



**KANSAS BAR
ASSOCIATION**

TO: The Honorable Lance Kinzer
And Members of the House Judiciary Committee

FROM: William Quick
On Behalf of the Kansas Bar Association

RE: House Bill 2261 – Enacting the Revised Uniform Limited Liability Company Act (RULLCA)

DATE: February 2, 2012

Good morning, Chairman Kinzer and Members of the House Judiciary Committee. My name is William Quick and I appear on behalf of the Kansas Bar Association in opposition of H.B. 2261, enacting the Revised Uniform Limited Liability Company Act (RULLCA). This committee should not adopt RULLCA for the following seven reasons.

1. Economic Recovery is Not the Time to Tinker with Small Businesses

- a. Neither Kansas business owners nor Kansas business lawyers have expressed any concern with the existing Kansas Revised Limited Liability Company Act (the “Act”). A complete replacement of the Act with the RULLCA will result in considerable expenditures of time and expense for Kansas business owners and their attorneys to adjust to the new law, which expenditures are unnecessary and would stifle other economic opportunities for Kansas businesses.

2. RULLCA Would be a Radical Shift for Kansas

- a. RULLCA is a “revised” version of the original Uniform Limited Liability Company Act, and is based upon and substantially follows that “Uniform Act.” The Kansas legal and business community considered and REJECTED the Uniform Act when Kansas initially adopted the Delaware model as the basis for the Act. There is no compelling rationale or impetus for upending that prior deliberative work or the years of experience, expectations and precedent that have anchored to the Act since its adoption. The Kansas legislature will bear the burden of explaining and justifying this change of course to the Kansas business and legal community.
- b. Kansas has modeled its corporation and LLC laws on Delaware precedent for over 40 years. The current Act is widely understood and accepted by the Kansas business community and legal community.

- c. Kansas businesses know and expect Delaware business law practices and principles. RULLCA would force thousands of businesses to expend time, money and other resources reevaluating their operating agreements, fiduciary duties and other rights, duties and obligations under a new law. Many small businesses would likely only discover the impact of the changes after a legal issue arises.
- d. Kansas courts have experience following Delaware judicial precedent in dealing with gaps in Kansas' own business law jurisprudence. RULLCA would throw away years of Kansas (and Delaware) precedent.

3. Businesses Prefer Delaware's Legal Environment

- a. The U.S. business community has voted with its feet. Both corporations and limited liability companies organized outside of their home state's jurisdiction overwhelmingly choose Delaware law.¹
- b. The trend of businesses that form out of state choosing Delaware becomes stronger the larger a business becomes.² This suggests that the more sophisticated or capable a business is of evaluating its legal environment, the more likely it is to select Delaware law.
- c. The quality of Delaware's courts in handling business litigation is a leading factor in businesses' decisions to form in Delaware.³ Following Delaware precedent levels the playing field in Kansas's competition for LLC formations.

4. Delaware is the World Leader in Business Law

- a. The Delaware legislature routinely updates its business laws based on business feedback, current events, recent cases, and developments in *de facto* national business law (e.g., federal securities regulation, exchange rules, accounting standards). In contrast, uniform laws are updated only periodically. There was a ten year gap between the original and revised Uniform Limited Liability Company Act, and that excludes the time it takes state legislatures to enact the revisions.
- b. Delaware's judicial precedent is high quality and comprehensive. Its courts specialize in business litigation and have a high volume of nationally important business cases. In contrast, RULLCA precedent is scattered across several jurisdictions, established by unspecialized judges with general dockets, and generally involves smaller stakes.
- c. By following Delaware, Kansas leverages Delaware's huge investment in staying at the cutting edge.

¹ Bruce H. Kobayashi & Larry E. Ribstein, *Delaware for Small Fry: Jurisdictional Competition for Limited Liability Companies*, 2011 U. Ill. L. Rev. 91 (2011).

² *Id.*

³ *Id.*

5. RULLCA is Hardly Uniform

- a. RULLCA has only been adopted in six jurisdictions, none of which are major centers of business activity (*i.e.*, Idaho, Iowa, Nebraska, Utah, Wyoming, and the District of Columbia).
- b. RULLCA was completed by the Uniform Law Commissioners in 2006. Its slow adoption by states indicates it may not ultimately be widely enacted.
- c. RULLCA has been criticized by certain legal scholars for not making use of LLC provisions already widely adopted.⁴ RULLCA's drafters have often selected minority approaches that make the nation's laws *less* uniform.⁵

6. RULLCA Drifts Away from the Sweet Spot between Corporations and Partnerships

- a. RULLCA's default rules lean too heavily toward a partnership approach. For example, RULLCA would shift voting rights for member-managed LLCs from proportional interests to *per capita*.⁶ Likewise, RULLCA would shift allocation of distributions from proportional interests to equal shares.⁷ These default rules do not track with the economic realities of most businesses.

7. RULLCA Contains Controversial and Problematic Provisions⁸

- a. RULLCA's fiduciary standards are extremely convoluted. It raises the standard of care from gross negligence to ordinary negligence, *i.e.*, a reasonableness standard.⁹ However, it overlays the business judgment rule, which generally requires that fiduciaries only make rational, not necessarily reasonable, decisions, thus creating confusion. Moreover, RULLCA's non-exclusive fiduciary duties bear a striking resemblance to, but clash with, the exclusive fiduciary duties found in the Kansas Uniform Partnership Act, further adding to the confusion.
- b. RULLCA eliminates statutory agency powers common in most LLC acts and attempts to fall back on common law agency theories instead.¹⁰ However, common law agency theories are less developed in the LLC context.
- c. RULLCA raises the required vote for voluntary dissolution from a majority to unanimous approval.¹¹

⁴ Bruce H. Kobayashi & Larry E. Ribstein, *The Non-Uniformity of Uniform Laws*, 35 J. Corp. L. 327 (2009-2010).

⁵ *Id.*

⁶ RULLCA, § 407(b)(2) (2006).

⁷ RULLCA, § 404(a) (2006).

⁸ For critiques of RULLCA, see Larry E. Ribstein, *An Analysis of the Revised Uniform Limited Liability Company Act*, 3 Va. L. & Bus. Rev. 35 (2008); Kobayashi & Ribstein, *supra* n. 4; Rutheford B. Campbell, Jr., *The "New" Fiduciary Standards under the Revised Uniform Limited Liability Company Act: More Bottom Bumping from NCCUSL*, 61 Me. L. Rev. 27 (2009).

⁹ RULLCA, § 409(c) (2006).

¹⁰ RULLCA, § 404(a) (2006).

¹¹ RULLCA, § 701(a)(2) (2006).

- d. RULLCA’s operating agreement provisions, including limitations on contracting out of fiduciary duties, are convoluted and overly complex.¹²
- e. RULLCA allows involuntary judicial dissolutions of LLCs if a court finds minority member oppression by the majority.¹³ Kansas’s corporation code does not offer an equivalent remedy to minority shareholders.
- f. RULLCA’s dissociation rules are overly complex.¹⁴

For the reasons stated above, and for those expressed during my oral presentation, the Kansas Bar Association respectfully opposes H.B. 2261, enacting RULLCA.

About the Kansas Bar Association

The Kansas Bar Association (KBA) was founded in 1882 as a voluntary association for dedicated legal professionals and has more than 7,000 members, including lawyers, judges, law students, and paralegals. www.ksbar.org

¹² See RULLCA, § 110 (2006).

¹³ RULLCA, § 701(a)(5) (2006).

¹⁴ See RULLCA, § 601 (2006).