

New Jersey Adopts the Revised Uniform Limited Liability Company Act

On September 19, 2012, Governor Chris Christie signed into law the New Jersey Revised Uniform Limited Liability Company Act (the "Act"). The legislation had been passed almost unanimously by the New Jersey Assembly (77-1) and the New Jersey Senate (38-0). **The Act will impact every New Jersey limited liability company ("LLC").**

General Benefits of the Act. The Act will replace New Jersey's existing LLC law, which was adopted in 1993. It will provide New Jersey with authoritative analysis from the National Conference of Commissioners on Uniform State Laws, which drafted the Revised Uniform Limited Liability Company Act ("RULLCA"), the uniform law that forms the basis of New Jersey's new LLC law. Because the Act is based on a uniform law, it will provide New Jersey with case law from other jurisdictions and analysis from law reviews and professional journals. These resources will benefit LLCs and their owners (known as "members"), and the courts, in interpreting the Act. As noted below, **the Act will make significant changes in New Jersey's LLC law and eventually will apply to all New Jersey LLCs (including those formed under New Jersey's existing LLC law).**

Distributions. Under the Act, each member of an LLC will be entitled to an equal share of the profits or losses. This is a significant change in the law. Under existing law, each member is entitled to share profits or losses based on the agreed value of each member's capital contribution to the LLC, unless a different method is provided for in the LLC operating agreement. By way of example, assume member A contributes \$75,000 and member B contributes \$25,000 to an LLC. Under existing law, A would receive 75% (\$75,000/\$100,000) and B would receive 25% (\$25,000/\$100,000) of the profits. Under the new law, A and B would each receive 50% of the profits. To avoid the equal distributions provided in the Act, members of an LLC will want a written operating agreement that clearly states how they will allocate profits and losses and make cash distributions, especially when the members' capital contributions are not equal.

Voting. Unless otherwise provided in an LLC operating agreement, ordinary matters will be decided by a majority of the members, with each member having one vote, and extraordinary matters, including mergers, will be decided unanimously by the members. This is a significant change in the law. Under existing law, unless a different voting method is provided for in the LLC operating agreement, all matters are decided by a majority of the profit percentages. Therefore, if there are three members of an LLC and one of them owns 51% of the LLC and receives 51% of the profits, he has 51% of the vote and makes the decisions for the LLC. Under the new law, each member will have an equal vote. Therefore, in the prior example, the two minority members, together owning 49% of the LLC, can outvote the majority member, 2-1, and make decisions for the LLC. To avoid the equal voting provided in the Act, members of an LLC will want a written operating agreement that specifically sets forth how decisions will be made, especially when their ownership interests are not equal.

Fiduciary Duties. Under the Act, members and managers of LLCs will have newly defined fiduciary duties of care and loyalty and a covenant of good faith and fair dealing. New Jersey's existing LLC statute does not address fiduciary duties, and there are no court decisions discussing fiduciary duties with respect to New Jersey LLCs. Therefore, many existing LLC operating agreements do not address fiduciary duties. As a result, the conduct of the members and managers of these LLCs will be governed by the provisions of the Act. The Act allows aspects

of these duties to be altered and even eliminated. As a result, LLCs should review and, if necessary, amend their written operating agreements to address fiduciary duties to avoid application of the default provisions of the Act.

Resignation. Under existing law, a member is entitled to resign from an LLC and have his equity purchased by the LLC for fair value. Under the Act, a resigning member will continue to own his equity interest. He will be considered a dissociated member and continue to be entitled to receive distributions, if any, made by the LLC, but will not have any management or voting rights. Members of an LLC will want to make certain that they have a written operating agreement that addresses resignation of members, including valuation and purchase rights with respect to a resigning member's LLC equity interest, based on terms that they believe are fair to the resigning member and to the LLC and its remaining members.

Oppression. The Act provides protection for oppressed members of an LLC by providing them with rights and remedies that previously were not available under New Jersey's LLC law. These rights and remedies will be similar to those available to oppressed minority shareholders of corporations under New Jersey's Business Corporation Law. In cases of oppression, a court will be able to order a remedy other than dissolution of the LLC, such as requiring the LLC and the other members to purchase the equity interest of the oppressed member.

Indemnification. The Act will also provide for mandatory indemnification of members, managers, employees and agents of an LLC under certain circumstances, similar to New Jersey's corporate law. An LLC may alter or eliminate this mandatory indemnification in its written operating agreement. By comparison, existing LLC law merely provides discretionary indemnification as decided by the LLC on a case-by-case basis.

Operating Agreements. The Act will allow oral and implied operating agreements. In light of the significant changes made to existing New Jersey LLC law by the Act, some of which are summarized in this advisory publication, members of every New Jersey LLC should seriously consider memorializing their agreements in a written operating agreement. If an issue is not covered in an agreement, the default provisions of the Act will apply. For this reason, the Act will impact every New Jersey LLC. A written operating agreement will minimize, if not completely eliminate, disputes and surprises. Without one, an LLC and its members and managers may have to spend money proving their oral or implied agreements in court in the event of a dispute.

Conversion and Domestication. The Act will allow a corporation or other form of entity to convert to an LLC in a straightforward manner instead of being required, under existing law, to form an LLC and then merge the existing entity into the new LLC. Likewise, the Act will allow an out-of-state entity to easily domesticate to a New Jersey LLC instead of being required, under existing law, to form a New Jersey LLC and then merge the out-of-state entity into the New Jersey LLC.

Effective Date. The Act will apply to new LLCs formed after March 18, 2013 (180 days after enactment of the law), and then to all LLCs 18 months after enactment of the law (March 2014). In the meantime, existing and new LLCs can elect to be governed by the Act before these dates.

If you have any questions regarding the impact of the New Jersey Revised Uniform Limited Liability Company Act on your LLC or operating agreement, please contact Gianfranco A. Pietrafesa, Partner in Archer & Greiner's Corporate Department, at (201) 498-8559, or gpietrafesa@archerlaw.com, or another member of the firm's Corporate Department in Haddonfield, NJ at (856) 795-2121, Hackensack, NJ at (201) 342-6000, Princeton, NJ at (609) 580-3700 or Philadelphia at (215) 963-3300. Mr. Pietrafesa is the immediate past chairman of the Business Law Section of the New Jersey State Bar Association and a member of the committee that drafted the Act for adoption in New Jersey.

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