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Corporate and Business Law

Laurence V. Parker Jr.

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CORPORATE AND BUSINESS LAW

*Laurence V. Parker, Jr. **

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INTRODUCTION

This year there were a number of significant legislative changes to the Virginia Stock Corporation Act (“VSCA”) and the Virginia Limited Liability Company Act. Part I discusses certain statutory changes related to Virginia Corporations. Part II summarizes the changes to VSCA, including changes related to ratification of defective corporate acts, appraisal rights in asset sale transactions, multiple changes related to interspecies transactions, improving and making the effect of merger, domestication, and conversion language more uniform, refining the process for abandoning fundamental transactions, regulating the second step merger following a tender offer, modifying the corporate opportunity doctrine, allowing for a court to remove directors, permitting officer reliance, revising provisions related to officer and director indemnification, simplifying the voting information required in documents filed with the State Corporation Commission (“SCC”), regulating the use of forum selection clauses in governance documents, modifying cumulative voting, and modifying shareholder information rights. Part III describes the Uniform Protected Series Act, which Virginia adopted this year as an amendment to its Limited Liability Company Act. Part IV reviews a Supreme Court of Virginia case addressing the statutory safe harbor permitting an asset sale without shareholder approval and the ability to amend that safe harbor.

I. CERTAIN STATUTORY CHANGES RELATED TO CORPORATIONS

A. *Ratification*

In 2014, Delaware added section 204 to the Delaware General Corporation Law, which permits a Delaware Corporation to ratify past actions that may not have been approved in the prescribed manner under the Delaware General Corporation Law or the corporation’s articles of incorporation or bylaws.¹ This year Virginia followed suit and adopted a provision similar to Delaware.

Virginia now has enabling language in VSCA that permits a corporation to ratify any defective corporate action, which includes, “(i) any corporate action purportedly taken that is, and at the time such corporate action was purportedly taken would have been,

1. DEL. CODE ANN. tit. 8, § 204 (2017); 79 Del. Laws ch. 72, § 22 (2013).

within the power of the corporation, but is void or voidable due to a failure of authorization, or (ii) an over-issuance of shares.”² Over-issuances include issuances in excess of the authorized number of shares, or shares of an unauthorized class.³ In order to ratify a defective corporate action, the board must adopt a resolution stating:

1. The defective corporate action to be ratified and, if the defective corporate action involved the issuance of putative shares, the number and type of putative shares purportedly issued;
2. The date of the defective corporate action;
3. The nature of the failure of authorization with respect to the defective corporate action to be ratified; and
4. That the board of directors approves the ratification of the defective corporate action.⁴

Ratifying defective corporate actions that would have otherwise required shareholder approval also requires shareholder approval under the new Article 1.1 of VSCA (the new Ratification Article).⁵

A defective corporate action that required a filing with the SCC, like an amendment to the articles, a merger, conversion, domestication or dissolution, may also be ratified, and a ratification statement may then be filed with the SCC indicating such action has been ratified.⁶ A portion of the ratification statement filed with the SCC includes a description of what has happened, including: (1) the description of the defective corporate action; (2) the date of the defective corporate action; (3) how the authorization failed; and (4) “[a] statement that the defective corporate action was ratified in accordance with section 13.1-614.3. . . .”⁷ The remainder of the ratification statement is more specific to the particular defective corporate action and requires specific information: (1) if there was a filing at the time of the defective corporate action and that filing does not need to be corrected; (2) if there was a filing at the time of the defective corporate action and that filing needs to be corrected;

2. Act of Mar. 21, 2019, ch. 734, 2019 Va. Acts __, __ (codified at VA. CODE ANN. § 13.1-614.1 (Cum. Supp. 2019)).

3. *Id.* ch. 734, 2019 Va. Acts at __.

4. *Id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-614.3(A) (Cum. Supp. 2019)).

5. *Id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. §§ 13.1-614.3(C), -614.4 (C)-(D) (Cum. Supp. 2019)).

6. *Id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-614.7(A) (Cum. Supp. 2019)). Amendments to the articles, a merger, conversion, domestication, and dissolution are only some of the actions that require a filing with the SCC. *See* VA. CODE ANN. §§ 13.1-710, -720, -722.5, -722.12, -743 (Cum. Supp. 2019).

7. Ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-614.7(B)(1)-(4) (Cum. Supp. 2019)).

or (3) if there was not a filing at the time of the defective corporate action.⁸ Where a correction to a prior filing is needed or where no filing was previously made, the filing must include “a statement that a filing containing all of the information required to be included under the applicable section or sections of [VSCA] to give effect to such defective corporate action is attached as an exhibit”⁹

How the SCC interprets this somewhat vague language when accepting ratification statement filings will be interesting to see. For example, in the case of a merger, does this just require articles and a plan of merger, i.e., the documents necessary to be *filed* to bring about the defective corporate action, or does it also require the long form merger agreement, the board resolution, and the shareholder resolution needed to approve the merger originally, along with those needed to ratify it, i.e., the other documents arguably needed to *give effect* to the defective corporate action?

B. *Appraisal Rights Following Sale of Substantially All Assets*

This year Virginia significantly narrowed the availability of appraisal rights following a sale of all, or substantially all, assets. Previously, appraisal rights were available in a sale of substantially all assets if the proceeds, less reasonable reserves, were not entirely distributed to the shareholders pro rata in accordance with their shares within one year.¹⁰ Now, appraisal rights are only available if a corporation consummates a sale of substantially all assets and that transaction is an interested transaction.¹¹ In this case an “interested transaction” is a sale of all or substantially all assets with an “interested person.”¹² For purposes of appraisal rights, “interested person” means a person who, except in the case of a tender offer within the last year, holds twenty percent of the voting power, has the power to elect more than twenty-five percent of the directors of the corporation, or is a senior executive officer or

8. *Id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-614.7(C)(1)–(3) (Cum. Supp. 2019)).

9. *Id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-614.7(C)(3) (Cum. Supp. 2019)).

10. VA. CODE ANN. § 13.1-730(A)(3) (Repl. Vol. 2016).

11. Ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. § 13.1-730(A)(3) (Cum. Supp. 2019)).

12. *Id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-729 (Cum. Supp. 2019)).

director receiving a benefit not generally available to shareholders (excluding certain employment and/or retirement benefits put in place separate from the transaction, similar to what the officer had in place before the transaction or board position with the acquirer).¹³

C. *Interest Holder Liability, Amendments, Mergers, Domestications, and Conversions with Eligible Entities*

Significant changes were made throughout VSCA to define the parameters of a Virginia corporation's ability to engage in interspecies transactions, including amendments to articles of incorporation, mergers, conversions, and domestications. The "eligible entities" that may be parties to these transactions, such as domestic or foreign corporations, nonstock corporations, partnerships, limited liability companies, limited partnerships, or business trusts have not changed,¹⁴ but language was added throughout VSCA to address issues that may arise in connection with these interspecies transactions.

An amendment to a corporation's articles of incorporation can include "new interest holder liability," a partnership-like concept where liability is imposed on a shareholder by virtue of the amendment, but only if each shareholder signs a written consent to become subject to the new interest holder liability.¹⁵ This new interest holder liability only applies with respect to liabilities that arise after the date of the amendment, and an amendment does not discharge any prior interest holder liabilities.¹⁶

New sections 13.1-718(I), 13.1-722.3(7), and 13.1-722.11(B) deal with new interest holder liability incurred in a merger, domestication, or conversion similar to the way the amendment provisions deal with this issue.¹⁷ Each shareholder who becomes bound by a new interest holder liability by virtue of a merger, domestication,

13. *Id.* ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. § 13.1-729 (Cum. Supp. 2019)).

14. *Compare id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-603 (Cum. Supp. 2019)), *with* VA. CODE ANN. § 13.1-603 (Repl. Vol. 2016).

15. Ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. § 13.1-707(E)-(F) (Cum. Supp. 2019)).

16. *Id.* ch. 734, 2019 Va. Acts at __; *id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. §§ 13.1-721(C), -722.7:1(C), -722.13(C)-(D) (Cum. Supp. 2019)).

17. Ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. §§ 13.2-718(I), -722.3(7), -722.11(B) (Cum. Supp. 2019)).

or conversion, must sign a written consent to be bound by that new interest holder liability.¹⁸ New sections 13.1-721(C), 13.1-722.7:1(C), and 13.1-722.13(C) to (D), also clarify that following a merger, domestication, or conversion, new interest holder liability only applies with respect to liabilities that arise after the date of the transaction, and a transaction does not discharge any prior interest holder liabilities.¹⁹

D. *Effect of Merger, Domestication, and Conversion*

Significant changes were made to VSCA's language regarding the effect of merger. Notably, with regard to assignment of contracts, the language arguably forbidding a transfer of a contract by merger where the "assignment would violate a contractual prohibition on assignment by operation of law" was deleted, and language was added clarifying that a merger is not a transfer.²⁰ Now section 13.1-721(A)(3) reads: "[a]ll property owned by, and every contract right possessed by, each domestic or foreign corporation or eligible entity that merges into the survivor is vested in the survivor without transfer, reversion, or impairment."²¹ Similarly, language was added making clear that the survivor retains all rights previously held, and all other rights, privileges, franchises, and immunities held by the merging corporations become rights, privileges, franchises, and immunities of the survivor.²² This change may be an attempt to further clarify that a merger does not bring about a transfer by operation of law and the General Assembly's intent to overturn caselaw that suggested that certain government-issued franchises may not transfer via merger.²³

18. *Id.* ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. §§ 13.1-718(I), -722.11(7), -722.11(B) (Cum. Supp. 2019)).

19. *Id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. §§ 13.1-721(C), -722.7:1(C), -722.13(C)-(D) (Cum. Supp. 2019)).

20. *Id.* ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. § 13.1-721 (Cum. Supp. 2019)).

21. *Id.* ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. § 13.1-721(A)(3) (Cum. Supp. 2019)).

22. *Id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-721(A)(9)-(10) (Cum. Supp. 2019)); *see also id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-721(F) (Cum. Supp. 2019)) (stating that a merger does not trigger a dissolution, liquidation, or winding up of the nonsurviving corporation).

23. *See, e.g., Metro Van & Storage Co. v. Commonwealth*, 216 Va. 544, 221 S.E.2d 127 (1976) (holding that a merger caused the nonsurviving entity to cease to legally exist, requiring revocation of a government-issued certificate).

A new section addressing the effect of a domestication and the revisions to the effect-of-conversion statute are largely identical to section 13.1-721(A)(3), except the word “transfer” is strangely omitted from the effect-of-conversion statute.²⁴

E. *Abandonment of Fundamental Transactions*

Virginia modified VSCA provisions regarding abandonment of a merger before the effective time designated in the certificate of merger,²⁵ and adopted similar abandonment provisions with respect to amendments to articles of incorporation,²⁶ the plan of domestication,²⁷ and the plan of conversion.²⁸ A merger can be abandoned before the effective time designated in the certificate of merger if a statement signed by all parties is filed prior to the effective time.²⁹ This statement must include the name of the corporation, the date of the original filing, the original requested effective date, and a statement that the transaction is being abandoned.³⁰ A similar filing can be made to abandon amendments to articles of incorporation, conversions, or domestications.³¹

F. *Merger Following a Tender Offer*

Virginia rewrote VSCA section 13.1-718(G), which had permitted a merger without a shareholder vote following a tender offer.³² The target corporation no longer has to be a public corporation, at

24. Compare ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-722.7:1 (Cum. Supp. 2019)) (“All property owned by, and every contract right possessed by, the domesticating corporation are the property and contract rights of the domesticated corporation without transfer, reversion, or impairment.”), with ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. § 13.1-722.13 (Cum. Supp. 2019)) (“All property owned by, and every contract right possessed by, the converting entity remains the property and contract rights of the converted entity without reversion or impairment.”).

25. *Id.* ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. § 13.1-721.1 (Cum. Supp. 2019)).

26. *Id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-712.1 (Cum. Supp. 2019)).

27. *Id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-722.6(B)–(C) (Cum. Supp. 2019)).

28. *Id.* ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. § 13.1-722.12:1(B)–(C) (Cum. Supp. 2019)).

29. *Id.* ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. § 13.1-718(G) (Cum. Supp. 2019)).

30. *Id.* ch. 734, 2019 Va. Acts at __.

31. See *supra* notes 26–28 and accompanying text.

32. VA. CODE ANN. § 13.1-718(G) (Repl. Vol. 2016).

least under VSCA.³³ Several of the previous conditions to not holding a shareholder vote to consummate a merger following a tender offer were rewritten so a purchaser may tender to purchase all shares (other than those held by the purchaser, its parent, subsidiaries, or by the target corporation, which do not need either to be purchased or to receive merger consideration), and if: (1) it acquires enough shares (including those it or its parent or subsidiaries previously held) to approve a merger; (2) the merger offers the same consideration as is offered in the tender offer; and (3) the merger will be consummated promptly following the offeror's acquisition of a sufficient number of shares via the tender offer.³⁴ Two new conditions were added: (1) the offer must be held open for ten business days; and (2) the offeror must purchase all tendered shares that are not withdrawn.³⁵

G. *Limitations on the Corporate Opportunity Doctrine*

Virginia added express enabling language to VSCA that permits a corporation, in its articles of incorporation, to eliminate the duty of a director, or any other person, to present business opportunities to the corporation.³⁶ For these concepts to apply to officers, the board must approve its application to the specific officer, and the board may limit the application of the provision to one or more officers.³⁷

H. *Court Removal of Directors*

Virginia added section 13.1-681.1 to VSCA, which allows a corporation or shareholders in a derivative proceeding to seek the removal of a director if the court finds that:

- (i) the director engaged in fraudulent conduct with respect to the corporation or its shareholders, grossly abused the position of director, or intentionally inflicted harm on the corporation and
- (ii) considering the

33. Ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. § 13.1-718(G) (Cum. Supp. 2019)) (deleting “[t]he corporation is a public corporation”). Whether a tender offer is feasible under state and federal securities laws is beyond the scope of this Article.

34. *Id.* ch. 734, 2019 Va. Acts at __.

35. *Id.* ch. 734, 2019 Va. Acts at __.

36. *Id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-619(B)(5) (Cum. Supp. 2019)).

37. *Id.* ch. 734, 2019 Va. Acts at __.

director's course of conduct and the inadequacy of other available remedies, removal would be in the best interest of the corporation.³⁸

I. *Officer Reliance*

Section 13.1-694(B) was added to VSCA to allow officers the ability to rely on others in a similar, but not identical, fashion to the way directors may rely on others under section 13.1-690.B.³⁹ Officers, but not directors, may rely on responsibilities properly delegated to or information, opinions, reports, or statements made by one or more employees "whom the officer believes in good faith to be reliable and competent" in performing the responsibilities delegated or providing the applicable information, opinions, reports, or statements.⁴⁰ Like a director, an officer may rely on information, opinions, reports, or statements from legal counsel, public accountants, or other persons retained by the corporation.⁴¹ However, the officer may only do so if he believes in good faith that the matters are within the person's professional or expert competence, similar to those directors or those to which the particular person merits confidence, which is different from the director's standard.⁴²

J. *Director and Officer Indemnification*

While it was previously clear that for a Virginia corporation, an amendment to its articles of incorporation or bylaws could not alter the corporation's obligation to indemnify for matters arising prior to the amendment, revisions to VSCA this year made it clear that board or shareholder resolutions also cannot alter the corporation's obligation to indemnify for matters arising prior to the adoption of those resolutions.⁴³ In addition, subsection E was added to regulate

38. *Id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-681.1(A) (Cum. Supp. 2019)).

39. *Id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-694(B) (Cum. Supp. 2019)).

40. *Id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-694(B)(1)–(2) (Cum. Supp. 2019)).

41. *Id.* ch. 734, 2019 Va. Acts at __.

42. *Id.* ch. 734, 2019 Va. Acts at __.

43. *Id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-704(D) (Cum. Supp. 2019)). Delaware adopted a similar provision in title 8, section 145(g) of the Delaware General Corporation Law in 2009 after *Schoon v. Troy Corp.*, 948 A.2d 1157 (Del. Ch. 2008). See DEL. CODE ANN. tit. 8, § 145(g) (2019).

the indemnification obligations of the survivor of a merger with respect to officers and directors of the non-surviving entity: namely, unless expressly provided otherwise, the survivor is obligated to indemnify the nonsurviving entity's officers and directors as provided in the nonsurviving entity's articles of incorporation and bylaws and not under the survivor's articles of incorporation and bylaws.⁴⁴

K. *Voting Information in Filed Documents*

Virginia revised provisions of VSCA to simplify and harmonize how shareholder approvals are described in various documents filed with the SCC, including amendments to articles of incorporation, amended and restated articles of incorporation, articles of merger, articles of domestication, articles of conversion, or articles of dissolution.⁴⁵ In all instances, filings now require a simple statement that the shareholders approved the action either by unanimous consent or in the manner required by the applicable article, versus the previous requirement, in some instances, to list the total number of shares entitled to be cast by each voting group and either the total votes cast for the transaction by each voting group, or a statement that the votes cast in favor by each voting group were sufficient for approval by that voting group.⁴⁶

L. *Forum Selection*

Virginia expanded, or at least clarified, the scope of claims that can be covered in a forum selection bylaw to include all claims that may be brought under the "internal affairs doctrine"; all claims that may be brought under VSCA; a corporation's articles or bylaws, not just those against the corporation or current or former directors or officers; and claims brought by shareholders regarding any breach of duty.⁴⁷ The language also clarified that a bylaw may

44. *Id.* ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. § 13.1-704(E) (Cum. Supp. 2019)).

45. *Id.* ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. §§ 13.1-710(A)(5), -710(A)(5), -711(C)(6)–(8), -720(A)(3), -722.5(A)(4), -722.12(A)(4), -743(A)(3) (Cum. Supp. 2019)).

46. *Id.* ch. 734, 2019 Va. Acts at __.

47. *Id.* ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. § 13.1-624(C)(2) (Cum. Supp. 2019)).

not confer jurisdiction on any court that did not already have jurisdiction over such claim. So, for example, a forum selection clause requiring all claims to be adjudicated in federal district court, would not always be enforceable as written.⁴⁸ If a bylaw provides jurisdiction in a Virginia court that does not have personal or subject matter jurisdiction, the claim may be brought in another court in the Commonwealth that does have personal and subject matter jurisdiction, even if not specified in the bylaw.⁴⁹ Finally, a provision in the articles of incorporation or bylaws cannot prohibit an internal corporate claim from being brought in Virginia courts or mandate that such a claim be determined by arbitration.⁵⁰

M. *Cumulative Voting*

Cumulative voting for directors, even if authorized by the articles of incorporation or bylaws, is not permitted unless the meeting notice or proxy statement accompanying the notice states conspicuously that cumulative voting will be permitted.⁵¹

N. *Shareholder Information Rights and Confidentiality Obligations*

Virginia corporations may impose reasonable restrictions on the confidentiality, use, or distribution of the subset of records that a shareholder is entitled to receive only if he or she (1) has been a shareholder for more than six months or owns more than five percent of the outstanding shares, (2) makes a demand in good faith and for a proper purpose, and (3) in the demand describes the requested documents with reasonable particularity.⁵² Similarly, a Virginia court can impose reasonable restrictions on the confidentiality, use, or distribution of the same category of records.⁵³ Fi-

48. See *id.* ch. 734, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-624(D) (Cum. Supp. 2019)).

49. *Id.* ch. 734, 2019 Va. Acts at __.

50. *Id.* ch. 734, 2019 Va. Acts at __.

51. *Id.* ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. § 13.1-669 (Cum. Supp. 2019)) (deleting clause giving shareholders the right to opt into cumulative voting outside of the meeting notice).

52. *Id.* ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. § 13.1-771(D)–(E) (Cum. Supp. 2019)).

53. *Id.* ch. 734, 2019 Va. Acts at __ (codified as amended at VA. CODE ANN. § 13.1-773(C) (Cum. Supp. 2019)).

nally, a court may order that a corporation pay a shareholder's attorneys fees and other expenses if it determines the corporation imposed unreasonable restrictions on the confidentiality, use, or distribution of demanded records, or refused inspection without a reasonable basis.⁵⁴

II. CERTAIN STATUTORY CHANGES RELATED TO LIMITED LIABILITY COMPANIES

A. *Series LLCs*

In the 2019 General Assembly session, Virginia adopted its version of the Uniform Protected Series Act (the "Series LLC Act").⁵⁵ Most laws passed in the 2019 General Assembly session became effective July 1, 2019; however, the Series LLC Act will not become effective until July 1, 2020.⁵⁶ The delayed effective date is likely to give practitioners more time to understand the Series LLC Act and to give the SCC more time to study how it will accept filings under the Series LLC Act. The Series LLC Act roughly tracks the organization of the Uniform Protected Series Act:

- Sections 13.1-1088 to -1094 correspond to Article 1 of the Uniform Protected Series Act (including Definitions, Nature, Powers, Duration, and Governing Law);

- Sections 13.1-1095 to -1099 correspond to Article 2 of the Uniform Protected Series Act (Protected Series Designation and Amendment, Name, Registered Office and Registered Agent, Service of Process, Notice or Demand, and Effectiveness of Notice);

- Sections 13.1-1099.2 to -1099.6 correspond to Article 3 of the Uniform Protected Series Act;

- Sections 13.1-1099.7 to -1099.10 correspond to Article 4 of the Uniform Protected Series Act;

54. *Id.* ch. 734, 2019 Va. Acts at __.

55. Act of Mar. 19, 2019, 2019, ch. 636, 2019 Va. Acts __, __ (codified at VA. CODE ANN. §§ 13.1-1088 to 1099.27 (Cum. Supp. 2019)); *see also* Nat'l Conference of Comm'rs on Unif. State Laws 2017, UNIF. PROTECTED SERIES ACT, <https://www.uniformlaws.org/HigherLogic/System/DownloadDocumentFile.ashx?DocumentFileKey=2ddffb95-cb77-2bfb-f952-bdc260051563&forceDialog=0> [<https://perma.cc/N4XE-Y5LS>].

56. Ch. 636, 2019 Va. Acts at __.

- Sections 13.1-1099.11 to -1099.13 correspond to Article 5 of the Uniform Protected Series Act;
- Sections 13.1-1099.14 to -1099.20 correspond to Article 6 of the Uniform Protected Series Act;
- Sections 13.1-1099.21 to -1099.24 correspond to Article 7 of the Uniform Protected Series Act; and
- Sections 13.1-1099.25 to -1099.27 correspond to Article 8 of the Uniform Protected Series Act.⁵⁷

By rough analogy, a “Series LLC” is a Virginia limited liability company that as a parent entity (a Series Limited Liability Company under the Series LLC Act)⁵⁸ can form subsidiary limited liability companies (“Protected Series” under the Series LLC Act)⁵⁹ that are treated as separate entities for purposes of liability and the allocation of economic rights but that are treated as part of the parent for other purposes (like annual state filing fees).⁶⁰ A Series LLC can house multiple Protected Series within one entity that for state law purposes at least are very similar to separate subsidiaries as it relates to liability.⁶¹ The members of the Series LLC can own differing percentages of each Protected Series, and each Protected Series is a separate tax partnership.⁶² The advantages of forming a Series LLC over an actual subsidiary LLC are the lack of a separate entity fee and filing requirements for each Protected Series and more flexibility as to some of the limited liability company formalities associated with managing separate entities. The disadvantages include the complexity and uncertainty as to the tax treatment of Series LLCs and their Protected Series, very specific

57. See *supra* note 55.

58. Ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1002 (Cum. Supp. 2019)).

59. *Id.* ch. 636, 2019 Va. Acts at __.

60. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1089 (Cum. Supp. 2019)).

61. See Jay Adkisson, *Understanding the Protected Series Act: Liability Limitations and Claims*, FORBES (Oct. 21, 2018, 12:38 PM), <https://www.forbes.com/sites/jayadkisson/2018/10/21/understanding-the-protected-series-act-liability-limitations-and-claims/#bfc358946ad6> [<https://perma.cc/57WD-JBQM>].

62. See ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. §§ 13.1-1089, -1099(A), -1099.5(C) (Cum. Supp. 2019)); see also Terence Floyd Cuff, *Delaware Series LLCs and Transactional Practice—Part I*, 38 REAL EST. TAX’N 118, 120–21, 124 (2011); Allen Sparkman, *Tax Aspects of Series LLCs*, BUS. L. TODAY (Feb. 28, 2013), https://www.americanbar.org/groups/business_law/publications/blt/2013/02/03_sparkman/ [<https://perma.cc/K472-N7RX>].

asset-based record keeping requirements,⁶³ the inability to sell a Protected Series, the inability to merge into another entity, and the inability to engage in any transaction where the result is separation from its parent Series LLC (except a merger with a second Series LLC where the second Series LLC is the survivor).⁶⁴

It is important to note that the National Conference of Commissions on Uniform State Laws designed the Uniform Protected Series Act to function in concert with the applicable state's Limited Liability Company Act, so for key provisions it "extrapolates" from the underlying Limited Liability Company Act.⁶⁵ In other words, the Uniform Protected Series Act draws analogies to the Limited Liability Company Act so, for example, a Protected Series is treated as if it were a separate limited liability company.⁶⁶ Since a Series LLC is an entirely new form of business entity and has the potential to be much more complicated than other entity forms, some of the more routine provisions of the Series LLC Act, like the definitions, the nature of a protected series, the powers and duration of a protected series, and the governing law, are more important than usual.

1. Definitions, Nature, Powers, Duration, Governing Law, Non-Waivable Provisions of the Operating Agreement, and Limitations on the Operating Agreement

Key definitions include "associated asset," "associated member," "non-associated asset," "protected series," "series limited liability company," and "protected series membership interest." An "associated asset" is an asset that has been associated with a Protected Series by satisfying the record keeping requirements in section 13.1-1099.2 of the Series LLC Act.⁶⁷ This concept is key to protecting an asset from vertical creditors of the parent Series LLC or horizontal claims by creditors of other Protected Series LLCs parented by the same Series LLC.⁶⁸

63. See Cuff, *supra* note 62, at 119–20.

64. UNIF. PROTECTED SERIES ACT, *supra* note 55, at § 104(6) cmt.

65. *Id.* at Prefatory Note pt. 6(A).

66. *Id.*

67. Ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1088 (Cum. Supp. 2019)).

68. See *id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.10(B) (Cum. Supp. 2019)).

An “associated member” is a member of a Series LLC who has a protected series membership interest in a Protected Series.⁶⁹ This is one of the most important concepts in the Series LLC Act, allowing the members of the Series LLC to have varying economic rights in the Protected Series.⁷⁰ For example, a Series LLC may have varying ownership across the parent Series LLC and its subsidiary Protected Series similar to the table below:

| Members | Ownership In Series LLC | Ownership In Protected Series-1 | Ownership In Protected Series-2 | Ownership In Protected Series-3 |
|----------|-------------------------|---------------------------------|---------------------------------|---------------------------------|
| Member A | 33.33% | 20% | 40% | 0% |
| Member B | 33.33% | 40% | 40% | 50% |
| Member C | 33.33% | 40% | 20% | 50% |

Importantly, you cannot have a member of a Protected Series who is not also a member of the parent Series LLC.⁷¹ As you might expect, a nonassociated asset is an asset that is not associated with either the Series LLC or any Protected Series.⁷² As discussed above, a “protected series” is a “person” in the legal sense “established under [section] 13.1-1095” of the Series LLC Act;⁷³ roughly similar to a subsidiary of its Series LLC parent. A Protected Series is separate from its Series LLC parent and has the capacity to contract in its own name, to sue and be sued in its own name, and the like.⁷⁴ In addition to personhood, the Protected Series has all other powers of a Virginia limited liability company, except that it ceases to exist when the parent Series LLC ceases to exist (so, except in the case of a merger, it cannot exist separate from its Series LLC parent), it cannot be a member of its own parent Series LLC, and

69. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1088 (Cum. Supp. 2019)); *id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.3 (Cum. Supp. 2019)).

70. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. §§ 13.1-1094(14)(2) -1099.3, -1099.4(A), -1099.5(C) (Cum. Supp. 2019)).

71. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.3(A) (Cum. Supp. 2019)).

72. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1088 (Cum. Supp. 2019)).

73. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1002 (Cum. Supp. 2019)).

74. *See id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. §§ 13.1-1089 to -1090 (Cum. Supp. 2019)).

it cannot establish its own subsidiary Protected Series.⁷⁵ Finally, “Series limited liability company” is a Virginia limited liability company with at least one protected series.⁷⁶ So, until a Series LLC forms at least one Protected Series, it is no different from any other Virginia limited liability company.

To give the greatest chance that the allocation of vertical liability between the Series LLC and its Protected Series and horizontal liability between the various Protected Series parented by a Series LLC are respected, the Series LLC Act is very specific about how the common law “internal affairs” doctrine should apply.⁷⁷ The Series LLC Act specifies that Virginia law governs the internal affairs of a Protected Series.⁷⁸ Since a Protected Series is a new concept, the Series LLC Act goes on to provide that its internal affairs include relations between a Series LLC and its various Protected Series; a Protected Series and its associated members; relations between the associated members of a Protected Series, relations among the Protected Series, its manager, its associated members, or associated member assignees (analogous to an assignee under section 13.1-1039(A)); the rights and duties of the manager of a Protected Series; governance of the Protected Series; and the process to become an associated member of a Protected Series.⁷⁹ Virginia law governs the relationship between a Series LLC and its Protected Series, its members, the members and managers of its Protected Series, assignees of the Series LLC and of the associated members of its Protected Series.⁸⁰ Virginia law governs the liability of a manager, protected series manager, member, associated member, assignee, associated member assignee, or a Protected Series, in such capacities, for any debt or liability of another Protected Series.⁸¹ Virginia law governs the liability of a Series LLC for its Protected Series solely because its Protected Series was

75. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1090 (Cum. Supp. 2019)).

76. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1002 (Cum. Supp. 2019)).

77. *See id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1091 (Cum. Supp. 2019)).

78. *Id.* ch. 636, 2019 Va. Acts at __.

79. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1091(1) (Cum. Supp. 2019)).

80. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1091(2) (Cum. Supp. 2019)).

81. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1091(3) (Cum. Supp. 2019)).

formed or modified, by acting as its manager, having a Protected Series act as its manager or owning an interest in a Protected Series.⁸² Finally, Virginia law governs the liability of a Protected Series arising from the Protected Series being a Protected Series of its parent Series LLC, acting as a manager of its Series LLC or any other Protected Series, being owned by its Series LLC.⁸³ The governing law provisions are reinforced by section 13.1-1092, which provides that the Series LLC's operating agreement governs the internal affairs of the Series LLC and its Protected Series.⁸⁴

Unlike in a typical limited liability company, where the freedom of contract reigns,⁸⁵ a Series LLC's operating agreement is subject to very specific nonwaivable provisions of the Series LLC Act. According to the Series LLC Act:

- A. An operating agreement shall not vary the effect of:
 1. Section 13.1-1093 (listing non-waivable provisions);
 2. Section 13.1-1089 (nature of protected series);
 3. Subsection A of § 13.1-1090 (powers and duration of protected series);
 4. Subsection B of § 13.1-1090 to provide a protected series a power in addition to the powers provided to a limited liability company under the other articles of this chapter;
 5. The limitations stated in subsection C or D of § 13.1-1090;
 6. Section 13.1-1091 (governing law);
 7. Section 13.1-1092 (relation of operating agreement, this article, and the other articles of this chapter);
 8. Section 13.1-1094 (rules for applying other articles of this chapter to specified provisions of this article);
 9. Section 13.1-1095 (protected series designation; amendment), except to vary the manner in which a limited liability company approves establishing a protected series;
 10. Section 13.1-1096 (name);
 11. Section 13.1-1099.2 (associated assets);

82. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1091(4) (Cum. Supp. 2019)).

83. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1091(5) (Cum. Supp. 2019)).

84. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1092 (Cum. Supp. 2019)).

85. *See* VA. CODE ANN. § 13.1-1001.1(C) (Repl. Vol. 2016).

12. Section 13.1-1099.3 (associated members);
 13. Subsection A or B of § 13.1-1099.4 (protected series membership interests);
 14. Subsection C, F, or G of § 13.1-1099.5 (management);
 15. Section 13.1-1099.7 (limitations on liability), except to decrease or eliminate a limitation of liability stated in § 13.1-1099.7;
 16. Section 13.1-1099.8 (claim seeking to disregard limitation of liability);
 17. Section 13.1-1099.9 (remedies of judgment creditor of associated member or protected series assignee);
 18. Section 13.1-1099.10 (enforcement of claim against non-associated asset);
 19. Subdivisions 1, 4, and 5 of § 13.1-1099.11 (events causing the dissolution of protected series);
 20. Section 13.1-1099.12 (winding up dissolved protected series; cancellation), except to designate a different person to manage winding up;
 21. Section 13.1-1099.13 (waiver of cancellation upon dissolution; reinstatement of series limited liability company);
 22. Sections 13.1-1099.14 through 13.1-1099.20 (merger);
 23. Sections 13.1-1099.21, 13.1-1099.22, and 13.1-1099.23 (foreign series LLCs);
 24. Sections 13.1-1099.25 (uniformity and construction) and 13.1-1099.26 (effect on certain actions); or
 25. A provision of this article pertaining to:
 - a. A registered office or registered agent; or
 - b. The Commission, including provisions pertaining to records authorized or required to be delivered to the Commission for filing under this article or chapter.
- B. An operating agreement shall not unreasonably restrict the duties and rights under § 13.1-1099.6 but may impose reasonable restrictions on the availability and use of information obtained under § 13.1-1099.6 and may provide appropriate remedies, including liquidated damages, for a breach of any reasonable restriction on use.⁸⁶

86. Ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1093 (Cum. Supp. 2019)).

These provisions are nonwaivable because a Series LLC, its powers, its governing law, the nature of its interests, and the vertical and horizontal liability protection under state law are all interdependent and permitting the modification of these provisions would, at best, incredibly complicate the interpretation of Series LLC operating agreements and, at worst, defeat the purpose of the Series LLC in the first place.

2. Protected Series Designation and Amendment, Name, Registered Office and Registered Agent, Service of Process, Notice or Demand, and Effectiveness of Notice

Section 13.1-1095 of the Series LLC Act provides that any Virginia limited liability company may establish a Protected Series by unanimous consent of the Members;⁸⁷ however, the unanimous consent requirement can be modified by the Company's operating agreement.⁸⁸ This section also addresses the filing requirements for the series designation and the way in which a series designation can be amended.⁸⁹ A series designation functions similarly to the articles of organization for an LLC on behalf of the Protected Series—it gives birth to the Protected Series, defines its name, and the principal office address.⁹⁰ However, the registered agent must be the registered agent for the parent Series LLC that formed the Protected Series.⁹¹

Any Protected Series must include specific identifiers in its name, either “protected series,” or the abbreviations “P.S.” or “PS.”⁹² In addition, the Protected Series must include its parent Series LLC's name in the Protected Series name.⁹³ So the naming convention could be as follows:

87. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1095(A) (Cum. Supp. 2019)).

88. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1093(A)(9) (Cum. Supp. 2019)).

89. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1095(B) (Cum. Supp. 2019)).

90. *Id.* ch. 636, 2019 Va. Acts at __.

91. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1097(A) (Cum. Supp. 2019)).

92. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1096(B)(2) (Cum. Supp. 2019)).

93. *Id.* ch. 636, 2019 Va. Acts __ (codified at VA. CODE ANN. § 13.1-1096(B)(1) (Cum. Supp. 2019)).

SERIES LLC NAME: Newco, LLC

PROTECTED SERIES NAME: Newco, LLC, PS 1

To keep service and notice simple, sections 13.1-1098 and -1099 provide that service upon or notice to the parent Series LLC or its registered agent is service or notice to each of its subsidiary Protected Series.⁹⁴ This was intended to avoid disputes about whether or not service on a Protected Series was effective.⁹⁵

3. Associated Assets, Associated Members, Protected Series Membership Interests, Management, and Rights of Person Not Associated Member of Protected Series to Information Concerning Protected Series

The associated assets and associated member provisions are the guts of the Protected Series LLC Act. The sections dealing with associated assets defines the universe of assets “owned” by a Protected Series and thus reachable by creditors of that Protected Series under state law.⁹⁶ This section also defines the universe of assets “owned” by a parent Series LLC and thus reachable by creditors of the Series LLC under state law.⁹⁷ For an asset to be an “associated asset” of a Protected Series, the Protected Series must: create and maintain records that identify the asset and distinguish it from other assets of the Protected Series, determine the parent Series LLC, or other Protected Series; determine when and from whom the Protected Series acquired the asset; and, if the asset came from the Series LLC or another Protected Series, determine the consideration paid.⁹⁸ Similar record keeping requirements apply to the parent Series LLC with regard to its associated assets.⁹⁹ The record keeping requirements are important because any asset that is not an associated asset becomes a non-associated asset, reachable by all creditors of either the Series LLC or its Protected

94. *Id.* ch. 636, 2019 Va. Acts __ (codified at VA. CODE ANN. §§ 13.1-1098, -1099 (Cum. Supp. 2019)).

95. *See id.* ch. 636, 2019 Va. Acts at __.

96. *See id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. §§ 13.1-1099.2, -1099.10 (Cum. Supp. 2019)).

97. *See id.* ch. 636, 2019 Va. Acts at __.

98. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.2(A)–(B) (Cum. Supp. 2019)).

99. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.2(C) (Cum. Supp. 2019)).

Series, and the burden of proving an asset is an associated asset rests with the applicable Series LLC or Protected Series.¹⁰⁰

The concept of “associated members” is similarly critical to a Protected Series. This concept allows a person, if a member of the parent Series LLC, to be associated with the subsidiary Protected Series as provided in the operating agreement of the Series LLC, or a procedure established by that document.¹⁰¹ It also allows for differing percentages to be held in each subsidiary Protected Series, as described above.¹⁰²

Section 13.1-1099.5 creates a management construct for a Protected Series. If there are no associated members, the parent Series LLC is the Protected Series’ manager. It also makes clear that the manager of a Protected Series only owes duties to that Protected Series and its associated members or their assignees.¹⁰³ In addition, this section deals with the voting and agency rights of associated members of a Protected Series—they are essentially the same as members of a typical limited liability company.¹⁰⁴

Section 13.1-1099.6 deals with information rights for a Series LLC. A member of a Series LLC that is not an associated member of the Protected Series has the same information rights, with respect to that Protected Series, as a member of a typical LLC.¹⁰⁵ A former associated member of a Protected Series has the same information rights as a dissociated member of a typical LLC.¹⁰⁶ The personal representative of a deceased associated member of a Protected Series has the same rights as the personal representative of a deceased member of a typical LLC.¹⁰⁷ A manager of a Protected Series has the same information rights as a manager of a typical

100. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. §§ 13.1-1088, -1099.10 (Cum. Supp. 2019)).

101. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.3 (Cum. Supp. 2019)).

102. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.4 (Cum. Supp. 2019)).

103. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099(C)–(D) (Cum. Supp. 2019)).

104. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099(E)–(F) (Cum. Supp. 2019)).

105. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.6(A) (Cum. Supp. 2019)).

106. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.6(B) (Cum. Supp. 2019)).

107. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.6(C) (Cum. Supp. 2019)).

LLC.¹⁰⁸ However, these information rights can be modified, but only reasonably, by the operating agreement.¹⁰⁹

4. Limitations on Liability, Claim Seeking to Disregard
Limitation on Liability, Remedies for Judgment Creditor of
Associated Member or Protected Series Assignee, and
Enforcement of Claim Against Non-Associated Asset

The provisions that describe limitations on liability create roughly the same liability construct as a parent LLC would have with regard to the subsidiary LLCs it forms.¹¹⁰ The parent Series LLC, its members, its manager, the associated members, and Protected Series manager are not liable solely by virtue of their status for the obligations of its Protected Series.¹¹¹ Similarly, one Protected Series is not liable solely by virtue of its status for the obligations of another Protected Series parented by the same Series LLC.¹¹² However, one substantial difference between the series construct and actual parent and separate subsidiary LLCs is that subsidiary LLCs can avail themselves of bankruptcy protection separate from their parent LLCs while, because the Series LLC Act is an entirely new creature of state law, it is unclear whether a Protected Series can seek bankruptcy protection separate from its parent Series LLC.¹¹³

Because the Series LLC Act creates a unique entity form, it directly addresses piercing-the-veil-type claims. Section 13.1-1099.8 analogizes Protected Series to subsidiary LLCs and provides that a legal or equitable claim, like a piercing the veil claim against a Protected Series seeking recovery from its parent Series LLC, should be governed by the same principles as a similar claim by creditors of a subsidiary LLC seeking to recover from its parent LLC.¹¹⁴

108. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.6(D) (Cum. Supp. 2019)).

109. *See id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1093 (Cum. Supp. 2019)).

110. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.7 (Cum. Supp. 2019)).

111. *Id.* ch. 636, 2019 Va. Acts at __.

112. *Id.* ch. 636, 2019 Va. Acts at __.

113. *See* Adkisson, *supra* note 61.

114. Ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.8 (Cum. Supp. 2019)).

Like a judgment creditor of a member of an LLC, a judgment creditor of an associated member of a Protected Series has only the rights of an assignee.¹¹⁵ Similarly, a judgment creditor of a Series LLC that is an associated member of its Protected Series only has the rights of an assignee.¹¹⁶

Section 13.1-1099.10 reflects the desire to prevent the use of Series LLCs as a way to defraud creditors, and as such, includes the penalties for failing to keep good records identifying assets as “associated assets” of either a Series LLC or a particular Protected Series it parented.¹¹⁷ As mentioned above, any asset that is not documented as an “associated asset” becomes a “non-associated asset.”¹¹⁸ Non-associated assets can be realized upon by the creditors of the parent Series LLC or any Protected Series.¹¹⁹ Timing is important; an entity cannot simply document an asset as an associated asset after a claim is made or a judgment is entered.¹²⁰ On the contrary, any asset that is not an associated asset on the date a Series LLC or Protected Series incurred the applicable liability (presumably, the date the breach of contract, tort, or other claim giving rise to liability arose) or the date the applicable judgment is enforced is protected from enforcement by a creditor.¹²¹ As mentioned above, the party seeking to claim an asset is an associated asset bears the burden of proof.¹²²

115. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.9(1) (Cum. Supp. 2019)).

116. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099(2) (Cum. Supp. 2019)).

117. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.10 (Cum. Supp. 2019)).

118. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1088 (Cum. Supp. 2019)).

119. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.10 (Cum. Supp. 2019)).

120. *See id.* ch. 636, 2019 Va. Acts at __.

121. *Id.* ch. 636, 2019 Va. Acts at __.

122. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.10(D) (Cum. Supp. 2019)).

5. Events Causing Dissolution of Protected Series, Winding Up Dissolved Protected Series, Voluntary Cancellation, Waiver of Cancellation Upon Dissolution, and Reinstatement of Series Limited Liability Company

A Protected Series is dissolved if its parent Series LLC is dissolved, if any trigger provided in the Series LLC's operating agreement occurs, if all members consent, if a court orders dissolution on application by an associated member or manager (same grounds are available to a member for an LLC), if a court orders dissolution on application by the Series LLC, if the Protected Series is engaged in illegal conduct, if a court orders dissolution on application by the Series LLC or a member of the Series LLC, or if the Protected Series or its parent Series LLC is automatically or involuntarily cancelled.¹²³ A Protected Series can voluntarily wind up its affairs or have a court-supervised wind up in the same way as an ordinary LLC.¹²⁴ Once its voluntary or court-supervised wind up is completed, a Protected Series files a statement of designation cancellation to terminate its existence.¹²⁵ A Protected Series that has dissolved can be reinstated in a similar way that a typical LLC can be reinstated.¹²⁶ However, it is important to note, unlike a typical LLC, a Protected Series cannot exist separate from its parent Series LLC; if the parent Series LLC terminates or dissolves, the Protected Series ceases to exist.¹²⁷

6. Entity Transactions and Merger

Unlike most other entities, a Protected Series cannot engage in most fundamental transactions. For example, a Protected Series may not be a party to a merger, convert to a different entity type, redomesticate, or engage in any similar transaction.¹²⁸ A Series

123. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.11 (Cum. Supp. 2019)).

124. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.12(A) (Cum. Supp. 2019)).

125. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.12(B) (Cum. Supp. 2019)).

126. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.13 (Cum. Supp. 2019)).

127. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.12 (Cum. Supp. 2019)). *But see id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.19 (Cum. Supp. 2019)) (allowing a Protected Series of a nonsurviving Series LLC to become a relocated Protected Series of the surviving Series LLC).

128. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.14 (Cum.

LLC is also constrained from engaging in several fundamental transactions.¹²⁹ A Series LLC cannot convert to a different type of entity, redomesticate, or be a party to a merger with any form of entity other than a limited liability company.¹³⁰

7. Foreign Series LLCs

Sections 13.1-1099.21 to -1099.24 cover in detail how Virginia law will apply to Series LLCs formed in other states. In particular, Virginia will apply the laws of the state of formation to the internal affairs of a foreign Series LLC.¹³¹ Virginia will require foreign Series LLCs and Protected Series transacting business in Virginia to register in the Commonwealth.¹³² However, the activity of a particular Protected Series will not confer jurisdiction over or require the parent Series LLC or other Protected Series to register to do business in Virginia, and the activity of the parent Series LLC will not confer jurisdiction over or require its subsidiary Protected Series to register to do business in Virginia.¹³³

III. SELECTED CASE AFFECTING CORPORATE AND BUSINESS LAW

A. *May v. R.A. Yancey Lumber Corporation*

In *May v. R.A. Yancey Lumber Corp.*, the Supreme Court of Virginia addressed whether a corporation can modify the safe harbor in section 13.1-724(A) of VSCA in its bylaws.¹³⁴

R.A. Yancey Lumber Corporation (“Yancy Lumber”) was a Virginia corporation that owned 2500 acres of real estate containing timber (the “Timber Business”) and a mill business that processed raw lumber into a finished product (the “Mill Business”).¹³⁵ In its

Supp. 2019)).

129. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.15 (Cum. Supp. 2019)).

130. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. §§ 13.1-1099.15, -1099.16 (Cum. Supp. 2019)).

131. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.21 (Cum. Supp. 2019)).

132. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.23 (Cum. Supp. 2019)).

133. *Id.* ch. 636, 2019 Va. Acts at __ (codified at VA. CODE ANN. § 13.1-1099.22 (Cum. Supp. 2019)).

134. 297 Va. 1, 822 S.E.2d 358 (2019).

135. *Id.* at 6, 822 S.E.2d at 361.

bylaws, Yancy Lumber attempted to modify the safe harbor in section 13.1-724(A) of VSCA (italicized below):

A. A sale, lease, exchange or other disposition of the corporation's assets, other than a disposition described in § 13.1-723, requires approval of the corporation's shareholders if the disposition would leave the corporation without a significant continuing business activity. *Unless the articles of incorporation or a shareholder-approved bylaw otherwise provide, if a corporation retains a business activity that represented at least 20 percent of total assets at the end of the most recently completed fiscal year, and 20 percent of either (i) income from continuing operations before taxes or (ii) revenues from continuing operations for that fiscal year, in each case of the corporation and any of its subsidiaries that are consolidated for purposes of federal income taxes, the corporation will conclusively be deemed to have retained a significant continuing business activity.*¹³⁶

This language is frequently referred to as the “safe harbor” language—if it fits within the safe harbor, the transaction does not require approval of shareholders holding two-thirds of the outstanding shares.¹³⁷ The board of Yancey Lumber included the following provision in its bylaws which was approved by shareholders holding a majority of the shares outstanding on December 16, 2015:

Notwithstanding anything herein or any non-mandatory provisions of the [Virginia Stock Corporation Act] to the contrary, either the Mill Business or the Timber Business alone, without the other or any other business activity, shall constitute a significant continuing business activity in the event such business is retained by the Corporation following the sale, lease, exchange or other disposition of the Corporation's other assets if the fair market value of the retained business assets constitutes at least twenty-five percent (25%) of the fair market value of all of the Corporation's assets in the aggregate prior to such sale, lease, exchange or other disposition, excluding for all purposes hereunder cash and cash equivalents. For purposes hereunder, the most recent assessed value for local tax purposes of real property owned by the Corporation shall be considered its fair market value, absent the existence of a fair market value determination by a qualified real estate appraiser made within one year prior to the relevant determination date, in which case the most recent of such determinations shall be used to establish fair market value. This Article XII is intended to operate in lieu of the definition of “significant continuing business activity” set forth in Section 13.1-724(A) of the Code of Virginia (which

136. VA. CODE ANN. § 13.1-724(A) (Cum. Supp. 2018); *May*, 297 Va. at 7, 822 S.E.2d at 361–62.

137. *May*, 297 Va. at 10, 822 S.E.2d at 363.

statutory definition is provided for use in the absence of a defined term in the applicable articles of incorporation or bylaws).¹³⁸

Subsequently, the board recommended that the third sentence above be amended to read as follows:

For purposes hereunder, the most recent . . . gross land and improvement values determined by local tax authority for local . . . taxation of real property owned by the Corporation, irrespective of any land use deferral, shall be considered . . . such real estate's fair market value, absent the existence of a fair market value determination by a qualified real estate appraiser made within one year prior to the relevant determination date, in which case the most recent of such determinations shall be used to establish fair market value.¹³⁹

A pair of minority shareholders, Sarah Yancey May and her ex-husband, Bill May, who collectively owned slightly more than one-third of the stock, voted against the first amendment.¹⁴⁰ Sarah also objected in writing to the first amendment.¹⁴¹ Bill, along with all shareholders other than Sarah, agreed to the second amendment on March 25, 2016, so the second amendment technically received approval of shareholders holding two-thirds of the outstanding shares.¹⁴²

In May 2017, Yancey Lumber executed a letter of intent to sell the assets of the Mill Business.¹⁴³ Sarah objected to the letter of intent and a subsequent amendment that added a \$250,000 break up fee in the event the sale of the Mill Business did not close.¹⁴⁴ On August 11, 2017, Sarah filed a complaint in the Circuit Court of Albemarle County seeking a declaratory judgment that the first amendment and second amendment could not modify section 13.1-724.A of VSCA, and thus, the sale of the Mill Business required shareholder approval.¹⁴⁵

The trial court, relying on the following phrase, “unless the articles of incorporation or a shareholder-approved bylaw otherwise provide,” found that the bylaw amendments could modify section 13.1-724.A of VSCA, noting the statute did not say a bylaw approved by two-thirds of the shareholders, and entered judgment in

138. *Id.* at 7, 822 S.E.2d at 361–62.

139. *Id.* at 8, 822 S.E.2d at 362.

140. *Id.* at 8, 822 S.E.2d at 362.

141. *Id.* at 8, 822 S.E.2d at 362.

142. *Id.* at 8, 822 S.E.2d at 362.

143. *Id.* at 8, 822 S.E.2d at 362.

144. *Id.* at 8, 822 S.E.2d at 362.

145. *Id.* at 9, 822 S.E.2d at 362.

favor of the Corporation.¹⁴⁶ Sarah appealed, and the Supreme Court of Virginia granted four assignments of error, one of which was

[t]he trial court erred in granting the Company's Special Plea in Bar and entering judgment against Sarah on the ground that a mere majority of the Company's shareholders may not amend or redefine the statutory safe harbor of [Virginia] Code § 13.1-724, nor create its own safe harbor, through the amendment of the Company's bylaws.¹⁴⁷

Yancey Lumber argued the position that a bylaw approved by shareholders, holding a majority of the shares present, was sufficient to modify the safe harbor given that the introductory language to the safe harbor appeared to allow modification and did not require a vote of two-thirds of the outstanding shares.¹⁴⁸ In its analysis, the court stated:

The plain language of the statute does not support the Corporation's claim that the exception in the safe harbor provision permits a corporation to adopt a bylaw that redefines the meaning of "significant continuing business activity" to be anything that the majority designates it to be. The safe harbor provision simply states a default threshold, and the plain language of the statutory exception to the application of that threshold only allows a corporation to accept or reject that threshold.¹⁴⁹

The court reasoned that another interpretation could render the requirement that two-thirds of the outstanding shares approve a sale of substantially all assets meaningless.¹⁵⁰ The court noted that section 13.1-724(E) of VSCA only permits a modification of the two-thirds vote requirement in the articles of incorporation.¹⁵¹

Yancey Lumber also argued that because Bill May approved the second amendment, he implicitly approved the first amendment, and thus the applicable bylaw amendment was approved by two-thirds of the outstanding shares.¹⁵² The court found that argument flawed, reasoning that the two-thirds vote requirement only applies to the asset sale, and that a vote for the second amendment could not ratify the entire bylaws.¹⁵³

146. *Id.* at 10, 13, 822 S.E.2d at 363–64.

147. *Id.* at 11–12, 822 S.E.2d at 364.

148. *Id.* at 13, 822 S.E.2d at 364.

149. *Id.* at 16, 822 S.E.2d at 366.

150. *Id.* at 16, 822 S.E.2d at 366.

151. *Id.* at 16, 822 S.E.2d at 366.

152. *Id.* at 13, 822 S.E.2d at 364–65.

153. *Id.* at 17, 822 S.E.2d at 364–65.

It is possible following this case that a corporation cannot modify the safe harbor in its articles of incorporation or bylaws, even to make it harder for the corporation to satisfy, for example, by increasing the percentage of total assets and either income or revenue to be maintained. Courts may end up interpreting this case to permit a corporation to make the safe harbor harder to satisfy with an amendment to its articles of incorporation that is approved by shareholders holding at least two-thirds of the outstanding shares. The case does make it clear that an amendment to the bylaws or articles of incorporation may approve or reject the safe harbor.¹⁵⁴ Perhaps the legislature will clarify whether the safe harbor can be modified, and if so, the vote necessary to do so.

CONCLUSION

The General Assembly made notable changes to VSCA and the Virginia Limited Liability Company Act this year. In VSCA this included addressing myriad issues from ratification of defective corporate acts, to improving and making the effect of merger, domestication, and conversion language more uniform. Virginia also this year became one of the earliest states to adopt the Uniform Protected Series Act, a fascinating innovation in business entity law. Finally, the Supreme Court of Virginia interpreted the safe harbor in section 13.1-724(A), which if satisfied, permits a sale of assets outside the ordinary course of business without a shareholder vote.

154. *Id.* at 16, 822 S.E.2d at 366.