2010, available at <http://www.leimbergservices.com>; Merric, Comer, & Worthington, "Charging Order: What does sole or exclusive remedy mean?" *Trusts & Estates* (Apr. 2010); Worthington & Merric, "Which Situs is Best?" *Trusts & Estates* 54 (Jan. 2010); Nelson, "Asset Protection for Estate Planners," Address at the 43rd Annual Heckerling Institute on Estate Planning (Jan. 2009), in 43rd Annual Heckerling Institute on Estate Planning at 18-34-18-35 (Matthew Bender, 2009); Jetel, "Asset Protection in the Context of LPs and LLCs," (Steve Leimberg's Asset Protection Planning Newsletter #121) Jan. 31, 2008, available at <http://www.leimbergservices.com>; Merric & Comer, "Searching for Favorable FLP & LLC Law — Part III," (Steve Leimberg's Asset Protection Planning Newsletter #117) Dec. 19, 2007, available at <http://www.leimbergservices.com>.

³⁶ Wyo. Stat. §17-29-503 (effective July 1, 2010).

³⁷ See Tex. Business Organizations Code §101.112 (effective Sept. 1, 2009); Tex. Business Organizations Code §153.256 (effective Sept. 1, 2009).

The fact that a state may have favorable charging order protection within its limited partnership act does not necessarily mean that the state's LLC laws are equally beneficial. In Florida for example, although the Florida Revised Uniform Limited Partnership Act of 2005 has favorable exclusive remedy and foreclosure provisions and is mentioned by a number of authors as one of the "Magnificent Seven,"³⁸ *Olmstead* is sure to put Florida in the cellar when it comes to protection of LLC members. Prudent practitioners should consider suggesting a jurisdiction where a charging order is the exclusive remedy and foreclosure is prohibited.³⁹ Carter Bishop, a Professor of Law at Suffolk University Law School, has written extensively on charging order issues.⁴⁰ He has summarized the laws of each state and has distinguished those states that specify that a charging order is the exclusive remedy, those that are silent, and those that provide protection beyond exclusive remedy language (e.g., by stating that remedies such as foreclosure are specifically prohibited).⁴¹ The Bishop articles referenced list a number of states that have favorable exclusive remedy and foreclosure limitation provisions. However in light of the pace of legislative changes in this area, no decision should be made in selecting a situs until current state law is verified.

³⁸ Merric, Comer, & Worthington, "Charging Order: What Does Sole or Exclusive Remedy Mean?" *Trusts & Estates* (Apr. 2010).

³⁹ Merric, Comer, & Monasky, "Forum Shopping for Favorable FLP and LLC Law: 2010 LLC Asset Protection Planning Table" (Steve Leimberg's Asset Protection Planning Newsletter #154) May 25, 2010, available at <http://www.leimbergservices.com>.

⁴⁰ See Bishop, "Fifty State Series: LLC & Partnership Transfer Statutes" (Suffolk University Law School Research Paper No. 10-25), available at <http://ssrn.com/abstract=1621694>; Bishop, "Fifty State Series: LLC Charging Order Case Table" (Suffolk University Law School Research Paper No. 10-15), available at <http://ssrn.com/abstract=1565595>; Bishop, "Fifty State Series: LLC Charging Order Statutes" (Suffolk University Law School Research Paper No. 10-03), available at <http://ssrn.com/abstract=1542244>; Bishop, "A Jurisdictional & Governing Law Quagmire: LLC Charging Orders" (Journal of Business Entities, Forthcoming; Suffolk University Law School Research Paper No. 10-05), available at <http://ssrn.com/abstract=1545855>; Bishop, "Reverse Piercing: A Single Member LLC Paradox," 54 *S.D. L. Rev.* 199 (2009); Bishop, "Through the Looking Glass: Status Liability and the Single Member and Series LLC Perspective," 42 *Suffolk U. L. Rev.* 459 (2009);

Bishop & Kleinberger, "The Next Generation: The Revised Uniform Limited Liability Company Act," 62 *Bus. Lawyer* 515 (2007); Bishop, Geu, & Kleinberger, "Charging Orders and the New Uniform Limited Partnership Act: Dispelling Rumors of Disaster," 18 *Prob. & Prop.* 30 (2004); Bishop, "Unincorporated Limited Liability Business Organizations: Limited Liability Companies and Partnerships," 29 *Suffolk U. L. Rev.* 985 (Winter 1995).

⁴¹ See *id.*

WHAT SHOULD STATES DO NOW?

As a result of *Olmstead*, the Florida Legislature should include exclusive remedy protection in the Florida Limited Liability Company Act or any update thereof, and remedies such as foreclosure should be expressly prohibited. In light of *Olmstead* and until Florida legislation is enacted, it would be prudent to form both single-member and multimember LLCs in states such as Texas, Alaska, Wyoming, and Delaware if protection of membership interests is an objective. The more difficult question is whether to provide exclusive remedy and foreclosure protection for both single-member and multimember LLCs. Carter Bishop's conclusion, as described below, provides helpful insight:

The sensible statutory restrictions applicable to transfers of a membership in a multiple member limited liability company are justified and intuitive. Specifically, the rules that permit a member to freely transfer economic rights to future distributions while at the same time requiring the consent of the remaining members to admit the transferee as a member are appropriate to balance the reasonable expectations of members of a close business association. However, when applied to a SMLLC ["single-member LLC"], the same rules create a perverse and unexpected result.... There are no other remaining partners to protect as in the case of a multi-member limited liability company.... Ultimately, these perverse results are best cured by statutory amendment. Preferably, every state would amend its SMLLC legislation to provide that upon the voluntary or involuntary transfer of the only economic interest in the SMLLC, the transferee will be admitted as a substituted member, with or without the consent of the only member. ⁴²

⁴² Bishop, "Reverse Piercing: A Single Member LLC Paradox," 54 *S.D. L. Rev.* 199, 231-32 (2009).

Based upon Bishop's analysis, the *Olmstead* court did, as far as single-member LLCs go, reach the right result, but for the wrong reasons. Florida's Legislature never had the opportunity to determine whether to extend the same protection provided in the Florida Revised Uniform Limited Partnership Act of 2005 to LLCs or general partnerships, but had they been given the choice, based upon the discussion above, they may not have provided such protections to single-member LLCs.

Currently, only Wyoming specifically provides exclusive remedy protection to a judgment debtor who is the sole LLC member by stating that its protection includes "any judgment debtor who may be the sole member" of an LLC. ⁴³ Other states, such as Delaware, that have exclusive remedy protection are silent as to whether their protection extends to single-member LLCs. A reasonable argument can be made that because no exclusion is provided in statutes such as Delaware for single-member LLCs, that exclusive remedy protection applies to them as well. Yet, as previously quoted from Carter Bishop, with a single-member LLC there are no remaining partners (or members) to protect. Those considering proposed legislative responses to *Olmstead* should be aware of the possibility of the aggressive asset protection that could result if single-member LLCs had equal exclusive charging order protection as multimember LLCs. Single-member LLCs could be formed and the sole member could contribute all of his or her business and personal assets (other than Florida Homestead) thereto. Would the sole member then benefit from the exclusive remedy charging order protection? ⁴⁴

⁴³ Wyo. Stat. §17-29-503(e), above note 4.

⁴⁴ In Florida, homestead protection could be lost for property tax purposes and asset protection if the homestead was conveyed to a Florida partnership or LLC. See Nelson, above note 35, at 18-30-18-34.

POTENTIAL ABUSE IF SINGLE-MEMBER LLCs ARE PROVIDED EQUAL PROTECTION

The examples below provide insight as to potential asset protection planning opportunities if single-member and multimember LLCs are treated the same, and applicable state law provides a charging order as the exclusive remedy and prohibits other remedies including but not limited to foreclosure of the

charging order:

Example 1: Mike is the sole owner of a manufacturing business that has been operating as a single-member LLC for the past five years. The LLC elects to be taxed as an S Corporation. The single-member LLC has annual sales of \$50 million and net profits of \$5 million.

Example 2: Sal, a real estate developer, forms multiple single-member LLCs to hold various commercial real estate properties valued in the aggregate at \$10 million. Each single-member LLC owns a separate property.

Example 3: Jose, a surgeon practicing without malpractice insurance, has no existing or known contingent creditors. He forms a single-member LLC and conveys title to his entire \$5 million marketable security portfolio thereto. Jose forms a second single-member LLC and conveys his \$4 million Aspen ski condominium thereto. He forms a third single-member LLC and conveys his art collection, his jewelry and his collection of sports memorabilia (having an aggregate value of \$3 million).

Assume the single-member LLC owners in examples 1 through 3, above, subsequently become subject to a judgment arising out of events occurring post-LLC formation and funding, resulting from an automobile accident that disabled a prominent 45-year-old Florida attorney with four children ranging from ages eight to 15, rendering the attorney unable to continue his law practice. What remedies should be available to the disabled attorney in trying to collect on his judgment against Mike, Sal and Jose in the above examples?

Ultimately, the attorney will obtain a charging order against Mike's LLC interest. If a charging order is the exclusive remedy against Mike's LLC interest, Mike can reinvest the operating profits and pay himself significant but reasonable compensation (wages). The disabled attorney would have no remedy other than to wait for a distribution or negotiate a settlement with Mike. The same results would occur with respect to Sal and Jose in examples 2 and 3 above, unless a judge takes the position that the protection afforded by a single-member LLC is not available with respect to personal assets.

As reflected in the examples above, providing exclusive remedy protection for single-member LLCs and prohibiting other remedies such as foreclosure, could create a lock box for the debtor/owner. As the sole member, the debtor/owner has no fiduciary duty to any other LLC members, and as such, has power to control the timing and character of all distributions. The policy of protecting the other LLC members from a judgment creditor does not apply in the case of a single-member LLC. If exclusive remedy and foreclosure prohibition is provided for the sole member of a single-member LLC, creation of single-member LLCs may be as effective, at least for purposes of negotiation, as using a domestic or foreign self-settled asset protection trust in jurisdictions that sanction such trusts. Furthermore, the restrictions and administrative burdens of self-settled asset protection trusts (e.g., the need to have a trustee in the jurisdiction) could be avoided by using a single-member LLC in a jurisdiction that provides exclusive remedy and foreclosure prohibition, where the sole owner could serve as the sole manager, as long as there is at least some nexus within the jurisdiction in which the LLC is formed.

It should be noted that, if a self-settled asset protection trust is respected, a judgment creditor generally will have no interest therein. Yet, the trustee could have discretion to make distributions for the benefit of a debtor beneficiary and upon the beneficiary's death, the beneficiary could have a power to designate successor beneficiaries through a testamentary special power of appointment. Upon the death of the debtor beneficiary without exercising the power of appointment, the assets of the self-settled trust would pass to the remainder beneficiaries of such trust, free and clear of any creditors of the debtor. However, with LLCs, even if the charging order is the exclusive remedy, once distributions are made to the LLC member, creditors would recover as a result of the charging order. Furthermore, upon the death of the judgment debtor, his or her LLC membership interests remain an asset that will be subject to creditor's claims, although subject to continued charging order protection. The practical consequences of the charging order protection as the exclusive remedy for an LLC or limited partnership is that creditors are being encouraged to negotiate a settlement with the debtor if the judgment creditor is unable to force distributions to the LLC member or limited partner through the courts. The sole member of an LLC will have exclusive authority to decide on the timing of distributions. As a result, the charging order protection for single-member LLCs will also serve to safeguard the debtor's LLC assets and bring creditors to the negotiating table.

There is a great disparity in the approach states have taken with respect to LLC charging orders. Robert H. Leonard, a Wyoming attorney active in his state's LLC legislation, said that Wyoming seeks to be considered as a premier venue for estate planning. Wyoming has self-settled asset protection trust

legislation and restated its entire LLC Act effective July 1, 2010. Leonard said the recent LLC changes were intended to clarify prior state law that provided charging order protection as the exclusive remedy for LLCs, without differentiating between single-member and multimember LLCs.⁴⁵ Leonard believes that single-member LLCs that are operating businesses, real estate holding companies, or even LLCs owning solely a vacation home, would be protected by Wyoming's exclusive remedy statute. Leonard also indicated that notwithstanding Wyoming law, it may be possible for a judge faced with a single-member LLC holding exclusively personal assets (such as jewelry and art) to provide remedies beyond a charging order due to lack of a business purpose.⁴⁶

⁴⁵ Wyo. Stat. §17-29-503, above note 4.

⁴⁶ It should be noted that neither Florida nor Wyoming requires a business purpose. See Fla. Stat. §608.403 ("A limited liability company may be organized under this chapter for any lawful purpose..." [emphasis added]); Wyo. Stat. §17-29-104(b) ("A limited liability company may have any lawful purpose, regardless of whether for profit" [emphasis added]). Both Florida and Wyoming require that an LLC may be organized for any lawful purpose.

Based upon the discussion and examples above, a statutory distinction could be made between single-member and multimember LLCs so that the exclusive remedy protection is not available to the owner of a single-member LLC but is available to multimember LLCs. Alternatively, LLC legislation similar to Wyoming's can be enacted to specifically provide charging order protection to single-member and multimember LLCs.⁴⁷ While drafting a statute to distinguish between single-member LLCs and multimember LLCs and providing exclusive remedy and foreclosure protection to only multimember LLCs does not seem to be a daunting task, implementation is likely to be a challenge. As an example, how would a multimember LLC be defined?⁴⁸ Could an LLC with a 99.99% member and a .01% member qualify as a multimember LLC? How could a statute be drafted that requires at least two significant or meaningful members that will not result in vast litigation? Should a safe harbor interest be provided that will create a statutory multimember LLC? Would the statute need to look through any business entity LLC members to determine whether beneficial ownership is entirely in one LLC member? Should the statute refer to a de minimis percentage of an LLC that would be disregarded in determining whether a single-member LLC exists? Should exclusive remedy protection be provided to single-member LLCs, but be subject to court oversight as provided, by way of example, in the revised Uniform Limited Liability Company Act which allows a court to foreclose and order the sale of the "transferable interest?"⁴⁹ Would such court discretion create uncertainty? The answers to the questions raised in this section are left to those who will need to devote significant time and effort to find an effective statutory solution. Each state will need to weigh its desire to be a business friendly jurisdiction against any policies to limit creditor protection. Any state law that differentiates between single-member and multimember LLCs may find it difficult to establish guidelines that would define single-member and multimember LLCs in such a way as to not be subject to manipulation by creative debtors and their lawyers. What is clear is that providing exclusive remedy and foreclosure protection for single-member LLCs is likely to result in an unanticipated asset protection vehicle that could exceed the asset protection benefits contemplated. States considering whether to enact provisions similar to Wyoming may want to establish reasons, such as lack of business purpose, to protect creditors. Possibly, states without domestic self-settled asset protection trust legislation may have an overall state policy against asset protection that would make it unlikely for such a state to pass legislation providing enhanced asset protection for single-member LLCs.

⁴⁷ Wyo. Stat. §17-29-503, above note 4.

⁴⁸ See Fla. Stat. 608.402(21) (defining an LLC member as "any person who has been admitted to a limited liability company as a member in accordance with this chapter and has an economic interest in a limited liability company which may, but need not, be represented by a capital account"). Due to the difficulties in statutorily defining what constitutes a member, it may be best to leave this issue to the courts, on a case-by-case basis, if single-member and multimember LLCs are provided different charging order protection.

⁴⁹ *Rev. Unif. Ltd. Liab. Co. Act* §503(c) (2006), above note 12.

LEGISLATIVE FIX MAY BE YEARS AWAY

In light of the Florida Supreme Court's *Olmstead* decision, members of Florida LLCs should consider

restructuring their LLC ownership. Florida Bar committees have been meeting regularly to determine how to address legislatively the consequences of *Olmstead*. Having recently returned from a combined meeting of Florida Bar committees that included the Chapter 608 LLC Drafting Task Force and an "Olmstead Patch Committee" held on August 5, 2010, and an August 17 follow-up telephone conference, some of the best and brightest members of the Business Law Section, the Tax Law Section, and the Real Property, Probate and Trust Law Section of the Florida Bar have been trying to decide what approach should be proposed to remedy the *Olmstead* decision. Among the options were to propose legislation that would: (i) provide that the charging order is the exclusive remedy that could be utilized for multimember LLCs and specify that foreclosure is specifically prohibited; or (ii) provide exclusive remedy protection for all LLCs (i.e., including both single-member and multimember LLCs), and specify that foreclosure is prohibited for all LLCs (i.e., single-member and multimember LLCs). Meetings are ongoing with the goal to have some resolution submitted to the Florida Legislature for the 2011 session. Until the proposal is submitted, approved and becomes effective, for those who want greater certainty that interests in multimember Florida LLCs will be protected by having charging orders considered as the exclusive remedy for a judgment debtor's membership interests, action should be considered now (e.g., moving the LLC to a state that has provided clear statutory language that a charging order is the exclusive remedy and foreclosure is prohibited).⁵⁰

⁵⁰ See Alaska Stat. §10.50.380; N.J. Stat. §42:2B-45; 18 Okl. St. §2034; S.D. Codified Laws §47-34A-504; Tex. Business Organizations Code §101.112; Wyo. Stat. §17-29-503, for examples of states that provide statutory language that clearly provides that a charging order is the exclusive remedy and other remedies, such as foreclosure, are not available for creditors of LLCs. Other states, such as Delaware, have exclusive remedy statutes but have only case law and legislative history prohibiting foreclosure. See *New Times Media LLC v. Bay Guardian Co.*, 2010 U.S. Dist. LEXIS 64395 (D. Del. 6/28/10).

CONCLUSION

The *Olmstead* decision will require states like Florida to reexamine their laws to determine remedies for judgment creditors against interests in single-member and multimember LLCs. There are plenty of landmines in this analysis. The discussion above shows how the lack of continuity between Florida's Limited Liability Company Act, Florida's Revised Uniform Limited Partnership Act of 2005, and Florida's Revised Uniform Partnership Act of 1995 has resulted in Florida's Supreme Court making an inaccurate assumption. *Olmstead's* tentacles will reach many practice areas, and Florida is likely to have a leadership role by having its Business Law, Tax Law and Real Property, Probate and Trust Law committees consider how to best resolve the existing uncertainty created by *Olmstead*. Practitioners need to carefully monitor this fluid situation.

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ISSN 1947-3923

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