

The Florida Senate
BILL ANALYSIS AND FISCAL IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the Banking and Insurance Committee

BILL: CS/SB 1152

INTRODUCER: Banking and Insurance Committee and Senator Simmons

SUBJECT: Limited Liability Companies

DATE: April 25, 2011 REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Hrdlicka	Cooper	CM	Favorable
2.	O'Connor	Maclure	JU	Favorable
3.	Matiyow	Burgess	BI	Fav/CS
4.				
5.				
6.				

Please see Section VIII. for Additional Information:

- | | | |
|------------------------------|-------------------------------------|---|
| A. COMMITTEE SUBSTITUTE..... | <input checked="" type="checkbox"/> | Statement of Substantial Changes |
| B. AMENDMENTS..... | <input type="checkbox"/> | Technical amendments were recommended |
| | <input type="checkbox"/> | Amendments were recommended |
| | <input type="checkbox"/> | Significant amendments were recommended |

I. Summary:

In response to a Florida Supreme Court holding about remedies available to a judgment creditor of a single-member limited liability company, CS/SB 1152 amends s. 608.433, F.S. The CS clarifies that the general application of the decision in *Olmstead v. Federal Trade Commission*¹ to single-member limited liability companies does not apply to multiple-member limited liability companies.

The CS provides, with one exception, that a charging order is the “sole and exclusive remedy” by which a judgment creditor of a member or member’s assignee may satisfy a judgment from a judgment debtor’s interest in a limited liability company or rights to distributions from a limited liability company. The exception arises in situations in which a limited liability company has only one member. The CS provides that the court may order the sale of a member’s interest in a single-member limited liability company if the judgment creditor shows that distributions under a charging order will not satisfy the judgment in a reasonable time.

¹ *Olmstead v. Federal Trade Commission*, 44 So. 3d 76 (Fla. 2010),

The CS provides that the amendments made to s. 608.433, F.S., are clarifying and apply retroactively.

This CS substantially amends section 608.433, Florida Statutes.

II. Present Situation:

Limited Liability Companies

Sections 608.401-608.705, F.S., comprise the “Florida Limited Liability Company Act.” A limited liability company, or LLC, is a statutorily recognized, “hybrid business entity that offers all of its members limited liability as if they were shareholders of a corporation but treats the entity and its members as a partnership for tax purposes. In other words, a limited liability company is a form of legal entity that has the attributes of both a corporation and a partnership but is not formally characterized as either one.”²

Members and managers of an LLC are separate from the company itself. Generally, the members and managers of an LLC are not liable, solely by reason of being a member or serving as a manager or managing member, under a judgment, decree, or order of a court, or in any other manner, for a debt, obligation, or liability of the limited liability company. However, this may be expanded or restricted by the provisions of the LLC’s articles of organization or operating agreement.³ Florida law permits single-member LLCs.

Generally, except as otherwise provided in the LLC’s articles of organization or operating agreement, no person may be admitted as a member unless a majority-in-interest of the current members consent.⁴ A member may assign his or her interest in the LLC, either the whole or a part, but the same general rule for becoming a member applies to the assignee as well.⁵ An assignee has no right to participate in the management of the business except as provided in the articles of organization or operating agreement and upon approval of all the members of the LLC, excluding the assigning member. An assignee’s interest generally only allows him or her to share in the profits and losses and receive distributions from the LLC.⁶

An assignee may become a member of the LLC only if all the members of the LLC, excluding the assigning member, consent, unless the articles of organization or operating agreement provide otherwise.⁷

According to the Division of Corporations of the Department of State, there are 548,893 active LLCs in Florida.⁸ The number of LLC filings has generally increased over the last 10 years.

² AMJUR LIMLIACO §1

³ Section 608.4227, F.S. See also s. 608.4228, F.S., which states that a member or manager shall not be personally liable for monetary damages to the LLC.

⁴ Section 608.4232, F.S.

⁵ Section 608.432, F.S.

⁶ The provisions related to assignments are the same as provisions related to partnerships, whereby if a partner transfers his or her interest, the remaining partners are not required to accept the new partner as an equal for management and voting purposes.

⁷ Section 608.433, F.S.

There were 25,566 new business entity filings related to LLCs in 2001, while 138,287 such documents were filed in 2010.

Judgments and Limited Liability Companies

A judgment is an order of the court creating an obligation, such as a debt. Chapter 56, F.S., provides mechanisms for execution of judgments. Section 56.061, F.S., provides that various categories of real and personal property, including stock in corporations, are subject to levy and sale under execution of a court's order or judgment. A member's own interest in an LLC is considered personal property, and is "reasonably understood to fall within the scope of 'corporate stock.'"⁹

Section 608.433(4), F.S., provides for a judgment creditor to apply to a court to charge the LLC membership interest of a member with payment of an unsatisfied amount of judgment owed to the creditor, with interest (otherwise known as a "charging order").¹⁰ "To the extent so charged, the judgment creditor has only the rights of an assignee of such interest."¹¹ However, the statute also provides that it "does not deprive any member of the benefit of any exemption laws applicable to the member's interest."¹²

A charging order does not give the judgment creditor governance rights with respect to the LLC, because an assignee has no right to participate in the management of the business, unless the articles of organization or operating agreement states otherwise. A judgment creditor, then, would only be able to share in the profits and receive distributions from the LLC.

The theory behind the charging order is that a judgment creditor can be paid from the profits or distributions from the LLC without the disruption of the business caused by inserting another member into the group or the damage caused to other members if the business, or portions of it, was sold to pay the judgment creditor.¹³ As a federal bankruptcy court has explained, "a charging order protects the autonomy of the original members, and their ability to manage their own enterprise."¹⁴

The charging order is not unique to the LLC business structure. Florida's Revised Uniform Partnership Act of 1995, ss. 620.81001-620.9902, F.S., and Florida's Revised Uniform Limited Partnership Act of 2005, ss. 620.1101-620.2205, F.S., similarly provide charging order remedies in partnership and limited partnership law.

⁸ Division of Corporations, Department of State, "Yearly Filings," available at http://www.sunbiz.org/corp_stat.html (last visited Mar. 12, 2011). The filing numbers reflect the number of new documents filed beginning January 1 and ending December 31 of each year.

⁹ *Olmstead v. Federal Trade Commission*, 44 So. 3d 76, 80 (Fla. 2010).

¹⁰ A "judgment creditor" is a person having a legal right to enforce execution of a judgment for a specific sum of money. Black's Law Dictionary, "judgment creditor" (9th Ed. 2010).

¹¹ Section 608.433(4), F.S.

¹² *Id.*

¹³ See, generally, *City of Arkansas City v. Anderson*, 752 P.2d 673, 681-84 (Kansas 1988) (discussing the charging order at common law and under the Uniform Partnership Act).

¹⁴ *In Re: First Protection, Inc.*, 440 B.R. 821, 830 (9th Cir. BAP (Ariz.) 2010) (citations omitted).

A limitation of the charging order remedy is that a creditor cannot recover unless the voting members of the LLC distribute profits. If the LLC does not make a distribution, the judgment creditor is not paid. Particular issues arise when a member of an LLC enters into bankruptcy, is subject to an adjudication of insolvency or appointment of a receiver, or makes an assignment of interest for the benefit of creditors.¹⁵ Section 608.4327, F.S., states that a person ceases to be a member of an LLC when these situations arise. This is because the economic interests of a creditor or receiver for an insolvent member would not be aligned with the best interest of the LLC.¹⁶ In the case of single-member LLC, there is tension between the interests of the creditors and employees of the LLC and the interests of the judgment creditor of the single member.

Olmstead v. Federal Trade Commission

In *Olmstead v. Federal Trade Commission*, 44 So. 3d 76 (Fla. 2010), the Florida Supreme Court held that Florida's statutory charging order provision is not the exclusive means for a judgment creditor to execute a judgment against the owner of a single-member LLC. The Court held that "a court may order a judgment debtor to surrender all right, title, and interest in the debtor's single-member LLC to satisfy an outstanding judgment."¹⁷

While the court's holding does not specifically apply to limited liability companies with more than one member, the court's reasoning would likely apply to all limited liability companies.

The Decision in Olmstead

In *Olmstead*, a federal court asked the Florida Supreme Court whether, under Florida law, a court may order a judgment debtor to surrender all "right, title, and interest" in the debtor's single-member LLC to satisfy an outstanding judgment. In the case, the Federal Trade Commission (FTC) alleged Olmstead was operating an "advance-fee credit card scam" and sued for unfair and deceptive trade practices.¹⁸ The FTC prevailed and obtained an order directing Olmstead to surrender all right, title, and interest in his LLC. Olmstead, the judgment debtor and sole member of an LLC, argued that a charging order under s. 608.433(4), F.S., was the sole and exclusive remedy available against his ownership interest in the LLC. He argued that no other remedy was applicable. The FTC argued that other remedies were available under Florida law – and that finding that the statutory charging order was the sole remedy for a single-member LLC would produce absurd results.¹⁹

The court held that a charging order under s. 608.433(4), F.S., was not the exclusive remedy. The court noted that s. 56.061, F.S., provides that stock in corporations is subject to sale and execution to satisfy a judgment and that because an LLC is a "type of corporate entity," an ownership interest in an LLC is reasonably understood to be corporate stock and subject to

¹⁵ At common law, the purpose of the charging order was to protect non-debtor partners from being forced into partnership with a judgment partner's creditor.

¹⁶ Davis, Gardner, and Mary Kendrick, *Single-Member LLC Will Not Shield Debtor's Assets from Judgment Creditor*, 29-Oct Am. Bankr. Inst. J. 52 (2010).

¹⁷ *Olmstead*, 44 So. 3d at 83.

¹⁸ See *Olmstead*, 44 So. 3d at 78.

¹⁹ See *Olmstead*, 44 So. 3d at 77-78.

execution under the statute.²⁰ The court rejected arguments that s. 608.433(4), F.S., displaced s. 56.061, F.S. It noted that Florida's partnership and limited partnership statutes contain similar charging order provisions but those provisions provide that the charging order is the exclusive remedy and that specific language relating to an exclusive remedy is not present in the LLC statute.²¹ Accordingly, the court said:

Specifically, 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 a single-member LLC... Section 608.433(4) does not displace the creditor's remedy available under section 56.061 with respect to a debtor's ownership interest in a single-member LLC.²²

Olmstead followed a similar holding from a Colorado court in 2003 – *In re Albright*, 291 B.R. 538 (Bkrcty.D.Colo. 2003). In *Albright*, “the sole-member of a Colorado LLC filed bankruptcy, and the court held that the Chapter 7 trustee became a ‘substituted member’ and could cause the LLC to sell its real property and distribute the proceeds to the estate.”²³ The court stated that the Colorado LLC laws exist to:

...protect other members of an LLC from having involuntarily to share governance responsibilities with someone they did not choose, or from having to accept a creditor of another member as a co-manager. A charging order protects the autonomy of the original members, and their ability to manage their own enterprise. In a single-member entity, there are no non-debtor members to protect. The charging order limitation serves no purpose in a single member limited liability company, because there are no other parties' interests affected.²⁴

However, the Colorado bankruptcy court specifically stated in a footnote that the holding would have been different if there had been other members in the LLC.²⁵ Colorado's statute on charging orders is similar to the law in Florida.

Criticism of Olmstead

In dissent, Justice Lewis argued that the majority opinion was rewriting the LLC Act to create a remedy not contemplated by the Legislature. He said that a reading of all of ch. 608, F.S., and not merely the provisions cited by the majority, makes clear that the LLC Act displaces ch. 56, F.S.²⁶ Justice Lewis warned:

This is extremely important and has far-reaching impact because the principles used to ignore the LLC statutory language under the current factual circumstances apply with

²⁰ *Olmstead*, 44 So. 3d at 80.

²¹ *See Olmstead*, 44 So. 3d at 81-82.

²² *Olmstead*, 44 So. 3d at 83.

²³ Miller, Elizabeth, *Are the Courts Developing a Unique Theory of Limited Liability Companies or Simply Borrowing from Other Forms?*, 42 Suffolk U. L. Rev. 617, 641-44 (2009).

²⁴ *In Re Albright*, 291 B.R. at 541 n.7.

²⁵ *In Re Albright*, 291 B.R. at 540.

²⁶ *Olmstead*, 44 So. 3d at 83-84 (Lewis, J., dissenting).

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.²⁷

The provisions of the LLC Act apply uniformly to all Florida LLCs, regardless of whether the LLC is a single-member LLC or a multiple-member LLC.

Commenters have explained the concern of some business law practitioners:

As a result of the dissenting opinion, many practitioners are concerned that a multiple-member Florida LLC arrangement may not provide charging order protection, although that is not what the majority held. ... [T]here is a good chance that there will be legislative clarification of this court-created "uncertainty by implication." In the interim, advisors should alert their clients to the exposure and consider bifurcating Florida LLC membership interests into voting and nonvoting interests, converting Florida LLCs to limited partnerships or limited liability limited partnerships, moving Florida LLCs to jurisdictions that have a more stable charging order protection law, or implementing other divestment of management control strategies.²⁸

III. Effect of Proposed Changes:

In response to a Florida Supreme Court holding about remedies available to a judgment creditor of a single-member limited liability company, CS/SB 1152 amends s. 608.433, F.S. The CS clarifies that the general application of the *Olmstead* decision to single-member LLCs does not apply to multiple-member LLCs.

Section 1 amends s. 608.433, F.S.

The CS defines a "charging order" as a lien on a judgment debtor's LLC interest or assignee rights. A judgment creditor has only the rights of an assignee of an LLC interest to receive any distributions that the judgment debtor would otherwise have been entitled to, limited to the extent of the judgment including interest.

The CS provides, with one exception, that a charging order is the "sole and exclusive remedy" by which a judgment creditor of a member or member's assignee may satisfy a judgment from a judgment debtor's interest in an LLC or rights to distributions from an LLC. The exception arises in situations in which an LLC has only one member. The CS provides that the court may order the sale of a member's interest in a single-member LLC if the judgment creditor shows that distributions under a charging order will not satisfy the judgment in a reasonable time.

Upon such a showing, the court may order the sale of the interest in the LLC pursuant to a foreclosure sale. The CS provides that the judgment creditor may make such a showing within a reasonable time after entry of the judgment and may do so at the time the judgment creditor applies for entry of the charging order. If the court orders a foreclosure sale, the purchaser at the

²⁷ *Olmstead*, 44 So. 3d at 84 (Lewis, J., dissenting).

²⁸ Gassman, Alan S., and Christopher J. Denicolo, David L. Koche, and Thomas O. Wells, *After Olmstead: Will a Multiple-Member LLC Continue to Have Charging Order Protection?*, 84-DEC Fla. B.J. 8, 10 (2010).

sale obtains the member's entire interest in the LLC, the purchaser becomes the member of the LLC, and the person whose interest is sold ceases to be a member of the LLC.

Section 2 states that the amendments made to s. 608.433, F.S., are clarifying and apply retroactively.

Section 3 provides that the act takes effect upon becoming law.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

D. Other Constitutional Issues:

This CS provides that it is intended to be clarifying and remedial in nature and shall apply retroactively (see Section 2). Retroactive application of legislation can implicate the due process provisions of the constitution.²⁹ As a general matter, statutes that do not alter vested rights but relate only to remedies or procedure can be applied retroactively.³⁰

The Florida Supreme Court has ruled that statutes enacted soon after a controversy over the meaning of legislation may be considered a legislative interpretation of the original law and not substantive change:

When, as occurred here, an amendment to a statute is enacted soon after controversies as to the interpretation of the original act arise, a court may consider that amendment as a legislative interpretation of the original law and not as a substantive change thereof. This Court has recognized the propriety of considering subsequent legislation in arriving at the proper interpretation of the prior statute.³¹

²⁹ See *State Department of Transportation v. Knowles*, 402 So. 2d 1155 (Fla. 1981).

³⁰ See *Metropolitan Dade County v. Chase Federal Housing Corporation*, 737 So.2d. 494 (Fla. 1999). See also *City of Orlando v. Desjardins*, 493 So. 2d 1027, 1028 (Fla. 1986) (citations omitted) (“If a statute is found to be remedial in nature, it can and should be retroactively applied in order to serve its intended purposes.”).

³¹ *Lowry v. Parole and Probation Commission*, 473 So. 2d 1248, 1250 (Fla. 1985) (internal citations omitted).

V. Fiscal Impact Statement:**A. Tax/Fee Issues:**

None.

B. Private Sector Impact:

The CS would benefit businesses by providing certainty and predictability to those establishing and maintaining multiple-member LLCs in Florida. Without such a change, businesses may move or create their LLCs in other states where certainty exists. It is not known how many, if any, businesses would relocate or not locate in Florida because of the *Olmstead* decision and without CS/SB1152 becoming law. Also, it is not known how many Florida LLCs, if any, would incur additional costs and change to a different business partnership structure.

C. Government Sector Impact:

None.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Additional Information:**A. Committee Substitute – Statement of Substantial Changes:**

(Summarizing differences between the Committee Substitute and the prior version of the bill.)

CS by Banking and Insurance on April 25, 2011.

The CS makes the following changes:

- Clarifies the purchaser of a court-ordered foreclosure sale obtains the member's entire LLC interest and not merely the rights of an assignee.
- Clarifies in the case of an LLC having more than one member, the remedy of foreclosure on a judgment debtor's interest in such LLC or against rights to distribution from such LLC is not available to a judgment creditor attempting to satisfy the judgment and may not be ordered by a court.

- Clarifies the CS does not limit:
 - The rights of a creditor that has been granted a consensual security interest in a limited liability company interest to pursue the remedies available to such secured creditor under other law applicable to secured creditors;
 - The principles of law and equity which affect fraudulent transfers;
 - The availability of the equitable principles of alter ego, equitable lien, or constructive trust, or other equitable principles not inconsistent with this section;
or
 - The continuing jurisdiction of the court to enforce its charging order in a manner consistent with this section.

B. Amendments:

None.