

**University of South Dakota School of Law**

---

**From the Selected Works of Thomas E. Geu**

---

2007

## Foreclosure and Dissolution Rights of a Member's Creditors: No Cause for Alarm

Thomas E Geu, *University of South Dakota School of Law*  
Thomas Rutledge



Available at: [https://works.bepress.com/thomas\\_geu/15/](https://works.bepress.com/thomas_geu/15/)

**A** recent article in this magazine by Elizabeth M. Schurig and Amy P. Jetel entitled *The Alarming Potential for Foreclosure and Dissolution by an LLC Member's Personal Creditors*, Prob. & Prop., May/June 2006, at 42, raised the specter that a judgment creditor of a member of a limited liability company (LLC) might apply for a charging order, obtain it, persuade the court to order foreclosure on the membership interest subject to the charging order before the charging order is redeemed, be the successful bidder at the foreclosure sale thereby becoming a transferee, petition the court for involuntary judicial dissolution of the LLC, and, finally, persuade the court to order an involuntary dissolution in conformance with the statutory prerequisites—all without regard to the consequences of such an order on a potentially successful business, its other members, employees, and creditors.

Even the threat of judicial dissolution could force a sale of the entity's assets or require the other members to purchase the interest at the foreclosure sale or from the purchaser at the sale at an inflated price. Any realistic possibility of judicial dissolution would therefore represent a serious threat to the "asset protection" goals of using an entity's separate existence to insulate personal assets from the reach of that member's creditors. Moreover, either event would be highly disruptive to the successful continuation of the LLC's business. If the consequences of the threat are more than a theoretical

---

Thomas E. Rutledge is a member of the Louisville, Kentucky, firm of Stoll Keenon Ogden PLLC and an adjunct professor of law at the University of Kentucky College of Law; Carter G. Bishop is a professor of law at the Suffolk University School of Law, Boston, Massachusetts; and Thomas Earl Geu is a professor of law at the University of South Dakota School of Law, Vermillion, South Dakota. Bishop was co-reporter for RULLCA; Rutledge and Geu were advisors to RULLCA.

## Foreclosure and Dissolution Rights of a Member's Creditors

No Cause for  
Alarm

PANIC

**By Thomas E. Rutledge, Carter G. Bishop,  
and Thomas Earl Geu**

Creditor/Transferee Rights	Uniform Acts	Comment
Right of creditor of the corporation to move for judicial dissolution.	Not in RUPA, RULPA, ULLCA, or RULLCA.	MBCA § 14.30 permits only on showing that corporation is insolvent.
Right of transferee to move for judicial dissolution.	RUPA §§ 503(b)(3), 801(6); ULLCA § 801(5).	Requires showing that dissolution is "equitable."
Right of creditor to enforce contribution obligation.	RUPA § 807(f); ULPA § 502(c); ULLCA § 402(b); RULLCA § 403(b).	May require reliance in having extended credit on that obligation.
Creditor enforcement of partner/member contribution obligations on winding up.	RUPA § 807(f); ULPA § 502(c); ULLCA § 402(b); RULLCA § 403(b).	
Transferee's rights to receive interim and liquidating distributions.	RUPA § 503(b); ULPA § 702(b); ULLCA § 502; RULLCA § 502(b).	
Right of transferee to apply for judicial supervision of winding up.	RUPA § 803(a); ULPA § 803(c), (d); ULLCA § 803(a); RULLCA § 702(d)(2).	In RULLCA, only if there are no remaining members.
Right to seek judicial dissolution on company breach of statutory buyout by dissociated member.	ULLCA § 801(4) & (5).	RUPA § 701, while providing for statutory buyouts, does not give a right to seek dissolution in the event of breach.

risk, they represent a serious impediment to the use of the LLC entity form.

The central difficulty with the previous article is that consummation of the threat requires the completion of multiple events, each with independent significance. The sequence of events becomes increasingly unlikely as they cascade toward the rarely granted remedy of judicial dissolution of an otherwise successful business simply because a member incurred an unrelated debt.

Statutory and equitable judicial dissolution remedies exist for all business entity forms and for good reason; they protect an owner from the fraudulent or nefarious behavior of other owners. Judicial dissolution remedies for *owners* (shareholders or partners, for example) have existed for over a century and yet are asserted rather sparingly by *full owners* and, further, rarely granted by a court to disrupt a profitable business enterprise. See Alan R. Bromberg & Larry Ribstein, IV *Bromberg and Ribstein on Partnership* § 17.06(e)(3), at 17:70.

Although judicial dissolution rights of business owners are rarely granted, similar rights of an owner's *transferee* are even more constrained. Generally speaking, unincorporated entity law

uniformly provides that a member's transferee may not exercise any of the member's rights to participate in management including, under many statutes, the statutory right to petition for judicial dissolution. Accordingly, there is, in fact, no cause for alarm.

#### **Rights: A Comparative Introduction Across Entities**

The place to start the analysis is the rights of *members* themselves. Every form of business entity permits the owners to agree unanimously to dissolve the entity, sell the assets, and distribute the net proceeds. See, e.g., RULLCA §§ 404, 701, 702. The motives of the owners are irrelevant because they act in concert and without oppression. A disquieting opportunity of menace, however, lurks in this unanimous sanctuary. A malcontent or obstreperous owner could cause harm and heartache to the other owners but withhold its consent to dissolution, trapping the other owners on a sinking ship. As a result, first equity and then law granted the trapped and aggrieved owners the sanctity of an involuntary dissolution of the entity ordered by a court, but only after a fair hearing to determine whether the business should

continue under the circumstances. See Model Business Corporations Act (MBCA) § 14.30, off. cmt. (b).

In the corporate context, and absent contrary agreement, a shareholder can transfer stock to any person it chooses, and the transferee of the shares is a shareholder, has all of the rights of any other shareholder, and may petition a court to dissolve the entity. If an individual shareholder's judgment creditor receives the shares in satisfaction of a debt, the creditor becomes a shareholder and, as such, has the ability to move for dissolution.

An unincorporated entity is different. Absent contrary agreement, an owner of an unincorporated entity may not transfer the full ownership right to another without the approval of the other owners. The law of these organizations presumes a close personal association from conception, and state statutes provide that economic rights are freely transferable but that governance rights are nontransferable. Uniform Partnership Act (UPA) § 27(1); RUPA § 503(a)(3); Uniform Limited Partnership Act (ULPA) (1985) § 702; Uniform Limited Liability Company Act (ULLCA) § 502; ULPA (2001) § 702(a)(3); RULLCA § 502(a)(3)(A).

LLCs and other unincorporated entities, therefore, have an initial advantage over corporations in the entity selection calculus in the closely held or asset protection context because the transfer of an ownership interest does not make the transferee a member by operation of law. For the purposes of this article, that difference is most important when the transfer is to satisfy the judgment debt of an individual member. See Jay Adkisson & Christopher Riser, *Asset Protection* 217 (2004).

The table on page 36 contains comparative information about the rights of creditors and transferees across business organizational statutes. In using the table, recall that transferees of corporate shareholders become shareholders themselves. As a result, corporate law is referenced only in a limited way. Determining whether the menu of rights is entirely rational as it varies across business forms is beyond the scope of this article. The chart serves only as background for the limited purposes of this article.

As the table suggests, both *creditors of the entity* and *transferees of ownership interests* have a limited menu of statutory rights. These limited rights of creditors and assignees seem reasonable in the broad context of the different types of unincorporated entities. Illustratively, creditor enforcement of contribution obligations is understandable when one considers that “paid in capital” forms a basis on which credit is extended and, in part, on which credit is priced. Transferee rights for oversight of winding up protect the reasonable expectation of receipt of liquidating distributions.

None of the uniform acts provides assignees interim oversight or accounting rights for *interim* distributions. As such, during the period the partnership/LLC is operating, the transferee is not provided information on the operations leading to the distributions. Restricted information rights do exist for transferees but only when active business operations have terminated and the partnership/LLC is in the winding up phase. See, e.g., RUPA § 802(a); ULPA § 803(a); RULLCA § 502(a)(3)(B).

Further, under most current unincorporated entity statutes, the transferee of an owner, unlike the owner, does not at law have the *statutory* right to petition for judicial dissolution of the entity. For example, in a limited partnership, only general and limited partners typically have the right to apply for judicial dissolution, and transferees do not have a similar statutory right. RULPA § 802; ULPA (2001) § 802. Likewise, in a *term* (but only in a term) general partnership, only partners have the statutory right to apply for judicial dissolution. UPA § 32(1); RUPA § 801(5). There is an

Absent contrary agreement, an owner of an unincorporated entity may not transfer the full ownership right to another without the approval of the other owners.

exception to the “partners only” rule for a term general partnership when it extends beyond its term. Under those circumstances a transferee has the right to seek judicial dissolution. UPA § 31(2)(a); RUPA § 801(6)(i). More importantly, however, transferees of an interest in an at-will general partnership have the statutory right to seek judicial dissolution only when it is “equitable” to dissolve the partnership. UPA § 31(2)(b); RUPA § 801(6)(ii).

ULLCA (1996) carried over the at-will and term distinction from the law of general partnerships, including the rights of transferees to apply for judicial dissolution (as constrained by the equitable standard). ULLCA § 801(5). It is important to note, however, that ULLCA (1996) was adopted in eight states, and there was departure from the at-will and perpetual distinction; thus, it is arguable that criticisms relat-

ing specifically to ULLCA (1996) should form the primary basis for the larger debate.

Even under UPA, RUPA, and ULLCA (1996), the application of the dissolution provisions requires equitable reasons. UPA was silent on this point, but the context of the grounds for granting judicial dissolution clearly implied the necessity of equitable grounds in that RUPA § 801(6) and ULLCA § 801(5) expressly limit a transferee’s right to obtain judicial dissolution subject to a showing of equitable grounds.

RULLCA (2006) places a greater limitation on the right to seek judicial dissolution than ULLCA (1996). Judicial dissolution *may only be sought by a “member”* and, for these purposes, “member” does not include a “dissociated member.” RULLCA § 701(a)(5). The order to dissolve is limited to circumstances that are similar to those for judicial dissolution of a corporation; that is, when the conduct of the entity is unlawful (RULLCA § 701(a)(4)(A)); it is not reasonably practicable to carry on the entity’s activities in conformity with the certificate or the operating agreement (RULLCA § 701(a)(4)(B)); the managers or members in control have, are, or will act in an illegal or fraudulent manner (RULLCA § 701(a)(5)(A)); or the managers or members in control have acted or are acting in a manner that is oppressive and was, is, or will be directly harmful to the applicant (RULLCA § 701(a)(5)(B)). In all cases, the court is granted authority to enter a remedy other than dissolution (RULLCA § 701(b)).

Moreover, RULLCA deleted the “equitable” language of ULLCA. Do transferees have such an extra-statutory right to obtain dissolution in equity? And, if so, is such an equitable right so destabilizing to entity continuance that this particular entity form is undesirable? The possibilities are troubling, particularly when the creditor of an owner can foreclose on the ownership interest and petition for involuntary judicial dissolution like under the old ULLCA. After all, a creditor is uniquely disinterested in the prospect of rewards

attributable to risk sharing and particularly interested in the entity's assets as a liquid resource of repayment of its loan. First, the concern is not unique to RULLCA. Second, even under these troubling circumstances, there is need only for caution, and not alarm, because the judgment creditor's journey is long and tortured, and the risk is neither a new nor novel one to LLCs. After all, the general equity power of courts would apply consistently to all types of entities.

### **More Than One Concern: Beware of Unintended Consequences**

The primary "alarm" identified in the previous article to which this article responds is that a member's creditors may move for judicial dissolution of the LLC. It may be helpful to recall where the former judgment creditor

The idea of "cabining" creditor rights within the charging order remedy is an important one for operational certainty and for asset protection planning.

stands at the time it seeks this outcome. It is not a transferee by reason solely of being a creditor of a member and, to the extent the interest is purchased by the creditor at a foreclosure sale, it is no longer a creditor of the member/partner (or former member/partner). Thus, the issue needs to be considered in the light of all transferees. Should the unique case of the plaintiff transferee (who is a former holder of a charging order, the foreclosure purchaser, and who is seeking judicial dissolution) be used to justify a "no judicial dissolution by transferee rule" in all cases? Transferee status arises, after all, in other contexts such as (1) the interest of

the surviving spouse of a member of a two-member LLC who finds all of the income diverted to the remaining member or (2) a family member who has "gifted" transferee rights in a family business. These other contexts raise concerns beyond pure asset protection. For example, without some rights, whatever they may be, what is the current value of an interest for a member or a transferee for wealth transfer planning purposes?

The idea of "cabining" creditor rights within the charging order remedy nonetheless is an important one for operational certainty and for asset protection planning. The statutory language stating that charging orders and foreclosures are the "exclusive remedy" for the judgment creditor plus the existence of the careful and limited statutory scheme for foreclosure and redemption may be helpful and necessary to cabin the rights of a creditor of a member in an ascertainable way. See, e.g., RULLCA § 503.

Indeed, one reason for providing a comprehensive statutory scheme is that, absent such limitations (or alternatives), courts are left with the creditors' remedies under general creditor rights statutes or are invited to fashion unique remedies under the true power in equity. For example, a real property mortgage treatise published in 1904 stated: "When [statutory] provisions in detail are made on this subject, they are generally founded on principles and rules of practice already established by courts of equity under the general jurisdiction they have always exercised on the subject; and the powers of these courts are only enlarged and defined by the statutes." Leonard A. Jones, 3 *Jones on Mortgages* § 1443, at 1 (7th ed. 1904). The same treatise stated that the appointment of a "receiver of the rents and profits," too, is a matter of equity. A treatise on British real and personal property mortgages, published in 1857, stated that the right of redemption is "an equitable process." William Richard Fisher, *The Law of Mortgage* (1857), at 32. Thus, the fact that the acts address details like redemption and the appointment of receivers helps to define and cabin those traditionally

equitable concepts within the statute and to avoid the greater uncertainty caused by a court's recourse to its general equitable powers outside the statute.

This seems particularly relevant because it appears to be an open question (at minimum) whether the grant of general equity power in a given state's constitution is necessarily or constitutionally limited even by the "exclusive" language of a statute that may be, in fact, an attempt to strip a court of that power. To reiterate, it may be important for a court to be able to find a statutory procedure that provides a comprehensive statutory structure lest it be tempted to engage its general equitable powers. Moreover, restricting the rights of a judgment creditor "too much" may have the unintended consequence of increasing the pressure to use equitable orders. Use of such power may cause an undesirable and unpalatable result for the judgment debtor member but one with possibly catastrophic consequences for the entity and the other members.

A different negative scenario that might result from pushing and paring charging order remedies "too far" at the level of policy is that it might lead to the judicial expansion of other remedial doctrines, like notions of fraud, that are not as statutorily cabined or even as certain as the statutory provisions on charging orders and foreclosures. Finally, some small risk probably exists that judgment creditors and their allied interests could push back politically and champion legislation far less restrictive than that which currently exists. All these reasons suggest that the single-minded pursuit of maximizing asset protection goals in an unincorporated entity act might create a larger problem than it seeks to solve.

### **Back to the Sequence of Events: Creditor "Ownership," Charging Order to Foreclosure, and Beyond**

The pathway to foreclosure in unincorporated business organizations is sequentially ordered through the charging order. Stated in the negative: no charging order, no foreclosure, at least

by a judgment creditor. In turn, no foreclosure sale, no transferee.

The charging order affords the judgment creditor of a partner/member (not the creditor of the entity) the right to receive the distributions made to that partner/member until such time as the judgment is satisfied. As originally crafted, this limited right served to protect the business organization from the disruption that would follow from the judgment creditor seeking to take possession of that portion of the business organization's property that "belonged" to the judgment debtor. See J. Gordon Gose, *The Charging Order Under the Uniform Partnership Act*, 28 Wash. L. Rev. 1 (1953). It continues to provide certainty for what are (and are not) the rights of a partner's/member's judgment creditor today even with the entity treatment of unincorporated business organizations and the effective elimination of any argument that the partner/member owns a portion of the organization's assets. See, e.g., RUPA §§ 201(a), 203; ULPA § 703; ULLCA § 501(a); RULLCA § 503.

In addition, unincorporated entity law has long contemplated that following the entry of a charging order that was left unsatisfied, a judgment creditor could statutorily foreclose on the interest. Early statutes were admittedly oblique on foreclosure, stating only that an interest could be "redeemed at any time before foreclosure." See, e.g., UPA § 28(2). Although, for limited partnerships, RULPA § 703 did not expressly contemplate foreclosure, RULPA § 1105 "linked" RULPA to UPA for situations not expressly covered in RULPA. See Elizabeth S. Miller, *Linkage and Delinkage: A Funny Thing Happened to Limited Partnerships When the Revised Uniform Partnership Act Came Along*, 37 Suffolk L. Rev. 891 (2004); RUPA § 504(b); ULLCA § 504(b); ULPA (2001) § 703(b); RULLCA § 503(c). Current uniform acts all expressly authorize foreclosure. In particular, RULLCA § 503(c) provides that a condition of foreclosure is a showing that the charging order will not pay the judgment within a reasonable time, demonstrating that foreclosure is an extraordinary equitable remedy. (A few states—

Delaware and Florida, for example— have eliminated the right to foreclose following issuance of a charging order, but this elimination might increase pressure on the court to expand the judgment creditors' rights under the charging order itself. See, e.g., Jacob Stein, *Building Stumbling Blocks: A Practical Take on Charging Orders*, 8 Bus. Entities 28 (Sept./Oct. 2006).)

The purchaser at foreclosure acquires the member's transferable interest. Foreclosure and the creation of a new transferee are not, however, foregone conclusions when an owner finds her interest subject to a charging order. Foreclosure is not a unilateral right of the judgment creditor; it must apply to the court for foreclosure, and the court may order foreclosure. Foreclosure is ordered if and only if the judgment creditor is able to demonstrate that doing so is appropriate; for example, when the interest in question yields little current income and the judgment will not otherwise be satisfied in a reasonable period. See, e.g., *FDIC v. Birchwood Builders, Inc.*, 573 A.2d 182 (N.J. Super. Ct. App. Div. 1990).

Even when a court determines that foreclosure is appropriate, the judgment debtor, another member, or the LLC may redeem the charged interest before the foreclosure sale. UPA § 28(2); ULPA §§ 703, 1105; RUPA § 504(c); ULLCA § 504(c); ULPA (2001) § 703(c); RULLCA § 503(d)–(e). In the typical case, the reasonable economic expectation would be that, if the intrinsic value of the interest exceeds the value of the judgment, the interest will be redeemed, and proceeds of the redemption will be paid over to the judgment creditor and the charging order will be discharged.

When there is an order of foreclosure and no redemption, the proceeds of the foreclosure sale are paid first to the judgment creditor in satisfaction of the judgment, and any excess is paid to the prior holder of the interest.

The purchaser at foreclosure becomes a transferee (RUPA § 504(b); ULPA § 703(b)) and because the debtor partner/member no longer owns an economic stake in the business enterprise, the member may be expelled or

the voting interest may be simply extinguished, dependent on the entity. See RUPA § 601; ULLCA § 601; RULLCA § 602.

Perhaps redemption under the charging order foreclosure statutes involves a more nuanced policy issue than first appears. On the one hand, requiring the entire amount of the judgment to be paid before foreclosure may lead to "hostage taking" and may be seen as a statutory infirmity because it makes it more difficult for friendly parties to excise the creditor or transferee even though the creditor or transferee has few statutory rights. On the other hand, any attempt to provide a statutory mechanism to value the transferable interest (other than by negotiation) to solve the "hostage"



problem comes dangerously close to writing indirect and informal "put" rights into the acts similar to those provided by statute in RULPA (1976)/ (1985). Put rights were roundly rejected on other policy grounds in, for example, RULLCA (2006). Further, giving nonmembers such "informal rights" would give them greater rights than members; or the suggestion of a valuation mechanism for an interest might provide an indirect two-step mechanism for members themselves to exercise put-like rights simply by becoming friendly with a prospective judgment creditor.

Though imperfect, redemption

under a limited set of circumstances does represent an opportunity for the entity or other members to “clean out” charging order holders and avoid future dealings with the member’s creditor. Moreover, the mere existence of a statutory redemption scheme may discourage courts from applying equitable redemption doctrines from other debtor-creditor relationships. Similarly,

The purchase of a transferable interest at a foreclosure sale and the determination of the purchase price are volitional acts of the purchaser with full knowledge of the limited rights afforded a transferee.

the acts all clearly contemplate sale after foreclosure, which helps avoid strict foreclosure under other creditor remedy doctrines or statutes.

### The Gravamen: Assignee Rights Revisited in More Detail

A transferee is not a full participant in a business entity. Rather, a transferee holds only a “transferable interest” and not an “interest in the partnership,” has only the right to receive distributions and perhaps limited accounting rights after dissolution, does not have inspection rights or other rights for company information while the business is operating, does not have a voice in management, is not owed fiduciary obligations, and is not the beneficiary of any obligations of good faith or fair dealing. RUPA §§ 502, 101(9), 503(a)(3); RULLCA §§ 501–504. Partners and members are not precluded from mod-

ifying the partnership or operating agreement even if those modifications have a negative effect on the transferees. See generally *Bauer v. Blomfield Company/Holden Joint Venture*, 849 P.2d 1365 (Alaska 1993). This reality prevents a transferee’s static rights from “freezing the deal” at the time a person becomes a transferee under the modern acts. Cf. RULLCA § 502, § 112(b) cmt.

A transferee is not in an enviable economic or legal position. There are good reasons for the holder of a charging order not to seek foreclosure and thereby become a transferee. For example, having foreclosed and purchased, the holder turned transferee will almost certainly be treated as a partner for federal income tax purposes and, as such, will be forced to recognize phantom income to the extent of partnership allocations irrespective of distributions. See, e.g., Thomas E. Rutledge, *Charging Orders: Some of What You Ought to Know (Part II)*, 8 J. Passthrough Entities 21, at 21–22 (July/Aug. 2006).

According to RUPA and ULLCA (1996), a transferee may only apply for judicial dissolution on showing that a term entity has extended business beyond the agreed term or it is “equitable” to wind up an at-will entity. RUPA § 801(6); ULLCA § 801(5); RULLCA § 112(b) cmt. Although it may be possible that a transferee could file such an application on general equitable grounds, this is not likely given that partners and members do not owe such persons any fiduciary duties. E.g., *Bane v. Ferguson*, 890 F.2d 11 (7th Cir. 1989). Even for partners and members, the statutory “equitable” threshold is high. For example, the fact that a particular entity may not generate sufficient distributions to satisfy a particular judgment does not evidence that it is impracticable to operate the partnership in accordance with its partnership agreement. *Baybank v. Catamount Const. Co., Inc.*, 693 A.2d 1163 (N.H. 1997).

Further, the purchase of a transferable interest at a foreclosure sale and the determination of the purchase price are volitional acts of the purchaser with full knowledge of the limited rights

afforded a transferee. It is the purchaser’s own pricing error if it pays too much for the interest at the sale. It is illogical that such volitional pricing decisions should implicate equitable remedies against the entity absent other material facts.

The remaining question therefore begins to sound rhetorical: given that partners and members do not owe transferees any fiduciary duties, under what, if any, facts may a transferee of a partner or member seek judicial dissolution? Even in the “full rights” corporate context of *shareholder (owner)* “oppression,” dissolution is not without limits. Indeed, a leading treatise states it is unlikely dissolution will be granted solely because the complaining *shareholder* has individual and personal financial problems. F. Hodge O’Neal & Robert B. Thompson, *2 O’Neal & Thompson’s Oppression of Minority Shareholders and LLC Members* § 7.13 (rev. 2d ed. 2004) (Cum. Supp. 2006), at 35.

### Theory May Be Instructive: The Two Sides of Limited Liability

Limited liability is a two-sided coin. The first side, and the one most often examined, provides that the owners, qua owners, are not liable for the debts and obligations of the business organization beyond their agreed investments therein. See, e.g., ULLCA § 303(a); RULLCA § 304(a)(2); MBCA § 6.22. This follows from the understanding that the business organization is a separate legal debtor. A counterbalance to the latter rule is the possibility of “piercing the veil” and holding the owners liable for the obligations of an impecunious business under certain circumstances. “Piercing” is based on equitable principles, though it is channeled by statute in some states.

The other side of the coin is that of *asset partitioning*, namely that the assets of the business organization are dedicated to its purposes and generally are not available to satisfy the creditors of the owners. This second side of limited liability exists for the benefit of the *business organization’s creditors*, assisting them in the pricing of credit through

the knowledge that absent distributions (which may by contract be limited); capital, whether paid in or in accumulated earnings, will not be applied to satisfy creditors of the individual owners. A counterbalance to this rule is the "reverse pierce" wherein the assets of the entity are made available to meet the personal debts of an owner. See, e.g., Gregory S. Crespi, *The Reverse Pierce Doctrine: Applying Appropriate Standards*, 16 J. Corp. L. 33 (1991). (Efforts to provide bulletproof asset protection may be frustrated through "reverse piercing," especially if the asset transfer to the entity occurs after the judgment is secured and if the entity is a single-member LLC. See, e.g., *Litchfield Asset Management Corp. v. Howell*, 799 A.2d 298 (Conn. App. Ct. 2001).)

Both sides of the limited liability coin encourage efficient capital formation and economic activity through the formation of operating business entities. One side encourages equity investment while the other undergirds the availability of debt capital to the entity and, to a lesser extent, to the individual owner. Charging order schemes and remedies are at the edge between the two sides of limited liability and act as policy-switching mechanisms. As this article has implied, both "sides" need to be considered before proposing any changes solely to maximize one of many features of the existing comprehensive schemes.

### No Cause for Alarm: No Perfect Solution

Any asset protection benefit enjoyed by the partner/member by reason of the charging order as it was originally crafted is entirely derivative of the asset partitioning that it supports. The holder of a charging order is not a transferee of the charged interest, and it does not have even the limited rights of a transferee under the latest versions of the uniform laws. Entry of a judgment against a partner/member does not automatically lead to the entry of a charging order. Even if the statute in question affords a transferee the right to petition for judicial dissolution, the holder of a charging order is not auto-

matically a transferee and therefore does not have the right to petition for dissolution. And, as a practical matter, of course, other assets owned by the debtor-member (including insurance in the case of some tort liability) that can be immediately accessed and transferred to the judgment creditor will be preferred to the charging order and the consequent delay in receipt of satisfaction of the judgment.

The authors can find no published

The holder of a charging order is not a transferee of the charged interest, and it does not have even the limited rights of a transferee under the latest versions of the uniform laws.

or unpublished court decisions involving a third-party judgment creditor who obtained a charging order, sought and obtained foreclosure, purchased the interest at foreclosure, applied for judicial dissolution, and was granted dissolution. *Leventhal v. Five Seasons Partnership*, 581 A.2d 449 (Md. Ct. Spec. App. 1990), is not such a case. The Five Seasons Partnership was dissolved in the course of the litigation between the partners. Furthermore, Maryland's charging order provision at the time expressly allowed the holder of a charging order to seek judicial dissolution; it was not necessary that there be a foreclosure first. Moreover, with greater familiarity, courts seem to be interpreting the provisions more correctly. Prof. Daniel S. Kleinberger has brought to the authors' attention the decision of *Goldberg v. Winogradow*, No. CV000093186S (Conn. Super. Ct. Oct. 12, 2006).

Finally, state law cannot preclude a

bankruptcy trustee from stepping into the member's shoes for purposes of administering the bankruptcy estate of the member and attempting to exercise the member's right to seek judicial dissolution. Thus, state law alone cannot reduce the risks associated with federal bankruptcy law. See, e.g., Thomas Earl Geu & Thomas E. Rutledge, *Guess Who's Coming to Dinner?: The Bankruptcy Trustee's Ability to Become a Member and the Ehmann Decision*, 7 Bus. Entities 32 (Mar./Apr. 2005).

In summary, it is difficult for even a member to force dissolution of an LLC under RULLCA. There are real hurdles, both practical and legal, for a judgment creditor to become a transferee under RULLCA. Most importantly, RULLCA does not contain an explicit right for transferees to move for dissolution because the broad and vague "equitable" language in ULLCA was completely revised to provide greater clarity and direction to courts. Thus, LLC statutes generally, but particularly under the new RULLCA, provide workable and practical rules for the multiple goals of entities used in a variety of contexts.

Simply, there seems to be no cause for "alarm" concerning the choice of an LLC in the entity selection calculus, though care in reviewing any specific state act for entity selection choices is certainly warranted. ■

The *Journal* is online!  
[www.abanet.org/rppt/journal](http://www.abanet.org/rppt/journal)

