HAND OUT #5

Mississippi Secretary of State
2008 Business Reform Committees
Minutes of LLC/ Partnership Study Group Meeting #1
June 12, 2008

The first meeting of the LLC/ Partnership Study Group was called to order on Thursday, June 12, 2008 at 11:00 A.M. at the Office of the Secretary of State, 700 North Street, Jackson, Mississippi. The attendees are listed in Exhibit A. Secretary of State Delbert Hosemann called the meeting to order by thanking all the committee members for attending.

Purpose of and Mission of the Business Reform Committees

Secretary Hosemann described the six business reform committees established by his office. He commented that the proposed business court would be administering the new limited liability company ("LLC") statute that the LLC Study Group would produce.

The Secretary commented that he anticipated sweeping changes to the existing LLC Act. He noted that the members had tremendous experience both in using and drafting LLC statutes. The Secretary stated that the various committees were on a short time frame, attempting to complete their assigned tasks by the end of the summer. The Secretary concluded by remarking about the exciting opportunity this initiative created. He noted that Mississippi now has more LLCs than corporations, and that the LLC entity would be the vehicle for the operation of business for years to come.

Introduction of Members

Cheryn Baker recognized the three Co-Chairs of the LLC/ Partnership Study Group and the other attendees introduced themselves.

Co-Chair Introductory Remarks

Steve Hendrix invited any and all input. He stated that the agenda included some core issues and was not meant to be exhaustive, but rather a starting point. One of the objectives of this meeting was to begin a list of concerns that would ultimately be addressed in subsequent meetings. Hendrix stated that the Committee would also form smaller groups to target specific areas of focus and to maximize time.

Next, David Grishman stated that the Co-Chairs hoped that throughout all discussions, the Committee members would give input freely and would raise other issues that were not on this or subsequent agendas- particularly issues that result from real-life experience.

Adoption of the Revised Uniform Limited Liability Company Act (2006)

David Webb introduced the possibility of adopting the Revised Uniform Limited Liability Company Act (2006) ("RULLCA"). Webb noted that the original uniform LLC Act was adopted in the mid-1990's and that the RULLCA was the most recent amendment.

Webb referenced the materials that discussed concerns with the RULLCA and also noted that the RULLCA provided more certainty in specific situations such as duties of loyalty and care imposed on members and managers of LLCs. By contrast, the Mississippi and Delaware Acts leave those duties up to the drafter of the LLC's operating agreement. Webb commented that he preferred the flexibility of the present Mississippi and Delaware Acts. Webb stated that he did not see the Committee's charge as necessarily adopting or not adopting the RULLCA, but rather to look at other laws and to choose provisions that the Committee thinks will improve and enhance Mississippi's existing LLC Act.

Co-Chair Hendrix referred to a comparison chart of the Mississippi, Delaware and Revised Uniform LLC Acts in the materials and noted that the chart would be expanded to discuss additional sections in more detail. Hendrix expressed his hope that the issues on the chart would spur discussion.

Adoption of More Default Provisions in LLC Act vs Operating Agreement Requirement

Hendrix then asked the Committee about whether it would be better to have many default provisions (which would benefit LLCs that did not seek legal advice) or to let the operating agreement control. Hendrix commented that there was certainly more than one side to the issue and feedback from the Committee followed. Many of the members supported the concept of having more default provisions which would address issues that are vague or not covered in the LLC's operating agreement, or in the absence of an operating agreement. This would allow clients to "have it both ways." Secretary Hosemann expressed his desire that the statute be as complete as possible—subject to operating agreements—to service those who do not have an operating agreement.

The group then discussed the pros and cons of requiring a written operating agreement or posting a model operating agreement on the website. One member commented that if the LLC was a single member LLC, he saw no need to require a written agreement, but if the LLC was one of multiple members, then those members would need the protection of a written agreement. Several members expressed concern about posting a model agreement. Hendrix noted that if the statutes were drafted properly, the statutes would serve as a default operating agreement in the absence of a written agreement, which would eliminate the need for a model written agreement.

Conversion Statutes

Webb and the group discussed conversion statutes.

- The Co-Chairs noted the convenience of simple conversion and expressed that tax implications represented the more complex side of entity conversion. Webb stated that the adoption of conversion statutes would certainly simplify the administrative portion of converting entities.

- Grishman expressed concern that if there is an easy way to convert from one entity to another, there will probably be many entities that convert from a corporate form to an LLC, simply because they can do it easily. Unfortunately, they may not consider the negative tax consequences, especially those entities without tax or legal counsel.

- Co-Chair Webb noted that aside from tax consequences, organizational documents would need to be changed in a conversion. For example, would the by-laws of a corporation that is converted into an LLC become the operating agreement?

- One member asked if the proposed conversion statutes would include cross-entity mergers. Webb answered affirmatively, that such was one purpose of considering a conversion statute.

- The Secretary shared that he serves on the Governor's tax study commission. The Secretary stated that one item on the agenda of the tax study commission was a merger exemption for an entity converting from a corporation to an LLC. He felt the tax savings would present a greater incentive for LLCs to locate in Mississippi.

Model Registered Agent Act

Next, Steve Hendrix discussed the Model Registered Agent Act ("MoRAA"). He noted that each business entity statute in Mississippi law has its own registered agent provision. Hendrix noted MoRAA provides for a global registered agent statute that applies to all types of business entities to eliminate inconsistencies regarding agents within the various entities' governing laws. There are also benefits to registered agents that represent multiple clients in the State. He noted also that adoption of such a statute would assist the Secretary of State's office in becoming more automated and efficient in several respects.

Baker stated that a joint study group comprised of members from the LLC/Partnerships Committee, the Corporations Committee and the Nonprofits Committee would be formed to study MoRAA and the conversion statutes. The end result would be consistency among all the affected entities.

Other Cross-Entity Issues

Hendrix recommended that the Committee think about other areas, such as indemnification and others that cross over from one entity to another that might not be consistent. He offered as one example the possibility of one statutory definition for what constitutes doing business in Mississippi to avoid a situation where an action by a corporation is considered "doing business in the state" but the same action by a partnership is not considered "doing business in the state."

Filing Fees and Annual Report Requirement

Next, Webb referred to the materials comparing filing fees in Mississippi with those in other states. The group discussed the desirability of implementing expedited filings (with increased fees), and electronic and online filing capabilities.

Next, Hendrix raised the issue of annual filings, noting its connection to the related issue of administrative dissolution. The group discussed the possible benefits and drawbacks of requiring LLCs to file an annual report and reasons why LLCs should be treated differently from corporations with respect to this requirement. They also discussed problems they had experienced due to their

clients' failure to file annual reports. Several members were concerned about small LLCs possibly losing their liability protection if they were required to file annual reports and failed to do so. Others were concerned that an increase in compliance responsibilities would lead to court battles, arguing about why the members of a non-compliant LLC should not to be subjected to personal liability.

One member asked the Secretary about the efficiency of communication between the Tax Commission and the Secretary of State. The Secretary stated that the Commission no longer mass-mails forms. His office was continuing to work on the issue of streamlining filing requirements, possibly with the Tax Commission and internally in the Secretary of State's Office.

Next, a Committee member asked Secretary Hosemann about the burden on the Secretary's Office presented by an inactive LLC. The Secretary answered that the burden was not in storing the data so much as in the availability of the name of the defunct LLC to others desiring to use it. He expressed his desire to have some system in place to "purge" the system of defunct LLCs. He expressed his intention to be very cautious to not delete the inactive LLC as an entity, but rather keep the LLC in a suspended status.

The Treatment of LLCs as Partnerships or Corporations

Hendrix noted that the RULLCA treats member-managed LLCs more like partnerships, while treating manager-managed LLCs more like corporations—with managers being viewed as counterparts to the officers and board of directors of a corporation. He noted that Delaware law makes no such distinction. Another Committee member cautioned that a brightline rule based on a member-managed or manager-managed distinction may lead to litigation for certain small LLCs that write their own operating agreements (which include a mixture of member-managed and manager-managed provisions in them).

A member commented that there were a line of cases in Mississippi that found that shareholders in a closely-held corporation have to treat other shareholders in a way that is "intrinsically fair," a significantly high standard. He wondered if a standard was not specified in the LLC statute, would the courts apply the "intrinsically fair" standard to an LLC. He expressed that the Committee should consider this when making revisions to the Act. Secretary Hosemann recommended a definitive course of action, so as to avoid any uncertainty. Hendrix agreed, noting that locating businesses want certainty and predictability, and that explained much of Delaware's success.

Authority of Members to Act on Behalf of LLCs

Next, a member of the Committee raised the question of who binds, or acts on behalf of the LLC, with regard to the distinction between member-managed and manager-managed LLCs. He noted that in his practice, he often formed LLCs with a corporate-type structure, with persons (officers) acting on behalf of the LLC on a day-to-day basis other than members or managers. He stated that if a document was submitted to the Secretary of State signed by one of these persons ("President" for example) it would be rejected. The document must have been signed by a manager (or member). The Committee member thought this was an area in which more flexibility would be desired to accommodate clients' desire to form LLCs but to keep the corporate structure and titles they are familiar with. Several members echoed this sentiment. Co-Chair Webb noted that the

present LLC Act had no reference to officers. A member noted that the Tennessee Act offered three organizational structures to choose from, each structure having default provisions. It was suggested that the Committee reference the Tennessee statute.

Review of Certificate of Formation

Next, Secretary Hosemann commented that the Committee should review the certificate of formation. He anticipated that the Committee would desire to re-write it.

Fiduciary Duties of LLCs

Next, Hendrix gave an overview of the present Mississippi law of fiduciary duties of LLCs, noting that it allowed LLCs to eliminate all duties except those of good faith and fair dealing. He also noted that Delaware's approach was nearly identical, echoing the partnership aspect of LLCs. He stated that the RULLCA's approach was to impose duties of loyalty and care and the business judgment rule on the members and managers—a different concept than the historical one. He also noted that under RULLCA there were certain provisions that could not be eliminated by the operating agreement. Many members had opinions on this issue:

- One response was that freedom of contract must remain paramount. The imposition of statutory duties that could not be eliminated would be more of a hindrance than a help in bringing business to Mississippi.
- Another member expressed concern with how to protect oppressed minority members if fiduciary duties were eliminated.
- Hendrix acknowledged the wide variety in LLCs: from the complex LLC to the large percentage of LLCs that are formed for a specific short-term purpose and are comprised of members who have other interests outside the interest of the LLC and do not want the imposition of fiduciary duties.
- Secretary Hosemann noted that the privilege of limited liability should be balanced by obligations of managers to the LLC. He cautioned that if the state "drifted too far" from those duties, to a point of assuming that everyone is an educated investor, or that minority members should not be supported, we will find ourselves in trouble. He noted that we wanted the most favorable LLC statute, but cautioned that we must be careful about waiving all fiduciary duties.
- Hendrix noted that some judicial opinions held that the standards of good faith and fair dealing from contract law were broad enough to encompass fiduciary duties and that those duties do not have to be elevated to the corporate duties that have grown up over the years.
- The Secretary commented that he wanted the Committee to be decisive about the duties, one way or the other, but not to leave the issue unclear.
- One member stated that he liked the status of fiduciary duty in Mississippi presently, that the protection of minority interest members should be governed by the operating agreement.
- Another member noted that if the choice were small investor-friendly or promoter/manager/developer-friendly, Delaware would be characterized as promoter/manager/developer-friendly.

Remedies for Breach of Agreement and Procedure for Contested Matters

Chairman Grishman stated that both of these issues represented areas not specifically addressed in the statute, and are potential areas for instituting default provisions. Grishman asked if any Committee members had problems with either of these areas. A few members responded in the affirmative. One member noted when a generic operating agreement had been used and did not cover the reason for dissolution, the current statute did not fill the gap. Another member mentioned the problems with the transition of new members to an LLC—whether the addition of new members requires consent of all the members, or whether the operating agreement controls.

Series LLCs and Springing LLC Members

Next, Hendrix briefly explained Series LLCs (included in the materials) and springing members. He asked the Committee to consider them for future discussion.

Other Issues

A Committee member asked if the Delaware LLC Act created business opportunity in Delaware. Members responded that favorable laws in Mississippi could certainly bring economic impact, but that the lack of Mississippi case law was counterproductive. The Committee member who posed the question then asked if the creation of a business court system was critical to any business opportunity.

Secretary Hosemann responded to the question. He noted that an industry has been formed just to analyze the appropriate state in which to register an entity. Several factors are analyzed. The Secretary stated the advent of a business court and a cutting-edge LLC system in Mississippi would be additional "arrows in the quiver" along with tort reform, in comparison to neighboring states. Associated businesses would follow the businesses that come to Mississippi.

Co-Chair Grishman invited the members to raise additional issues. The group was invited to submit issues and questions following the meeting to Assistant Secretary Baker.

Upcoming Meeting Dates and Programs

Assistant Secretary Baker referred the group to the website for the Policy and Research Division for the Committee roster and minutes from the meetings. She noted that the next meeting would be July 10, 2008 and there will be speakers at the meeting who were involved in drafting the RULLCA. She noted that September 8, 2008 was the proposed deadline for the Committee to submit its recommendations.

Secretary Hosemann thanked the Committee; the meeting was adjourned at 12:47 P.M.

Respectfully submitted by:

Cheryn Baker

Cheryn Baker
Assistant Secretary of State
Policy and Research Division

Mississippi Secretary of State
2008 Business Reform Committees
Minutes of the LLC/Partnership Study Group, Meeting # 2
July 10, 2008

The second meeting of the LLC/Partnership Study Group was called to order on Thursday, July 10, 2008 at 11:30 A.M. at the Office of the Secretary of State, 700 North Street, Jackson, Mississippi. A list of the persons who were present in person or by telephone is attached at Exhibit A.

Introduction

The minutes from the first meeting were approved and Cheryn Baker, Assistant Secretary of State, Policy and Research Division, introduced the panelists for the meeting. The panelists (who were present by teleconference) were:

- Thomas E. Rutledge
- Elizabeth S. Miller
- Scott E. Ludwig
- Robert R. Keatinge

Biographies of the four panelists are attached as Exhibit B.

Presentation by the Panelists

- Overview of the Revised Uniform Limited Liability Company Act ("RULLCA")

The panelists described RULLCA as an act containing many provisions that are more specific than those contained in earlier uniform limited liability company ("LLC") statutes. Furthermore, the panelists explained that there were some provisions in RULLCA which are not found in any other statutes. Scott Ludwig noted that one of the best aspects of RULLCA was its inclusion of provisions regarding what can and cannot be modified or eliminated in a written operating agreement. He stated that the drafters of RULLCA attempted to de-couple the idea of management being statutorily authorized so that the authority to bind the company would be contained in the operating agreement. Mr. Ludwig explained that any LLC act must be reviewed and updated on a yearly basis.

- Written Operating Agreement Requirement

The panelists agreed that any LLC statute should be flexible enough to allow both written and implied operating agreements. Moreover, the panel cautioned against adopting a provision stating that an unwritten operating agreement would serve no function. Mr. Keatinge explained that courts increasingly analyze the parties' course of conduct to determine the terms of verbal or implied operating agreements. Ms. Miller added that certain provisions of an operating agreement

that are regulated by the statute of frauds must be in writing in order to be enforceable.

- Default Provisions

The panel agreed that in the event that an issue was not addressed by a written or verbal operating agreement, then default provisions in the LLC would act to fill in any gaps that were left.

- Conversion Statutes

Mr. Keatinge explained that Colorado had faced the problem of its corporation conversion provisions and LLC conversion provisions being inconsistent with one another. He stated that Colorado solved the problem by creating a separate statute which served as a "junction box" and contained one conversion provision that was consistent for corporations and LLCs. In relation to post-conversion documents, Mr. Keatinge noted that there was not much that could be done to address this issue by statute. Mr. Ludwig added that a corporate conversion to an LLC dramatically changes the shareholder's rights; therefore, a shareholder's rights should be carefully considered before such a conversion is made.

- Series LLCs

The panel explained that a significant problem with series LLCs is that across the county there is no uniform understanding of what constitutes a series LLC. The panel listed several questions which are still outstanding in the area of series LLCs, including:

- Whether a series LLC is a separate entity;
- How series LLCs are to be treated in bankruptcy;
- How state revenue commissions should look at series LLCs;
- How real estate can be transferred from one series to another;
- Whether, if a single series of a multiple-series LLC transacts business in a state that does not recognize series LLCs, there is a tax nexus.

Mr. Rutledge suggested that it would better to take Colorado's approach of studying these issues, but waiting to see how other states resolve the problems which have arisen in regard to series LLCs. As for Texas, Ms. Miller explained that the state had determined that the time was not yet ripe to adopt series LLC provisions.

- Fiduciary Duties

The panel explained that there are two main schools of thought in regard to fiduciary duties: one whose aim is to protect all of the LLCs participants, and second, a school which first and foremost values the freedom of contract. Furthermore, Mr. Ludwig explained that choosing between the two depended on

the state and the state's thought process. Mr. Keatinge added that the idea of eliminating fiduciary duties becomes more of an issue than it should more often than not. He explained that Delaware has a baseline that one can not eliminate the duties of good faith and fair dealing.

Conclusion of Meeting

Mrs. Baker concluded by stating that certain group members had been assigned to the Model Registered Agent Act subcommittee. She indicated that the subcommittee would have a separate notebook with information explaining how the act pertained to each type of business entity. Steve Hendrix, Co-Chairman of the LLC/Partnership Study Group, noted that there was a great deal of information which the group needed to digest. He explained that in the next meeting the group would discuss which areas of the LLC act it should address. Mr. Hendrix opined that subcommittee assignments should be held off until the next meeting. With no further business, the meeting was adjourned at 12:45 P.M.

Respectfully submitted,

Cheryn Baker

Cheryn Baker
Assistant Secretary of State
Policy and Research Division

Mississippi Secretary of State
2008 Business Reform Committees
Minutes of the LLC/Partnership Laws Study Group, Meeting # 3
July 31, 2008

The third meeting of the LLC/Partnership Laws Study Group was called to order on Thursday, July 31, 2008 at 11:15 A.M. at the Secretary of State's Office, 700 North Street, Jackson, Mississippi. A list of the persons who were present in person or by telephone is attached at Exhibit A.

Introduction

Cheryn Baker, Assistant Secretary of State for Policy & Research, welcomed the group and took attendance of the members who participated in the meeting by teleconference. Next, the group adopted the minutes of the second meeting, which was held on July 10, 2008.

Discussion of Adopting the Revised Uniform Limited Liability Company Act (RULLCA)

Co-chair David Grishman opined that it would be too ambitious for the study group to make a determination on whether to adopt RULLCA, given the group's time constraints and the complexity of the subject matter. However, he urged the members to continue studying the act in hopes that the group could reconvene and address adopting RULLCA at some point in the future.

Formation of Subcommittees

Cheryn Baker announced the creation of subcommittees to study the following issues:

- Conversion and "junction box" statutes;
- Potential amendments to the Mississippi Limited Liability Company Act regarding fiduciary duties, default provisions, who has the authority to bind an LLC, and whether operating agreements should be required to be in writing; and
- Changes to LLC reporting and registration forms, the desirability of offering online filing and expedited processing, and fees associated with LLC filings.

In addition, Mrs. Baker stated that certain group members had been assigned to a joint committee which would study the Model Registered Agent Act and recommend whether Mississippi should adopt it in whole or in part.

Many members volunteered for positions on each of the subcommittees. As for those members who did not state a preference, Ms. Baker said they would be assigned to subcommittees as needed.

Time Line

A member suggested that if the group wanted its recommendations to be considered by the Mississippi State Legislature during the 2009 regular session, that these recommendations would need to be made by October at the latest.

Series LLCs

Co-Chair Grishman asked the members for their input on other issues that the study group could or should address. Several members stated their opinions on whether the group should look at the issue of recognizing so-called "series LLCs." One member expressed his opinion that the group would be better served by studying how Mississippi should treat out-of-state series LLCs, rather than focusing on statutes which would authorize the creation of series LLCs within the state. After several members expressed their interest in the concept of series LLCs, the group decided that at least some members of the group who had a particular interest in series LLCs should organize a study group to look into the issues surrounding series LLCs.

Other Business

The group agreed with Co-Chair Grishman's suggestion that the various subcommittees should meet twice per month. Further, the group elected to forego holding a full meeting on August 14, opting instead to hold subcommittee meetings during that time. The members also decided that the subcommittees would prepare periodic status reports to present to the full study group.

Conclusion of Meeting

With no further business, the meeting was adjourned at 12:00 P.M.

Respectfully submitted,

Cheryn Baker

Cheryn Baker
Assistant Secretary of State
Policy and Research Division

2008 BUSINESS REFORM COMMITTEES
Minutes of the
JOINT MEETING OF THE CORPORATIONS LAW STUDY GROUP
AND THE LLCS AND PARTNERSHIPS LAWS STUDY GROUP

NOVEMBER 6, 2008

The joint meeting of the Business Corporations Laws Study Group and the LLCs and Partnerships Laws Study Group was called to order on Thursday, November 6, 2008 at 11:00 A.M. at the Office of the Secretary of State, 700 North Street, Jackson, Mississippi. A list of the persons who were present in person or by telephone is attached at Exhibit A.

Introduction

Cheryn Baker, Assistant Secretary of State for Policy and Research, welcomed the members to the meeting. The minutes from the LLCs and Partnerships Laws Study Group Meeting held on July 31, 2008 were approved.

Report from Corporations Laws Sub-Group on Forms, Filings and Fees

Tommy Shepherd, Chair of this Sub-Group, presented the Report attached at Exhibit B. After some discussion a motion to approve the recommendations of the Sub-Group report was made and seconded. The report was approved unanimously by the Group.

Report from LLCs Laws Sub-Group on Forms, Filings and Fees

David Webb, Chair of this Sub-Group, presented the Report attached at Exhibit C. The Group discussed the recommendation to require LLCs to file annual reports or bi-annual reports. Ms. Baker explained the staff was considering making the reports bi-annual to avoid having to hire additional staff to process these reports, but that Secretary Hosemann had since expressed a preference for annual reports. The consensus of the group was that it would be less confusing if all entities filed annual reports. Ms. Baker also mentioned that at least some of the additional revenue to be gained from instituting annual report filing requirements could be used to help fund a business court.

The Group also discussed the recommendation to allow the Secretary of State to charge $25 for accepting service of process on defendant LLCs. One member of the group questioned the need for this recommendation if the Group was going to recommend that all fees be set forth in the rules. Baker suggested that the Group leave this recommendation in the report as a fall back in case the legislature did not agree to amend the statute to permit the Agency to establish all fees by rule.

Following the discussion a member made a motion to approve the recommendations of the Sub-Group report, which was seconded and approved unanimously by the Group.

Report from Corporations Laws Sub-Group on Amendments to the Corporations Act

Henry Chatham, Chair of this Sub-Group, presented the Report attached at Exhibit D. Ms. Baker explained the recommendation concerning the change to Section 79-14-14.22. After some discussion, a motion to approve the recommendations of the Sub-Group report was made and seconded. The report was approved unanimously by the Group.

Ms. Baker informed the group that the Division would prepare a report to the Legislature of the recommendations and the proposed bills to effect the recommended changes. The Division will forward these documents to the Group and obtain their approval of them before submitting them to the Legislature.

Other Sub-Groups Status Reports

Ms. Baker reported on the status of the Model Registered Agent Act Joint Committee. This committee has met and will meet again in 2009. It will have recommendations for the 2010 Legislative Session. Steve Hendrix, Chair of the LLCs Act Amendments Sub-Group discussed the issues that this Sub-Group is considering. He stated that it will not have any recommendations for the 2009 Legislative Session, but that he hoped the group would be able to make a recommendation of comprehensive changes to the LLC Act for the 2010 Legislative Session. Ms. Baker stated that the Series LLCs and Conversions Sub-Groups were still being organized and have not yet held any meetings. She informed the group that if anyone was interested in serving on either one of these committees to let her know and she would add them to the committees. These groups will not have recommendations for the 2009 Session.

Other Business

Cory Wilson, Chief of Staff, thanked the members for their attendance and their participation in the study groups. He stated that Secretary Hosemann was talking about the study groups around the state and he was getting good feedback concerning them. Ms. Baker asked the members to assist the Agency with promoting the recommendations approved at this meeting to the Legislature. She asked them to contact their legislators about these reports and express to these legislators their support of these reports. She also indicated that she would be contacting them when the 2009 Legislative Session begins about things they could do to help in this regard.

With no further business, the meeting was adjourned at 11:45 A.M.

Respectfully Submitted,

Cheryn Baker

Cheryn Baker
Assistant Secretary of State
Policy and Research