

California's New LLC Law: Next Steps for California LLCs

By Riaz A. Karamali and Didi S. Chow

On January 1, 2014, California's Beverly-Killea Limited Liability Company Act (Old Act) was superseded by the California Revised Uniform Limited Liability Company Act (New Act). The New Act includes a number of substantive changes that may adversely affect existing California limited liability companies unless they amend their operating agreements.

The New Act took effect on January 1, 2014 and is codified at Section 17701.01 et seq. of the California Corporations Code. It is based on the Revised Uniform Limited Liability Company Act (RULLCA) first promulgated in 2006 by the National Conference of Commissioners on Uniform State Laws. The New Act contains significant differences from both the Old Act and the RULLCA. The New Act applies automatically – there is no procedure to opt in or opt out – and impacts all existing California limited liability companies (LLCs) as well as all LLCs formed under the laws of California after January 1, 2014.

The basic concepts under the New Act are similar to the Old Act. However, the New Act includes a number of substantive changes that may require the members of California LLCs to review and modify their LLC operating agreements. A few of these changes are highlighted below.

Expansion of Default Rules and Mandatory Rules

For existing California LLCs, the provisions of the New Act may effectively supplant portions of existing operating agreements, as the New Act provides a more detailed set of default rules that apply when an operating agreement is silent. For example, a new default rule under the New Act requires the consent of all members of an LLC in order for the LLC to take any act outside the ordinary course of the LLC's activities. Accordingly, if an operating agreement was drafted with the intent to give the manager broad discretion with respect to business decisions but fails to specify that the manager may take actions outside of the ordinary course of business, the default rule under the New Act would arguably override the existing language in the operating agreement.

Further, the New Act also includes a number of mandatory rules that may *not* be overridden (or which may be varied only to a limited extent) by an operating agreement. These mandatory

provisions cover, among other things, fiduciary duties, information rights and organic changes such as dissolution and mergers.

Dissociation Events and Potential Impact

The New Act furnishes more detail regarding withdrawal and the resulting consequences of withdrawal (referred to as “dissociation”) of an LLC member from an LLC. The New Act sets forth certain events that automatically result in a member’s dissociation. For example, a member may be expelled as set forth in the operating agreement or as a result of a trigger event stated in the LLC agreement as causing a member’s dissociation. A member who becomes a debtor in bankruptcy is also automatically dissociated. The dissociation of a member can also change the member’s status to that of a transferee. As a consequence, such member will only have limited rights and not the more expansive statutory rights of a member. If the members of an LLC do not want the automatic dissociation provisions to be triggered, the operating agreement should specifically address the statutory provisions.

Indemnification

The Old Act provided that an operating agreement may provide for the indemnification of any person that acts on behalf of the LLC, including any manager, member, officer, employee or agent of the LLC. Under the New Act, indemnification is mandatory for any member in a member-managed LLC and any manager of a manager-managed LLC who complies with the duties set forth in the New Act. However, the New Act also provides that an operating agreement may modify or eliminate such indemnification. Under the New Act, indemnification is permitted, but not mandated for officers, employees and agents.

Next Steps

Listed above are just a few of the many changes under the New Act. Managers and members of California LLCs should conduct a detailed review of the New Act and their LLC operating agreements, particularly with respect to the default rules of the New Act, and consider whether amendments are needed to their existing operating agreements.

If you have any questions about the content of this alert, please contact the Pillsbury attorney with whom you regularly work, or the authors below.

Riaz A. Karamali (bio)
Silicon Valley
+1.650.233.4052
riaz.karamali@pillsburylaw.com

Didi S. Chow (bio)
Los Angeles
+1.213.488.7476
didi.chow@pillsburylaw.com

This publication is issued periodically to keep Pillsbury Winthrop Shaw Pittman LLP clients and other interested parties informed of current legal developments that may affect or otherwise be of interest to them. The comments contained herein do not constitute legal opinion and should not be regarded as a substitute for legal advice.

© 2014 Pillsbury Winthrop Shaw Pittman LLP. All Rights Reserved.