

SENATE BILL REPORT

SB 5489

As Passed Senate, January 28, 2022

Title: An act relating to business entities.

Brief Description: Concerning business entities.

Sponsors: Senators Pedersen, Padden, Dhingra and Mullet; by request of Washington State Bar Association.

Brief History:

Committee Activity: Law & Justice: 1/11/22, 1/13/22 [DP].

Floor Activity: Passed Senate: 1/28/22, 43-0.

Brief Summary of Bill

- Amends the Washington Business Corporations Act provisions governing record dates, special meetings, maintenance of shareholders lists, and mergers and share exchanges.
- Amends the Washington Uniform Limited Partnership Act provisions governing certain definitions, distributions, partner transactions with partnership, partner's transferable interest, and property in conversions and mergers.
- Changes provisions in the Washington Limited Liability Company Act governing foreign professional limited liability companies, admission of members, member disassociation, and plan of conversion.

SENATE COMMITTEE ON LAW & JUSTICE

Majority Report: Do pass.

Signed by Senators Dhingra, Chair; Trudeau, Vice Chair; Padden, Ranking Member; McCune, Assistant Ranking Member; Honeyford, Kuderer, Pedersen, Salomon and Wagoner.

This analysis was prepared by non-partisan legislative staff for the use of legislative members in their deliberations. This analysis is not part of the legislation nor does it constitute a statement of legislative intent.

Staff: Ryan Giannini (786-7285)

Background: The Washington Business Corporations Act (WBCA) provides requirements for creating, organizing, and operating corporations and the relationship between shareholders, directors, and officers of the corporation. Many of the provisions of the WBCA provide default rules that may be altered in the corporation's articles of incorporation or bylaws. The articles of incorporation and the bylaws are the governing documents for the corporation and set forth rules for numerous organizational and operational issues. The WBCA is modeled largely after the American Bar Association's revised Model Business Corporations Act (MBCA). The Corporate Act Revision Committee (CARC) of the Business Law section of the Washington State Bar Association periodically reviews the WBCA and makes recommendations to keep it up to date.

Record Date. Record date means the date on which a corporation determines the identity of its shareholders and their shareholdings. The bylaws of a corporation may fix or provide the manner of fixing the record date for one or more voting groups to determine the shareholders entitled to notice of a shareholders' meeting, to demand a special meeting, to vote, or to approve any other corporate action. If the bylaws do not fix or provide for fixing a record date, the board of directors of the corporation may fix a future date as the record date.

Special Meetings. Under the WBCA, a corporation may hold a special meeting of shareholders on call of its board of directors or the person or persons authorized to do so by the articles of incorporation or bylaws, or if shareholders holding at least 10 percent of all the votes entitled to be cast on any issue proposed to be considered at the proposed special meeting execute, date, and deliver to the corporation one or more written demands for the meeting. The record date for determining shareholders entitled to demand a special meeting is the first date on which an executed shareholder demand is delivered to the corporation.

Shareholders Lists. Corporations must prepare an alphabetical list of the names of all of its shareholders on the record date who are entitled to notice of a shareholder's meeting. The shareholders list must be available for inspection by any shareholder beginning ten days prior to the meeting and continuing through the meeting.

Mergers and Share Exchanges. The WBCA requires articles of merger or share exchange filed with the Secretary of State to effect a merger or share exchange include the plan of merger or share exchange itself. Generally, shareholders of a Washington corporation that is a party to a merger are required to approve the plan of a merger. In contrast, a medium-form merger dispenses with the requirement of a shareholder approval of a merger in the case of two-step transactions that involve a front-end tender offer followed by a back-end merger. The plan of merger must include the manner and basis of converting the shares of each corporation into shares, obligations, or other securities of the surviving or any other corporation or into cash or other property in whole or part.

The Washington Uniform Limited Partnership Act (WULPA) provides for a form of business organization known as a limited partnership. General partners manage the business and are personally liable for the debts and obligations of the limited partnership. Limited partners are liable for the partnership's debts and obligations only to the extent of their contributions to the partnership, except in limited circumstances where the limited partner participates in control of the business.

The Washington Limited Liability Company Act (LLC Act) provides for a form of business organization known as a limited liability company (LLC) that combines the tax advantages of a partnership with the limited liability advantages of a corporation. LLCs have flexible structures and management. An LLC only needs one individual member, owner, but multiple business organizations may also join together as members to form an LLC. Like a corporation, the LLC structure protects the members from liability in most circumstances. Like a partnership, LLCs are not taxed as a separate business entity under federal law.

The Partnership and LLC Law Committee of the Business Law section of the Washington State Bar Association periodically reviews both WULPA and the LLC Act and makes recommendations to keep them up to date with developments in the law.

Definitions. WULPA defines a partnership agreement to include the agreement as amended, whereas restatements of partnership agreements are also treated as partnership agreements. WULPA's definition of "person" includes both a corporation and a public corporation, whereas "corporation" is understood to include all corporations, whether publicly or privately owned.

Distributions. WULPA provides that a partnership's obligation to make distributions is subject to offset for any amount owed to the partnership by the partner or dissociated partner on whose account the distribution is made. WULPA limits the ability of a partnership to make distributions, based on the partnership's solvency and its ability to pay its debts in the ordinary course. WULPA requires that when a partnership's indebtedness is issued as a distribution, each payment of principal or interest on the indebtedness is treated as a distribution, the effect of which is measured on the date the payment is made. The corresponding provision in the LLC Act, however, distinguishes between two types of LLC indebtedness:

- indebtedness whose terms provide that payments can be made only to the extent a distribution could then be made, and
- all other indebtedness.

The effect of the LLC's indebtedness in the first category is measured when payments are made. But the effect of all other LLC indebtedness is measured when the indebtedness is distributed, rather than later, when payments on the indebtedness are made.

Partner Transactions With Partnership. WULPA provides that a partner has the same rights and obligations with respect to transactions with the partnership as a person not a partner.

A partner, however, is or may be subject to other applicable law that would limit the partner's rights and obligations in comparison with those of an unrelated party.

Partner's Transferable Interest. WULPA makes no statement concerning whether a partner's transferable interest includes an interest in specific partnership property.

Property in Conversions and Mergers. WULPA states that all property owned by the converting organization remains vested in the converted organization. WULPA also states that, in event of a merger, all property owned by each constituent organization that ceases to exist vests in the surviving organization.

Foreign Professional Limited Liability Companies. A "professional limited liability company" is defined as a Washington LLC formed for the purposes of rendering professional services. "Foreign professional limited liability company" is not defined, but the LLC Act authorizes a foreign professional limited liability company to render professional services in Washington State if it complies with the LLC Act and each individual rendering professional services in Washington State is legally authorized to do so.

Admission of Members. A person acquiring the interest of an LLC member (transferee) will hold all the economic rights of the transferor, and will be admitted as a member upon the consent of all members. When a single individual member dies, there are no members to approve the admission of the transferee as a member. If fewer than 90 days have passed since the death of the sole member, the transferee could vote to admit itself as a member.

Member Disassociation. A member may not withdraw from an LLC without the written consent of all other members. The withdrawal of a member is an event of disassociation, and the withdrawn member loses the right to participate as a member, but retains its economic rights as a transferee. A member's dissociation does not, of itself, discharge the member from any liability to the LLC or other members that the member incurred while a member of the LLC. However, a member may transfer its transferable interest—economic rights, including its entire transferable interest, without member consent. Unless admitted as a member by unanimous member consent, the transferee is not a member and has no management rights.

Plan of Conversion. The LLC Act currently requires unanimous approval of conversions. Conversions can implement material changes to the rights of an LLC member, but dissenters' rights are not available to the members of a converting LLC because of the unanimous-member approval requirement. The requirement for unanimous member approval can be modified by the LLC agreement. An LLC agreement can be oral or written. An oral LLC agreement can authorize a less-than-unanimous threshold for member approval of a conversion.

Summary of Bill: Changes to the Washington Business Corporations Act. Provisions

governing the fixing of record dates for share dividends and distributions are moved to more appropriate chapters within the WBCA. Corporations are not allowed to set a record date which precede the date on which the resolution fixing the record date is adopted by the board of directors.

When multiple shareholders aggregate their holdings to satisfy the ownership threshold required to call a special meeting, demands for a special meeting must be received within 60 days of the first demand delivered to the corporation, whereas previously there was no such requirement.

Corporations are expressly permitted to maintain the shareholders list on an electronic network.

Provisions governing the required content of articles of merger and share exchanges no longer require the plan of merger or share exchange to be included in the filing that effects the transaction. These provisions will only require the identification of the parties to the merger or share exchange, and the surviving corporation in the case of a merger, certain other information relating to satisfaction of shareholder approval requirements and, in the case of mergers, amendments to the surviving corporation's article of incorporation.

Medium-form mergers are authorized and are limited to public companies. Terms and definitions are created in relation to medium-form mergers. Dissenters' rights are clarified in relation to medium-form mergers.

A plan of merger governed by the WBCA must include the manner and basis of converting the shares of each corporation into shares, obligations, or other securities of the surviving or any other corporation or into cash or other property in whole or part, or contain the manner and basis of cancelling some or all shares.

Restatements that include amendments to a surviving corporation's articles of incorporation are expressly permitted in a plan of merger.

Changes to the Washington Uniform Limited Partnership Act. The definition of "partnership agreement" is amended to include partnership agreements that are amended or restated. The definition of "person" is amended to remove the distinction between public corporation and corporation.

The amendments to WULPA makes clear that a partner's rights may not, in all circumstances, be as clear as those of a non-partner, by noting that a partner may be subject to other applicable law.

The amount due and payable to the partnership by the partner or dissociated partner is the amount to be offset whenever distributions are made by the partnership.

The LLC Act's two-tiered approach to distributions of partnership debt is adopted. A distribution of partnership indebtedness for which payments are limited to the extent that a distribution could then be made, is treated as a distribution whose effect is measured on the date payment is actually made. Distributions of any other partnership indebtedness is to be measured as of the date the indebtedness is distributed.

A partner's transferable interest does not include an interest in specific partnership property.

Title in real estate and all other property owned by the converting organization remains vested in the converted organization. In the event of a merger, title in real estate and all other property owned by each constituent organization that ceases to exist vests in the surviving organization.

Changes to the Washington Limited Liability Company Act. "Foreign professional limited liability company" is defined as a foreign limited liability company formed for the purpose of rendering professional services. A professional LLC may be a member of another professional LLC, so long as the members and managers are licensed or legally authorized to render the same professional services. Similarly, a foreign professional LLC may be a member of another professional LLC, so long as the members and managers are licensed or legally authorized to render the same professional services in any jurisdiction other than Washington as the members and managers of the professional LLC.

A transferee is admitted as a member of an LLC after the transferee acquires all of the transferor's LLC interest, when the transferor is the only member of the LLC.

A person may be admitted as a member of an LLC without acquiring a transferable interest and without making or being obligated to make a capital contribution.

Withdrawal of a member or a holder of a transferable interest in an LLC is defined as the member or holder of the transferable interest providing written notice to the limited liability company of its intent to surrender all of its transferable interest and rights as a member to the LLC. A withdrawal is effective as of the later of the date the LLC receives the written notice of withdrawal or the date specified in such notice. Withdrawal is effective upon notice from a member or from the holder of a transferable interest that the member or transferee is surrendering to the LLC all of its economic rights and all of its management and other rights as a member. A member may withdraw from an LLC at any time, and a member's withdrawal does not entitle it to a return of its capital from the LLC.

LLC conversions must be approved by all members or as otherwise specified by a written LLC agreement.

Appropriation: None.

Fiscal Note: Not requested.

Creates Committee/Commission/Task Force that includes Legislative members: No.

Effective Date: Ninety days after adjournment of session in which bill is passed.

Staff Summary of Public Testimony: PRO: The bill clarifies ambiguities, makes largely administrative changes, and generally cleans up the statutes based on the recommendations of the Corporate Act Revision Committee and the Partnership and LLC Law Committee. The changes are recommended after a lengthy review process. The changes are made to continue to keep up with technology. The addition of medium-form mergers is consistent with almost every other state, and there are safeguards put in place that are generally considered customary. Washington is one of the few states that has not adopted medium-form mergers.

Persons Testifying: PRO: Senator Jamie Pedersen, Prime Sponsor; Michael Hutchings, WSBA Corporate Act Revision Committee; Matthew LeMaster, WSBA Partnership & LLC Law Committee.

Persons Signed In To Testify But Not Testifying: No one.