

Approved: May 11, 2012

(Date)

MINUTES OF THE HOUSE JUDICIARY COMMITTEE

The meeting was called to order by Chairperson Kinzer at 3:30 PM on Thursday, February 2, 2012 in 346-S of the Capitol.

All members were present except:
Dan Collins

Committee staff present:

Katherine McBride, Office of Revisor of Statutes
Jason Thompson, Office of Revisor of Statutes
Lauren Douglass, Kansas Legislative Research Department
Robert Allison-Gallimore, Kansas Legislative Research Department
Nancy Lister, Committee Assistant

Conferees appearing before the Committee:

Bud Burke, Advantage Metals
Ed Klumpp, Association of Chiefs of Police, Kansas Sheriffs Association, Kansas
Peace Officers Association
Professor David Walker, Drake University Law School
William Quick, Kansas Bar Association
Professor Edwin Hecker, University of Kansas Law School

Others in attendance:

See attached list.

Chairman Kinzer asked for bill introductions.

Representative Pauls introduced a bill regarding expungement in the case of child abuse victims, seconded by Chairman Kinzer and the bill was accepted without objection.

Representative Rubin introduced a bill to enact a new criminal obstruction of justice statute in Kansas, which will closely parallel the federal obstruction of justice statute with regard to destroying, altering, or shredding documents that are subpoenaed or are necessary in criminal proceedings. Representative Brookens seconded the request and the bill was accepted without objection.

Representative Patton requested a bill to amend the social hosting statute, seconded by Representative Pauls and the bill was accepted without objection.

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Chairman Kinzer opened the hearing on **HB 2470-Amending provisions concerning sales of certain scrap metal.** Katherine McBride provided an overview of the bill content.

Bud Burke testified in favor of **HB 2470** stating the bill is a result of language having been removed from *2011 HB 2312* that all of the parties had agreed to last session and it is codifying the agreement from last year. Chairman Kinzer affirmed this was agreed to in the Senate Judiciary and House Corrections and Juvenile Justice Conference Committee last year, which he was part of, and for whatever reason, it was an oversight and the language is being corrected and is consistent with what everyone had agreed to last year. (Attachment 1)

Ed Klumpp testified in favor of **HB 2470** and concurred with what Bud Burke testified to, advising the Attorney General issued an opinion, 2012-4, pointing out a problem with the wording in the 2011 Session Laws, Chapter 86 (1) (g), having to do with scrap metal dealers paying the renewal fee. The language is such that when they come up for renewal in 10 years, they have to not only pay the renewal fee, but also have to repay the original fee, which was not the intent. Mr. Klumpp requested the act be amended to strike the language “, which shall be in addition to the fee provided in subsection (e),” from subsection (g), which was in *2011 HB 2312*. (Attachment 2)

Chairman Kinzer asked Ed Klumpp to describe for the Committee what the problem is as a result of the current language in the bill. Mr. Klumpp stated the scrap metal dealers had trouble with the language, which basically said if scrap wire came in marked with the name of a utility company on the insulation, they could not accept the wire if the insulation was stripped. If the insulation was stripped they couldn't tell if it was marked, so it was agreeable to remove the language.

Representative Tietze stated she was recently listening to a radio broadcast where someone was talking about scrap metal dealers taking down driver's vehicle information when individuals brought in scrap metal to sell and because of that, many were now bringing in their scrap metal in wheelbarrows to keep their identities secret so they were unidentifiable. Ed Klumpp advised bringing in stolen wire is a problem most everywhere, but Kansas is ahead of many states as the scrap metal dealers are required to record every person's identification so Kansas doesn't really have this problem.

Representative Suellentrop offered it seems there are a lot of people from across the border in Oklahoma stealing metals in Wichita and hauling them back south, and he questions if there could be a regional compact to try and work together to stop this from happening. Ed Klumpp stated many states are enacting statutes now because this is such a big problem nationwide. Wichita is a good example because of the aircraft industry, where they use a lot of expensive metals, such as titanium. Kansas law enforcers are becoming a network among law enforcement

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investigators who specialize in metal thefts. Because of their integration with law enforcement across state lines, information is being shared about scrap metal thefts.

Representative Kuether inquired whether Kansas is gaining ground on this issue. Ed Klumpp offered headway is being made, as Kansas' thefts are not growing at the rate of other places. It used to be some cities had restrictions on what they would accept, but it was not consistent everywhere. With statewide application of the law, it ultimately limits the access thieves have to sell their stolen metals. The biggest thing is the change in the theft penalty, which increases the penalties based on the amount of damage they do rather than the amount of wire stolen.

With no further witnesses to testify, Chairman Kinzer closed the hearing on **HB 2470**.

Chairman Kinzer announced he is reopening the hearing on **HB 2261—Enacting the revised uniform limited liability company act**, as this is a continuation from one week ago, when the testimony was provided on the filing provisions associated with the act. Chairman Kinzer stated because the Committee has an expert available to testify, he welcomed Professor David Walker and asked him to explain the bill and discuss the issues that support the bill.

Professor Walker testified in support of **HB 2261**, which would enact the Revised Uniform Limited Liability Company Act (RULLCA) and repeal Kansas' present limited liability company (LLC) legislation. Professor Walker introduced himself as a teacher at Drake University Law School in Des Moines and shared he has taught for decades on business associations concentrating mostly on unincorporated entities such as partnerships, limited liability corporations, and closely-held corporations—more than publicly-held corporations, although he teaches on both. He is proud to be an active member of the Iowa Bar Association, has chaired and currently serves on the Business Law Section of the Iowa Bar, and chairs the for-profit Corporation Committee of the Iowa Bar. Since 1992, Professor Walker has served as one of Iowa's three Commissioners on Uniform State Laws and, in this capacity, has served on various drafting committees including the Uniform Limited Partnership Committee, the Model Entity Transactions Act, which Kansas adopted in 2009, and chaired the Drafting Committee for the RULLCA, which Kansas is now considering. He recently served on the Harmonization Committee, which has harmonized all of the business entity acts. He advised although he is not an expert on the act, he has looked at everything in the Act and feels it is flexible and tailored to meet people's particular preferences. (Attachment 3)

Professor Walker advised he would give a brief overview and commentary on RULLCA, speak about how **HB 2261** is modeled after Delaware's Act, and provide some information regarding Delaware's jurisprudence. He shared he had the pleasure of meeting with Kansas' Deputy Assistant Secretary of State, Ryan Kreigshauser, and understands the concerns he expressed and

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is supportive of harmonizing business law provisions dealing with the Secretary of State across all business entities. Professor Walker advised he is working with his Secretary of State, and as a member of the Business Law Section Council in Iowa, they are looking at the Model Registered Agents Act, which would unify provisions regarding registered agents for all business entities that are filing entities. By listening to the Secretary of State and including some language authorizing the use of e-mail for communications, the Council is also working on the revised acts. According to Doug Strike, Iowa's Deputy Secretary of State, his office might save as much as \$50,000 dollars a year by unifying the provisions and taking advantage of technology. The Iowa bill was drafted with the intention that each state would look at it with its Secretary of State and adapt the uniform act to local preference and practice. It was done in Nebraska and it was done in Iowa. At the request of the Kansas Secretary of State, Professor Walker drafted some language for the Corporate and Limited Liability Company (LLC) Acts unifying provisions regarding registered agents, and he hopes to continue working with the office.

Professor Walker stated the limited liability company is the entity of choice for small businesses and other organizations. Generally, LLCs are formed at two to three times the frequency that corporations are formed. The LLC offers enormous flexibility to people who want to form a company and tailor the deal just as they want. At the Uniform Law Commission in Iowa, they began to rethink the LLC act, which was first promulgated in 1996. When the Uniform Law Commission published the first LLC act within the span of seven years, between 1988, when the Internal Revenue Service (IRS) recognized the partnership tax effects for LLCs, and 1995, when the Uniform Law Commission approved its Act, 45 states had passed LLCs. There have been three generations of LLC acts. The first act was out of Wyoming in the late 70s. The first generation LLCs were those that took advantage of the revenue ruling by the IRS in 1988, where people saw they could have limited liability by partnership but tax treatment in the context of contract. People drafted statutes that plugged into the revenue ruling carefully. In 1997, the IRS changed the regulations. It considerably relaxed and made more flexible the formation and operation of LLCs. States began to make amendments in their legislation accordingly. In Iowa, they took up RULLCA in 2003, with 15 years of judicial opinions, examples of legislation in 50 states, and the benefit of practitioners from all over the country. It was exciting and an education. Commissioners from nine states were involved, as were American Bar Association (ABA) advisors representing five different sections of the ABA. There were a number of official observers, and the drafting committee drafted a very clear and up-to-date statute.

Professor Walker offered RULLCA is a modern up-to-date statute which preserves the salient, sought-after features of an LLC. It includes the presence of an LLC shield so members are not liable for the debts or obligations in tort, contract, or otherwise. It is grounded in contract. RULLCA provides three sections that address the operating agreement and questions that have

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arisen over 15 years time. It is a default statute and only applies to the extent that people do not address an issue in their operating agreement. For example, there is one section that says one cannot affect the jurisdiction of a court, cannot deny the capacity to be sued, and cannot affect the rights of third parties. In Iowa, in the first year under RULLCA, there were almost 9,000 LLCs formed. In Delaware, there were 80,000 to 90,000 LLCs formed in 2008 through 2010. In those same years, only one-third as many individuals formed corporations in Delaware.

Professor Walker expressed there were many LLCs formed by people who are not represented by lawyers. There are also LLCs that are formed by lawyers in small firms whose practices are not concentrated in business planning and transactional practice. Most lawyers are sole practitioners. The greatest mass of people practice law practice in firms of nine people or fewer, if they are not sole practitioners. Professor Walker advised some of the people who would be using this statute would be planning estates, be young lawyers representing friends, and be young people engaging in startups and entrepreneurs, where cash is low. RULLCA was a statute that was user friendly in its architecture and its provisions. Professor Walker likened it to a suit. One could spend \$2,000 for a custom suit, or go to a department store and buy a suit off the rack and get a pretty nice suit that serves the purpose. They followed the architecture, the structure-the floors- of the Revised Uniform Partnership Act, which Kansas has. Professor Walker advised the Kansas Court of Appeals turned to the Uniform Law Commission in Iowa for an understanding and instruction of the fiduciary duties: the duties of care, candor, and loyalty, which are what people expect and are found in RULLCA.

Professor Walker summarized three strong reasons for adopting RULLCA: it is a well-drafted, up-to-date statute that has been harmonized with other business entity legislation, including uniform acts Kansas has adopted; it preserves all of the essential, sought-after attributes of the LLC and is predicated on contract principles allowing members to tailor and define their deal as they want, while providing default terms many would choose, thus freeing organizers and members from the time and expense of drafting every last detail; and its structure and organization are familiar and provisions are fairly easy to locate and grasp.

Professor Walker highlighted selected provisions of RULLCA that help protect the LLC deal, including: the operating agreement; the fiduciary duties of LLC members; determining the manner in which the LLC will be managed; the authority of members; and the certificate of organization addressing the formation of an LLC. RULLCA provides a transferee of an LLC interest only obtains the economic rights to receive distributions when and if they are made, but does not have the right to participate in management or demand inspection of documents and records. RULLCA also provides that LLC members may amend the operating agreement even

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over the protest of a transferee; a dissociated member or transferee cannot “freeze the deal;” and members may alter, restrict, or even eliminate aspects of the duty of loyalty or define what is permissible or sufficient performance, and what they say will be enforceable “unless unreasonable.” RULLCA also contains current, clear provisions dealing with fundamental changes—merger, conversion, or domestication—and these provisions track and mesh with the Model Entity Transactions Act, which Kansas adopted two years ago as the Business Entity Transactions Act.

Professor Walker advised RULLCA does not contain a provision on “Series LLCs” because there was so much uncertainty, at the time of drafting, whether the IRS or U.S. Bankruptcy Courts or state courts would recognize a Series LLC as a valid means of insulating certain LLC assets from creditors of the LLC; it was simpler and safer just to form a separate LLC, just as a corporation would form a subsidiary, which would legally be separate from the parent. Some states, including Delaware and Iowa, provide for Series LLCs and the Uniform Law Commission itself provided for a Series to be utilized in the Uniform Statutory Trust Entity Act. The District of Columbia recently adopted RULLCA, and provided for Series LLCs. Iowa has the provision because it had provided for Series a decade earlier, and when Iowa’s Bar considered the issue there was testimony from at least one lawyer who utilized Series LLCs and it was useful. A number of questions continue to exist about Series LLCs and the Uniform Law Commission formed a Study Committee on Series, of which Professor Walker is a member. The Committee has learned some believe Series can serve useful purposes quite apart from the context of an investment or mutual fund where Series developed. They have also learned there are different approaches to Series LLCs. Delaware regards a Series LLC as an entity, which means it could sue and be sued, for example, raising questions about its relation to the LLC of which it is a part. The Statutory Trust Entity Act recognizes a Series trust but does not regard it as an entity. The bottom line question the Study Committee will try to answer is whether to draft provisions or a separate act creating and validating a Series LLC.

Professor Walker shared four observations about Delaware Business Entity Law with the Committee as a lawyer and Commissioner supporting RULLCA. He noted the Delaware Chancery Court is probably the most sophisticated business court in the United States and probably in the world. Their Supreme Court opinions clearly command respect. Delaware law is developed in the context and for the purpose of sophisticated, often high-end, and highly “lawyered” transactions where attention to and negotiation of detail and drafting of discreet provisions are the expectation and the assumption. Each provision is negotiated with two or three lawyers, then it is drafted, and then the drafts are reviewed, which takes time. This all entails expense, which is probably justified. Professor Walker offered most transactions are really not like that. Most people do not need high-end transactions with multiple lawyers. A professor in Pennsylvania did a study of LLCs and found the paradigm LLC had three to five members. People can pretty much do through RULLCA what they can do under Delaware law

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without having to negotiate and draft more specific contractual duties, yet still be able to customize their deal.

Professor Walker noted that Chief Justice Myron Steele, of the Delaware Supreme Court, has written and spoken up saying there should not be default fiduciary duties. What there should be are carefully negotiated contractual duties and no default fiduciary duties. This is not the law in Kansas, but it is in Delaware. There is something “off the rack” about RULLCA that allows it to be tailored and customized, but it doesn’t assume high-end transactions.

Professor Walker stated if one were to look at the Delaware LLC Act and compare the architecture structure of RULLCA to the Kansas Act, RULLCA is more user friendly. Past Chief Justice of the Supreme Court, Norman Veasey, in an opinion in the case Elf Atochem North America v. Jaffari, 727 A. 2d 286, 291 (Del. 1999) wrote: “Although business planners may find comfort in working with the Act in structuring transactions and relationships, it is a somewhat awkward document for this Court to construe and apply in this case. To understand the overall structure and thrust of the Act, one must wade through provisions that are prolix, sometimes oddly organized, and do not always flow evenly. Be that as it may, as a problem in mastering the Act as a whole, one returns to the narrow and discrete issues presented in this case.”

Professor Walker offered Delaware is a place where there have been a number of major surprises in the last thirty to forty years, which have lead to instability and unpredictability in the application of Delaware business law, corporate, and LLC law. For example, it recognized “good faith” as a fiduciary duty. Then, after ten to twelve years of litigation, the Supreme Court found “good faith” is not an independent fiduciary duty, but an aspect of the duty of loyalty and provided the meaning.

In closing, Professor Walker stated the Uniform Law Commission is about to complete a project of harmonizing and packaging in one business organization’s code, something that would bring everything the Secretary of State would want to see. The Iowa Bar will be looking at this. Professor Walker strongly expressed his support for the consideration of RULLCA and commended it to the Kansas Bar Association’s attention for consideration.

About one and a half years ago, Chairman Kinzer was in Chicago when this was first discussed. He was interested in discussing this area of the law because he had seen over the last several years- perhaps because of the economic downturn- an increase in litigations on the back end of LLCs that are struggling. The situation described in the testimony of individuals who are members of an LLC, who didn’t seek legal council for whatever reason in forming the LLC, is what he is seeing as quite common in the litigation filings. There is significant confusion, given a very cursorily drafted operating agreement, or in some instances, the complete lack of an

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operating agreement, the lack of default provisions and lots of misunderstanding as to the nature and extent of what fiduciary duties are. It has produced some results that are unfortunate for some of the litigants and has been very expensive on the back end, when, in the context of a lack of clarity, they were now trying to wind down an LLC or perhaps deal with the issue of whether one had behaved inappropriately with another. Chairman Kinzer stated although he was not emotionally invested in the Uniform Law approach or the Delaware Law approach, he did have some investment in trying to make sure Kansas law provides as much clarity as possible, particularly for unsophisticated individuals who are embarking in a business enterprise together. In instances where individuals may fail to deal with the seriousness of formation, if there is a greater amount of guidance in the statute with respect to what the effect would be of their decisions to act or not act in a given way, it would be helpful.

Chairman Kinzer thanked Professor Walker for his testimony.

William Quick testified in opposition to **HB 2261** as a corporate attorney at Poisenelli & Schugart in Kansas City as the President of the Corporation Business and Banking section for the Kansas Bar Association, and as the chair of the Limited Liability Act Subcommittee. The Subcommittee has been empanelled to review the current Act and recommend revisions to the Act, but not to recommend replacement of the Act. Mr. Quick acknowledged other Subcommittee members in the audience including Bill Matthews, an attorney with Foulston Seifken Law Firm, and the former president of the Corporation Business and Banking section of the ABA, Professor Webb Hecker, a corporate Law Professor at the University of Kansas Law School. (Attachment 4)

Mr. Quick advised Kansas has operated under the existing LLC Act for the past eleven years. At the time that Kansas enacted its current Act, the Kansas legal and business community considered, analyzed, and ultimately rejected the Uniform Limited Liability Company Act, the Act to which the revisions were made to develop the Revised Uniform Limited Company Act (RULLCA). **HB 2261** is a refinement to that Act. During these eleven years there has been an extensive amount of business activity in Kansas and people have built up their experience, expectations, precedent, and business models based on the existing Act and its continued existence in Kansas. Mr. Quick offered there are always opportunities to make improvements to the Act and the Subcommittee will be reviewing the Act and reviewing the changes Delaware has made to their LLC Act over the last couple of years. The Subcommittee will be considering other provisions that have been adopted in other states. Certainly if there are aspects of RULLCA which might make sense for Kansas, the Subcommittee would be happy to consider those as well.

Mr. Quick stated **HB 2261** would be a great error to replace the existing Act. In his opinion, if

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the existing Act was replaced with a whole new Act, there would be a great deal of opposition not only from those he has mentioned, but also from businesses at large in Kansas.

Mr. Quick stated there obviously need to be protections for small business owners, but there are also a number of business owners who use this Act on a regular basis. The existing Act does have default provisions just as RULLCA has. They come into play when people create their own LLCs, do not have attorneys involved, and do not form proper operating agreements to express their business realities. This is not a matter of adopting an act to look out after the little guy, as opposed to an act which ignores the little guy. The little guy is addressed in both. There may be a difference in how it is approached, but it has been the expectation of people for an extended amount of time.

The Committee inquired whether there were certain items of concern to the KBA that could be shared as examples of why there was opposition to the bill. Mr. Quick, having no specific examples, stated he would hope if there needs to be changes, they would be built upon the existing Act. Mr. Quick offered to defer to one of his colleagues, Professor Webb Hecker, and Chairman Kinzer invited him to address the Committee.

Professor Edwin "Webb" Hecker, stated he has been at the University of Kansas since 1972, which was also the year the Kansas Legislature decided to follow Delaware's corporation code. He served on the Drafting Committee when Kansas drafted the present LLC Act. There was a specific decision made not to follow the LLC Act but to follow the Delaware Act when the statute was revised in the late 90s, effective in the year 2000.

Professor Hecker expressed there are four things that are quite different in **HB 2261** and the current Act, and they have all been mentioned by Professor Walker. First, the agency principles- the idea whether a member or manager can go out and enter into a commercial transaction on behalf of the LLC and have that be binding on the LLC. The current law has detailed statutory provisions on that and no member can go out and bind the LLC- even if the transaction is highly extraordinary and unreasonable, there are clear statutory provisions based on the Uniform Partnership Act, which dates back to 1914. Professor Hecker offered the Uniform Partnership Act was revised over the 90s and he testified in favor of. It kept those same agency principles intact. When the Kansas LLC Act was drafted, they simply chose not to follow Delaware but cut and pasted provisions out of the Uniform Partnership Act and now have those agency provisions in the LLC Act. The Uniform Partnership Act in the revised version has been enforced in 49 of 50 states, with the exception being Louisiana. The language is uniform, and since 1914, there are tens of thousands of decisions all over the country interpreting those provisions. RULLCA is not going to have any provisions in the statute about agency law.

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RULLCA is going to let the common law develop. Professor Hecker pointed out, as Professor Walker had stated, LLCs are relatively new business organizations. People are not that familiar with how they operate, and they can operate in two different ways- one like partnerships, with all the members having managerial authority, or with managers, kind of like corporations, with centralized management. Without any statutory provisions for guidance, people are going to have to rely on lawyers and case law to develop the state agency rules for LLCs. It is going to take decades for that law to develop. It is already in our laws now, with language dating back to World War I days.

Professor Hecker's second point was regarding fiduciary duties. As Professor Walker said, the original Uniform LLC Act was based on the revised Uniform Partnership Act. It has statutory fiduciary duties, the duties of care and loyalty, which are basic duties, and then there are subsections under each. The people who drafted the Uniform Partnership Act and the original Uniform LLC Act, when they codified those duties, had a high degree of hubris, because in drafting statutory fiduciary duties, one would have to believe they are omniscient and can perfectly foresee everything that will happen in the future in order to draft the statute to cover those duties. The Kansas LLC Act, like the Kansas Corporation Act, does not have fiduciary duties. The law in Kansas on fiduciary duties is judge-made law, developed case by case, and the judge does not try to sit down and foresee what is going to happen in the next century in all these different situations. The Judge decides the case before him and the law builds up. This has worked. The problem is Kansas is not a highly populated state. For law to develop on a case by case basis, without the help of some other state, it takes a long time. This is where Delaware comes in and is why the Kansas legislature decided in 1972 and 1999, in passing the LLC Act, they were going to copy Delaware law, because not only do Kansans get the statutory law of the leading business commercial state in the country, but also got their judge-made law. It is free. We do not have to pay for it. Professor Walker also concurred with what Professor Walker had stated that the law is produced by the most sophisticated courts in the country. That law works for small businesses as well as it works for big businesses. It provides an incredible degree of rich texture to statutory law that is simply not found in the statutes.

Professor Hecker acknowledged Professor Walker, saying he wrote a 2006 article on fiduciary duties in business entities, and Professor Walker may be only one of a dozen or so people who have read the article, as it was very long. Professor Hecker stated the article was on fiduciary duties in the context of corporations, partnerships, and LLCs, and he compared and contrasted how those duties apply from one entity to another. The Supreme Court has said the statutes are based on Delaware law and therefore, in the absence of conflicting Kansas precedent, they follow Delaware decisions. In the absence of that attitude of the Supreme Court, his article would have been much shorter.

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Professor Hecker advised he had given Chairman Kinzer the KBA's Corporation Law and Practice book several weeks ago and, at the very end, there is a nod to LLCs that he wrote. It was just published this year. The previous edition was published the year immediately before Kansas adopted the present Act, so it was out of date within a year. Professor Hecker noted if RULLCA is adopted, his chapter will also be out of date within a year. If this occurs, it would be okay, as he would have more things to write about. Professor Hecker advised that he did not have a personal interest against RULLCA, but he had given to Chairman Kinzer Chapter 13 so he could see the number of Delaware cases that can be relied on in writing about the LLC law. If RULLCA is adopted, it has been around for six years and has been passed in about six states, so there is not a landslide of acceptance. The big value of uniformity is that judicial precedent transfers across state lines because the language of the statute that is being interpreted is the same. There are not many states that can be relied on to interpret ambiguous provisions in RULLCA. Of the states that have it, Minnesota, Iowa and Nebraska are mid-west states, like Kansas, and this is great except, like Kansas, they do not churn out highly specialized, highly sought-out case law the way Delaware does.

Professor Hecker stated another thing that stood out he wanted to mention regarded voting and distributions. The default rules are equality. As a teacher of partnership law, LLC law, and corporate law, he starts his teaching with partnership law-actually starting with agency- but the entities are partnership law. He tells his students Section 401b of the Revised Uniform Partnership Law provides for equal sharing of profits and equal means equal, not proportional. He tells his students if there are three partners, each one gets one third. Professor Hecker gave the example of one partner investing 10% in the partnership, the second partner invests 10% in the partnership, and the third partner invests 80%. When he asks his students how they share a \$10,000 profit, usually students will say \$1,000 goes to the first partner, \$1,000 goes to the second partner and \$8,000 goes to the third partner. He will have to tell them no, that is not equal. Equal is counterintuitive to business people. Business people are used to thinking what one invests is going to be proportional to one's return from the business. The default rule is backwards. The same thing is true on allocation of control and voting power. Everyone gets an equal vote under RULLCA, not in proportion to one's investment, which seems upside down.

Professor Hecker stated the fiduciary duties are okay, but what he finds mind boggling is in Section 10 of the bill, where one finds what the operating agreement can and cannot do to the fiduciary duties. After teaching for forty years and reading lots of business statutory law, it is confusing what one can do in terms of contracting around and out of fiduciary duties. The statute does say the operating agreement can eliminate fiduciary duties, which one cannot do under present Kansas law. One may expand the duties and restrict them, but there is no permission to eliminate them. One can eliminate them under RULLCA, provided it is not

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“manifestly unreasonable.” Professor Hecker pointed out it is a contradiction in terms people rely on fiduciary duties—loyalty and care—when they enter into these arrangements, and yet one can eliminate them if it is not “manifestly unreasonable.”

Representative Bruchman inquired of Professor Hecker, as a practicing Kansas corporate attorney who relies a great deal on Delaware’s judicial precedent, if this legislation is adopted, how it would impact the day to day practice of law and also clients in more sophisticated transactions. Professor Hecker offered he wasn’t sure he could add more than he’s said, but he personally thought it would be horrible. The new statutory language ultimately traces back to the Partnership Act but is different enough that it is highly problematic. There is no case law and no statute can answer all the questions. Professor Hecker stated the big payoff is the case law for following Delaware. He pointed out as Professor Walker made the statement that anything one can do under Delaware, one can do under RULLCA, it is equally true that anything one can do under RULLCA, one can do under Delaware law. Professor expressed it would be a disaster for business lawyers and their clients. It might bring big business to the business lawyers, as it would be a full employment Act for a while, but it wouldn’t be good for the client, as it would radically ratchet up unpredictability.

Chairman Kinzer thanked Professor Hecker for his comments. He offered Professor Walker the opportunity to make any brief closing comments.

Professor Walker stated the LLC Act that Kansas enacted was substantially changed. There were major differences between the two. The Revised Act rejected some of the Partnership Act provisions such as the quit option in Article seven. Regarding the agency principles, corporate law has utilized common law agency principles for hundreds of years, and it has not been problematic. Regarding Section 10 of the bill and the fiduciary duties and the freedom of the operating agreement to make changes, the section was substantially clarified in the harmonized version, and so it would be one that he would share with the Kansas Bar and suggested the Committee would want to look at, as it undercuts considerably the concern registered by some that it is difficult to read and apply. When reading the section, it would be clear that one cannot eliminate the duties of loyalty and care under RULLCA, but it does say certain aspects can be eliminated. In practice and business, for example in the real estate context, it is the deal that people want, and it is authorized in RULLCA. Professor Walker expressed he did not want a win-lose situation between the existing Act and RULLCA, but offered that everyone should look at the provisions, structure, and formatting of the harmonized act, as there is an advantage in the uniform approach. There is a lot of difference in the Partnership Act and the LLC Act, as far as fiduciary duties are concerned. The Partnership Act says the only fiduciary duties are care and loyalty. In contrast, RULLCA says the fiduciary duties include duties of care and loyalty. The Partnership Act, itself, has been changed in the harmonized version and the

Unless specifically noted, the individual remarks recorded herein have not been transcribed verbatim. Individual remarks as reported herein have not been submitted to the individuals appearing before the committee for editing or corrections.

Continuation Sheet

Minutes of the HOUSE JUDICIARY Committee at 3:30 PM on Thursday, February 2, 2012 in 346-S of the Capitol.

Partnership Act says the duty of loyalty is “limited to.” RULLCA does not say that the fiduciary duty is “limited to.” Professor Walker stated his appreciation for having the opportunity to testify and hoped this conversation would continue.

Chairman Kinzer thanked Professor Walker and stated it is always enjoyable to see people who know a lot about a given area and care deeply about a given area to have an opportunity to discuss it, and he hopes the Committee has found it useful.

Chairman Kinzer apologized to the Committee, stating he debated on going ahead and just introducing the harmonized version this year, to have that as the Committee’s base, but he decided not to go that route essentially to save the cost of introducing a new bill and the work that the Revisor’s office would have to do. Chairman Kinzer also noted he was thinking that the Committee would have the opportunity to have this hearing and then he would be able to get feedback from the Committee in order to determine whether they wanted to go down this road, and to the extent that there was interest, then the Committee would have the opportunity to look at the harmonization version.

Chairman Kinzer stated he would make an effort to work **HB 2121**, **HB 2253** and **HB 2473** on Monday.

The next hearing is scheduled for Monday, February 6, 2012. The meeting was adjourned at 5:23 p.m.