

The Georgia LLC Act Comes of Age

by L. Andrew Immerman and Lee Lyman

The Georgia LLC Act (the Act) has been a runaway success. A series of amendments to the Act in 2009 should ensure that its popularity continues and even increases. Although the amendments cover a wide array of disparate points, an overall theme emerges: that of accommodating the use of the LLC—limited liability company—in situations where corporations used to be the entity of choice, without sacrificing the LLC’s distinctive nature and flexibility.

The first Georgia limited liability company was formed in 1994, under legislation passed the previous year.¹ The original Act was amended sporadically over the years. But in view of the explosive growth of LLC law and in the use of Georgia LLCs,² the Partnership and LLC Committee of the State Bar of Georgia’s Business Law Section undertook a comprehensive review of the Act beginning in 2007. The consensus of the Committee was that the Act had held up well and that major revisions were not essential. Although the Committee’s final legislative proposals were lengthy, they were hardly radical. The package of proposals was endorsed by the State Bar of Georgia, introduced into the Georgia Legislature as H.B. 308, and ultimately enacted effective July 1, 2009 (the 2009 Amendments).³

The 2009 Amendments continue the longstanding “policy of this state with respect to limited liability companies to give maximum effect to the principle of freedom of contract and to the enforceability of operating agreements.”⁴ From the beginning, the guiding principle of the Act has been respect for the agreement of the parties. The flexibility granted to the members by the Act helps account for the Act’s continuing vitality.

The parties can put almost anything they want into Georgia operating agreements and rarely need to worry about exceeding the statute’s generous grant of flexibility. Accordingly, the Act is intended mostly as a series of default rules, which the parties are free to vary by agreement, although on many points a departure from the LLC default rules requires a written, and not merely oral, agreement.⁵

LLCs Are Not Corporations

In one sense, the growth of the LLC was too rapid. Many businesses—often on the sound advice of tax professionals—adopted LLCs in place of corporations, but without appreciating the significance of the switch.⁶ Unfortunately, in the move from corporations to LLCs, corporate law practitioners and businesspeople too often assume that an LLC is just a corporation that happens to have different initials at the end of its name. If an LLC and a corporation are essentially synonyms, little more is required in adapting to the LLC world than a mechanical substitution of other synonymous terms: “member” or “unitholder” for shareholder; “units” or “membership interests” for stock; “managers” or “governors” for directors; “company” for corporation; and so on.

Despite some similarities to corporations, Georgia LLCs are not constrained by the traditional apparatus of corporate law. There is nothing in the LLC world that is comparable to corporate shares of stock, shareholders, directors or officers—although the LLC operating agreement, as a contract, may employ those terms and may assign some meaning to them. The 2009 Amendments are to a large extent an attempt to clarify the similarities and differences between LLCs and corporations.

Using an LLC Instead of a Corporation

Despite the clear differences between LLCs and corporations, in certain instances it is appropriate for the structure and operations of an LLC to be similar to

those of a corporation. Certain of the 2009 Amendments were designed to reflect that correspondence, as we discuss below.⁷

Limited Liability

It is fundamental to LLC law that LLC members should have protection against unlimited personal liability that is at least as strong as the protection enjoyed by corporate shareholders. Two of the 2009 Amendments are designed to protect that fundamental principle.

The 2009 Amendments clarify that, unless otherwise agreed in writing, members, agents, employees and managers of an LLC are not at risk of unlimited personal liability to other members or to assignees of interests merely by virtue of their status as members, agents, employees and managers.⁸ This protection should have already been abundantly clear, but an out-of-state court decision might have raised needless doubts about it. In *Ederer v. Gursky*,⁹ New York's highest court held that a partner in a New York LLP bears unlimited personal liability to the other partners in the LLP, without regard to personal fault, and apparently without regard to the type of claim that the other partners may be making. If the members of the LLC want to waive liability protection, they may do so,¹⁰ but unlimited personal liability of the members to each other should be the exception and not the rule.

Ederer concerned LLPs rather than LLCs, and, we believe, would have come out differently had the entity been an LLC. Nevertheless, *Ederer* was so troubling that it was important to leave no room for doubt that the rule in *Ederer* is inapplicable to Georgia LLCs. Because the 2009 Amendments concerned only Georgia LLCs, those amendments make no attempt to modify Georgia's LLP provisions.¹¹ As *Ederer* itself pointed out, however, the partners may vary their responsibilities to one another and the partnership through agreement. Georgia LLPs



may want to examine their partnership agreements to see whether there is any possibility that the liability of partners to each other might be greater than intended.

Another one of the 2009 Amendments helps protect members and managers against personal liability on distributions that do not violate Georgia law. This is a subtle but important issue. Section 14-11-407(a) prohibits distributions that render the LLC unable to pay its debts, or that reduce assets below liabilities. The personal liability of a member or manager who wrongfully consents to such a prohibited distribution is not affected by the 2009 Amendments.

Nevertheless, it is possible—indeed, all too easy—for a distribution to violate the provisions of the articles of organization or the operating agreement, while otherwise being entirely permissible under Georgia law. Many operating agreements impose pointless formal requirements—for example, for annual meetings to be held with

advance notice and with a quorum—that are destined from the start to be ignored or forgotten. The Act, however, arguably could have been read as imposing personal liability for a distribution in violation of an LLC's self-imposed limitations. There is no justification for such personal liability. If the members of the LLC agree among themselves to bear personal liability on such a distribution, they of course may include such an agreement in the articles of organization or the operating agreement. Personal liability in those circumstances, however, should not be imposed by statute. LLC members should not have any greater personal liability than shareholders of corporations, and the amendments to section 14-11-408 bring LLC member liability more in line with corporate shareholder liability.

Continuity

Corporations, but not necessarily partnerships, have traditionally been designed to have indefinite

lives. We believe that, these days, an LLC, like a corporation, most often is expected to continue indefinitely. The 2009 Amendments help enable LLCs, much like corporations, to continue in business perpetually if they so choose, without worrying about needless disruptions to their status as ongoing businesses. Of course, it is still the case that an LLC operating agreement can easily provide for limited life if that is what the members want.

Under one of the 2009 Amendments, the personal representative takes over as member on the death or incapacity of the last remaining member by default, instead of that death or disability causing a dissolution of the LLC. Section 14-11-506 has new language stipulating that if there is only one member of an LLC, and that member dies or becomes incapacitated, the executor or other legal representative of the member will become the substitute member of the LLC. Without the change, it is too easy for the death or incapacity of the sole member of an LLC to trigger an unexpected and unwanted dissolution.

Other portions of the 2009 Amendments expressly permit the members of an LLC to waive their right to authorize the company to wind up and dissolve.¹² Like another 2009 Amendment,¹³ these amendments have the effect of facilitating the grant of enforceable rights to nonmembers (third parties). Some lenders require, before providing financing to an LLC, that the company's articles of organization or written operating agreement set forth certain limitations on dissolution. Nonmember managers sometimes also request the right to veto dissolution. The 2009 Amendments should help lenders and other third parties ensure that the LLC members cannot override limitations that the third parties are relying on. Of course, these amendments also have the effect of enhancing the continuity of life of an LLC.

Dissolutions themselves can now be undone within 90 days,

provided that the LLC has not filed a certificate of termination.¹⁴ A 2009 Amendment states that members of the LLC are now permitted in certain instances to amend the articles of organization or operating agreement to undo a dissolution, or, as long as there is at least one member, to continue the existence of the limited liability company after an event of dissolution.

Separate Entity

An LLC is largely the product of the agreement among its members. The LLC is also a separate entity, however, and not *merely* an agreement among the members or an aggregate of its members. Although partnership law has traditionally shown some ambivalence between "entity" and "aggregate"¹⁵ theories, corporate law and LLC law have not wavered in their allegiance to the "entity" camp. In perhaps its most radical departure from partnership law (and from the "aggregate" theory), a Georgia LLC with only one member is in no way defective. Although the validity of a single-member Georgia LLC has been clear for a long time—some would say since the time of the original Act—the 2009 Amendments reorganized and restated the rule.¹⁶

It has always been the rule that the "organizer" of the LLC need not be a member. Section 14-11-101(12), however, arguably carried an unintended implication to the contrary, and accordingly was amended. A partnership, by contrast, cannot be organized without the participation of at least one general partner.

New language in a 2009 Amendment confirms that an LLC is bound by its operating agreement, unless stated otherwise, and is not required to execute its own operating agreement.¹⁷ It has not been common practice in Georgia for an LLC to execute its own operating agreement, although some Georgia lawyers recommend it. But members, and perhaps third parties as well, have a legitimate expectation that the LLC will be

bound generally by its own operating agreement, whether or not the company signs the agreement. The new provision expressly validates the expectation that an operating agreement binds the LLC, while permitting an operating agreement to provide the extent, if any, to which the LLC is not bound.

Other Areas of Conformity to Corporate Code

There are and should be numerous differences between the Georgia Business Corporation Code¹⁸ and the Act. On the other hand, because the two statutory schemes are not always considered in tandem when one or the other of them is amended, some of the differences likely were historical accidents. The Committee did not undertake to review comprehensively the many differences. Nevertheless, a handful of the 2009 Amendments, in addition to some of the provisions noted above, do bring the Corporation Code and LLC Act closer together. For example, the 2009 Amendments clarify that notice under section 14-11-311(2) may be provided by electronic transmission. The Georgia Business Corporation Code provides for electronic notice, and it is appropriate for the Act to do so as well.

As a result of the 2009 Amendments, there is no longer any implication that the certificate of termination is mandatory after an LLC has wound up its business. Section 14-11-610 formerly said that a dissolved LLC "shall" file a certificate of termination with the Secretary of State "when" the LLC has wound up and can truthfully make certain required statements. But there was no time limit for filing the certificate, and it was unclear what liability would be incurred for failure to file the certificate. In practice, some—perhaps many—LLCs fail to file this certificate after winding up. The amendment recognizes that in reality the filing is optional. As a result of the 2009 Amendments, section 14-11-610 now corresponds more closely to its corporate counterpart.¹⁹

“Membership,” “LLC Interest” and Third-Party Rights

LLCs continue to function like partnerships in that LLCs tend to keep governance or management rights (associated with “membership”) and economic rights as an equity holder (“LLC interest” or “transferable interest”) separate. For corporations, both types of rights are generally aspects of “share” ownership. To add to the confusion, LLCs often want to grant enforceable rights to third parties who are neither members nor holders of equity interests. A number of amendments to the Act were intended to clarify the confusing relationship among “membership rights,” “LLC interests” and third-party rights.

Section 14-11-504(b) was amended to clarify that when a creditor receives a judgment against a member or an assignee of an LLC interest, the creditor is not thereby granted leave to interfere in the management of the LLC or to take certain other actions that would be disruptive to the company’s business. The prior language of the statute was already clear that when a judgment creditor obtains a “charging order” against the member or against an assignee of an interest in an LLC, the judgment creditor has no right to insert itself as a member of the company or otherwise interfere in management.²⁰ Instead, “the judgment creditor has only the rights of an assignee of the limited liability company interest.”²¹ Unless otherwise provided in the articles of organization or operating agreement, an assignee—including a creditor that has the rights of an assignee—has no membership rights and no rights to participate in management.²²

The limitation on the rights of a judgment creditor was already reflected in the “pick your partner” principle of the Act. This principle is at the heart of partnership law and has been carried over into the LLC statutes of every state. Under

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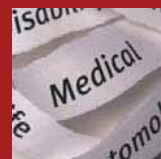
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this principle, a court cannot force you into partnership with someone you find objectionable; a partnership cannot be required against its will to admit someone as a partner. Similarly, the members of an LLC cannot be required against their will to accept some intruder as a member. Of course, the partnership or LLC can be required, like it or not, to make payments to a third party.

The concern prompting the proposal to amend section 14-11-504(b) was the risk that some open-ended language in that section might be interpreted as negating the “pick your partner” principle. Under section 14-11-504(b), the “remedy conferred by this Code section shall not be deemed exclusive of others which may exist. . . .” We know of no instance in which any court adopted an interpretation at odds with the “pick your partner” principle, and we do not believe that such an interpretation would be correct. Such an interpretation would essentially render meaningless the limitation on judgment creditors set forth in section 14-11-504(a). Nevertheless, because the language of the statute was vague, some Georgia lawyers advised LLC clients to form under the laws of Delaware or another state in which the statute is clear. Many other states, such as Delaware,²³ make the charging order the exclusive remedy. Georgia appears to be unique in its open-ended statement that the charging order is *not* exclusive.²⁴

The amendment was not motivated by any desire to expand the use of Georgia LLCs for protecting individuals’ assets from potential claimants. It is likely that jurisdictions, such as Nevada or Delaware, in which the charging order is expressly stated to be the creditor’s exclusive remedy, will continue to be more attractive for an individual interested in asset protection through an LLC.

It might have been preferable to bring Georgia even more into line with other states. But to minimize

changes to the prior statute, the amendment retains the open-ended structure of this provision and does not prejudge the issue of what other remedies may exist. With the amendment, however, section 14-11-504(b) is less troubling because, whatever other remedies may exist, the “pick your partner” principle clearly is not abrogated. Judgment creditors of members or assignees are prohibited from interfering with the management of the LLC, forcing a dissolution of the company or obtaining a court-ordered foreclosure sale of the interest.

The amendment, like the rest of section 14-11-504, relates only to judgment creditors of members. It has no implications for secured creditors of members. It is clear that a secured creditor that is also a judgment creditor does not lose any of the rights that it has as a secured creditor. The amendment also has no implications for creditors of the LLC.

Several amendments and three new subsections were added to section 14-11-505 to clarify matters related to the admission of members and the nature of a membership interest. The amendment to section 14-11-505(a) attempts to clarify the somewhat perplexing relationship between a “member” and the holder of a “limited liability company interest.” The amendment deletes certain language in section 14-11-505(a) to eliminate a possible implication that the “member” of an LLC must hold a “limited liability company interest.”

“Limited liability company interest,” as defined in section 14-11-101(13), is a technical term. “Limited liability company interest” is not strictly analogous to corporate “share.” Although “limited liability company interest” is sometimes thought to include the full panoply of rights that a member may have in an LLC, the term as defined by the Act has a more limited meaning. “Limited liability company interest” refers only to

the *economic* interest that the member may have as an equity holder—to the member’s share of profits and losses, and the member’s rights to receive distributions. The rights of a member may, and typically do, encompass more than such economic interest, including rights to governance or management or simply the receipt of information. These other rights are not inherently tied to the holding of a “limited liability company interest” in the somewhat narrow sense defined by the statute. If an LLC desires to designate some other stakeholder—such as an employee, creditor or former equity-owner—as a “member,” even though the stakeholder does not have a “limited liability company interest,” the statute should not prohibit the company from doing so.

The amendment incidentally helps clarify the purposes for which an LLC may be formed. The rule has long been that a Georgia LLC may be formed to engage in any “lawful activity.”²⁵ There are “lawful activities” other than business or other for-profit activities, and a natural reading of the rule was that an LLC did not need a profit motive.²⁶ Nevertheless, because it was arguable that a “member” needed to have an LLC interest, there was some concern that an LLC that was formed for purposes other than earning profits (or making distributions) could not have “members” in the strict sense. As noted above, an LLC without members is a confusing concept. If an LLC member need not have an economic interest, however, it is easier to give the rule permitting an LLC to engage in any “lawful activity” its natural reading.²⁷

The changes to section 14-11-101(18) confirm that an operating agreement may provide enforceable rights to a person who is not party to the operating agreement.²⁸ LLCs often find it useful to grant rights to persons (such as lenders, employees or option holders) who are not parties to



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the operating agreement, and the statute should provide assurance that Georgia law authorizes operating agreements to do so.

Issues for Another Day

The 2009 Amendments were intended not to be controversial. Although they stayed clear of some of the more contentious issues that are being debated around the country, those issues are not likely to go away. For instance, future consideration may be given to the possible conflict between LLC law, which permits operating agreements to include enforceable provisions that restrict the rights of the members to pledge or transfer interests in the LLC,²⁹ and certain provisions of UCC Article 9 that favor the alienability of interests, and invalidate many restrictions on assignment.³⁰ 



Andy Immerman is the immediate past chair of the Partnership and LLC Committee of the Business Law Section of the State Bar of Georgia.



Lee Lyman is the current chair of the Partnership and LLC Committee of the Business Law Section of the State Bar of Georgia.

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Endnotes

1. Ga. Act No. 174, 1993 Ga. Laws. 123 (effective Mar. 1, 1994); O.C.G.A. §§ 14-11-100 to -1109. For overviews of the 1993 legislation, see Charles R. Beaudrot, Jr. and Kendall Houghton, *Effective Use of*

Limited Liability Companies in Georgia: An Overview of Their Characteristics and Advantages, 45 MERCER L. REV. 25 (1993); Robert P. Bryant, *Georgia's New Limited Liability Company Act*, GA. BAR J., Winter 1993; and A.B. Cochran, III, *Review of Selected 1993 Georgia Legislation: Corporations, Partnerships and Associations*, 10 GA. ST. U. L. REV. 79 (1993-94).

2. Statistics attest to the remarkable rise of the Georgia LLC. In 2009, 54,134 Georgia LLCs were formed – nearly three times the number of Georgia For-Profit Corporations (18,275). These statistics are taken from the frequently-updated web site of the Secretary of State, at <http://www.sos.ga.gov/corporations/>.
3. Ga. Act No. 38, 2009 Ga. Laws 108 (sponsored by Rep. David Ralston, signed by the Governor Apr. 21, 2009, effective July 1, 2009). For a description of the Georgia Bar's full legislative agenda for 2009, see Mark Middleton, *State Bar Active in 2009 General Assembly*, 14 GA. BAR J., June 2009, at 26. Mark Middleton was instrumental in shepherding the 2009 Amendments through the legislature.
4. O.C.G.A. § 14-11-1107(b) (Supp. 2009).
5. See, e.g., *id.* § 14-11-304(a) (2003) (management is vested in the members unless otherwise provided in the articles or organization or a written operating agreement).
6. A powerful and illuminating case for the distinctiveness of LLCs and other unincorporated entities as compared to corporations is presented in a recent book, LARRY E. RIBSTEIN, *THE RISE OF THE UNINCORPORATION* (2009). Some differences between LLCs and corporations are discussed in L. Andrew Immerman, *Is There Any Such Thing as an LLC Unit?*, BUS. ENTITIES, July/Aug. 2009, at 20.
7. Another set of changes that helps to clarify the relationship between LLCs and corporations, and to conform the two types of entities where appropriate, relates to mergers and conversions. See O.C.G.A. §§ 14-11-212(a), -212(b), -212(c), -901(a), 905(a)(7), & -905(a)(8) (Supp. 2009). Such mergers—and even more so, conversions—were a novelty in 1993 but are now routine. See generally Cassady V. Brewer & L. Andrew Immerman, *Georgia Modifies and Expands its Entity Conversion Rules*, PUBOGRAM, July 2006, at 10.
8. O.C.G.A. § 14-11-303(a) (Supp. 2009).
9. 881 N.E.2d 204 (N.Y. 2007), *aff'g* 826 N.Y.S.2d 210 (App. Div. 2006) (interpreting New York Partnership Law § 26(b)). The decision of the Appellate Division arguably was made on much narrower grounds than that of the higher court. The Appellate Division may well have intended to impose personal liability on the partners only up to the value of the assets that the partners took out of the LLP. See L. Andrew Immerman & Lee Lyman, *A Hole in Lawyers' Liability Shield?*, BUS. L. SEC. NEWSL. (ST. BAR OF GA.), Jan. 2009, at 1.
10. See O.C.G.A. § 14-11-303(b) (Supp. 2009).
11. *Id.* §§ 14-8-15(b), 14-8-62 to 14-8-64 (2003). In the authors' view, *Ederer* was incorrectly decided and, even without any amendments to the Georgia statutes, should not be followed in Georgia with respect to any limited liability entity.
12. *Id.* §§ 14-11-602(a)(3), (b)(3) (Supp. 2009).
13. One of the changes to *id.* § 14-11-101(18).
14. *Id.* § 14-11-602(c).
15. Although Georgia partnerships are treated as separate entities in many ways, the Georgia Uniform Partnership Act, based on the UNIFORM PARTNERSHIP ACT (1914) (UPA), lacks the ringing endorsement of "entity" theory that became part of the UNIFORM PARTNERSHIP ACT (1994, amended 1997) (RUPA), § 201.
16. O.C.G.A. §§ 14-11-101(18), -203(e) (Supp. 2009).
17. *Id.* §§ 14-11-101(18), -505. Although the Delaware LLC Act (DEL. CODE ANN. tit. 6, § 18-101(7)) and 2006 Rev. Unif. Ltd. Liab. Co. Act (RULLCA) § 111(a) take the position that the LLC is bound by its own LLC agreement or operating agreement, most states do not have a statutory rule on the issue. Although most practitioners would likely argue that a Georgia LLC surely should be bound by its operating agreement, judicial

authority in other states, in the absence of a statutory rule, is actually mixed. *Compare* Bubbles & Bleach, LLC v. Becker, No. 97C 1320, 1997 WL 285938 (N.D. Ill. May 23, 1997) (LLC was not bound by the arbitration clause in its operating agreement), and Mission Residential, LLC v. Triple Net Props. LLC, 654 S.E.2d 888 (Va. 2008) (similar), with Elf Atochem N. Am., Inc. v. Jaffari, 727 A.2d 286, 293 (Del. 1999) (prior to enactment of Delaware statutory rule on point, LLC held to be a party to its LLC agreement).

18. O.C.G.A. §§ 14-2-101 to -1703 (2003 & Supp. 2009).
19. See *id.* § 14-2-1408(a) (2003) (corporation "may" dissolve by filing a comparable statement with the secretary of state).
20. Some recent commentaries on charging orders include: Alan S. Gassman & Sabrina M. Moravecky, *Charging Orders: The Remedy for Creditors of Debtor Partners*, EST. PLAN., Dec. 2009, at 21; Thomas E. Rutledge, Carter G. Bishop & Thomas Earl Geu,

Foreclosure and Dissolution Rights of a Member's Creditors: No Cause for Alarm, Suffolk U. L. Sch., Legal Studies Research Paper Series, Research Paper 07-18 (May 4, 2007), available at <http://ssrn.com/abstract=948917>.

21. O.C.G.A. § 14-11-504(a) (Supp. 2009).
22. *Id.* § 14-11-504(b). The language of amended O.C.G.A. § 14-11-504(b) was derived in part from N.J. STAT. ANN. § 42:2B-45.
23. DEL. CODE ANN. tit. 6, § 18-703.
24. See Carter G. Bishop, *Fifty State Series: LLC Charging Order Statutes*, Suffolk U. L. Sch., Legal Studies Research Paper Series, Research Paper 10-03 (Jan. 25, 2010), available at <http://ssrn.com/abstract=1542244>; Amy P. Jetel, *50-State Comparison of LLC Legislation*, Am. Bar Ass'n - Sec. of Tax'n & Sec. of Real Prop., Trust and Est. Law 2007 Fall Meeting (Sept. 28, 2007) (available on Westlaw at 2007 ABATAX-CLE 0928002). See also 2006 RULLCA § 503(g).
25. O.C.G.A. § 14-11-201(b) (2003).
26. The LLC rule differs from the partnership rule. O.C.G.A. § 14-8-

6(a) (2003) defines a partnership as "an association of two or more persons to carry on as co-owners a business for profit and includes, for all purposes of the laws of this state, a limited liability partnership" (emphasis added).

27. Some states are explicit that an LLC need not be devoted to profit. See, e.g., N.C. GEN. STAT. § 57C-1-03(3) (LLC may be organized for any lawful purpose or activity, "whether or not such trade, investment, purpose, or activity is carried on for profit").
28. See DEL. CODE ANN. tit. 6, § 18-101(7).
29. See O.C.G.A. §§ 14-11-502, -503 & -1107(b) (2003 & Supp. 2009). But see *RTS Landfill, Inc. v. Appalachian Waste Sys., LLC*, 267 Ga. App. 56, 598 S.E.2d 798 (2004) (reaching the surprising conclusion that a below-market "right of first refusal and purchase option" on LLC interests was unenforceable as an unreasonable restraint on alienation of personal property).
30. See U.C.C. §§ 9-406(d), 9-408.



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