IN THE SUPREME COURT OF FLORIDA

SHAUN OLMSTEAD et al.,
Appellants-Defendants,

v. CASE NO.: SC08-1009

FEDERAL TRADE COMMISSION,
Appellee-Plaintiff.

On Certification from the United States Court
of Appeals for the Eleventh Circuit, No. 06-13254-DD

On Appeal from the United States District Court
for the Middle District of Florida
The Honorable Thomas B. McCoun, III, United States Magistrate Judge
No. 8:03 CV-2353-T17-TBM

BRIEF OF AMICUS CURIAE DANIEL S. KLEINBERGER

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ARGUMENT SUMMARY

The certified question cannot be resolved merely by looking at the "plain language" of the charging order provision of the Florida Limited Liability Company Act, Fla. Stat. § 608.433(4). When that provision is understood in context, it is apparent that the ordinarily applicable strictures of the charging order make no sense when the limited liability company has only one member.

ARGUMENT

A. The statutory provision at issue in this case is part of an overall statutory scheme whose components must be read *in pari materia*.

Although the interpretation of the charging order provision of the Florida Limited Liability Company (LLC) Act of course depends on the wording of the provision,[1] that wording is only part of the relevant statutory language. The charging order provision, Fla. Stat. § 608.433(4), is part of an overall statutory approach reflecting the "pick your partner" principle. That principle reflects the foundational notion of (i) a voluntary association of co-owners, (ii) in a relationship of trust and confidence with each other, (iii) who organize their *inter se* relationships through contract, (iv) under the auspices of a statute that contains built-in protection on the owners' right to choose their business associates.[2]

This "pick your partner" principle was fundamental to the common law of partnership[3] and was codified across the United States through the first Uniform Partnership Act,[4] which was adopted in 1914 by the National Conference of Commissioners on Uniform State Laws ("NCCUSL"). Every subsequent uniform

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[1] City of Miami v. Galbut, 626 So.2d 192, 193 (Fla., 1993); In Re McCollam, 612 So.2d 572, 573 (Fla. 1993).
[2] Carter G. Bishop and Daniel S. Kleinberger, Limited Liability Companies: Tax and Business Law ("Bishop & Kleinberger"), ¶ 8.06[1] (Background; Limitations on Member's Power and Right to Transfer).
[3] Joseph Story, Story on Partnership 6 (Boston, Thurston 1850).
[4] Unif. P'ship Act (1914) ("UPA"), § 18(g).

partnership act, both uniform limited liability company acts,[5] and every state LLC statute[6] have taken essentially the same approach (albeit with some terminology changes). The right to be an owner in these unincorporated business organizations is, absent a contrary agreement, controlled by the owners collectively. No one owner has the power to force a fellow owner to accept a third party into the business.

LLC and partnership statutes provide this protection by subjecting the admission of new owners to the consent of the existing members and by limiting each existing owner's rights to sell a complete interest (i.e., including governance rights or other non-economic attributes of ownership) without the consent of fellow owners. The charging order remedy is ancillary to these fundamental protections, expressly extending the statutory "pick your partner" approach to protect the co-owned business against the claims of a co-owner's *personal* creditors.[7] That is, if a person who happens to be a co-owner of a partnership or

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[5] *See* Rev. Unif. Ltd. Liability Co. Act ("Re-ULLCA"), § 503, cmt. ("Charging order provisions appear in various forms in UPA, ULPA, RULPA, RUPA, ULLCA, and ULPA (2001).") (2006).

[6] Bishop & Kleinberger, ¶ 5.04[2][a] (Members; Financial and Governance Rights); Larry E. Ribstein and Robert R. Keatinge, Ribstein and Keatinge on Limited Liability Companies ("Ribstein & Keatinge") § 7:4 (Admission of Member and Transfer of Management Rights) (2004).

[7] *See* Re-ULLCA, Prefatory Note, Noteworthy Provisions of the New Act, Charging Orders ("The charging order mechanism: (i) dates back to the 1914 Uniform Partnership Act and the English Partnership Act of 1890; and (ii) is an

limited liability company has separate creditors, the charging order prevents those creditors from interfering with the partnership or LLC business to the prejudice of the other persons who are in business with the debtor.

The Florida Limited Liability Company Act follows the historical pattern, protecting the "pick your partner" principle through the three major statutory components: a rule requiring member consent for the admission of new members, Fla. Stat. § 608.4234; a rule limiting the rights of an assignee of a membership interest, Fla. Stat. §§ 608.432 and 608.433; and the charging order provision, Fla. Stat. §608.433(4).

These statutes indubitably are "[o]n the same subject; relating to the same matter"[8] and should therefore be understood *in pari materia*,[9] i.e. as a coherent whole. To properly evaluate the "plain meaning" of any, it is essential to consider the overall purpose, function, and language of them all.[10]

B. Considered in its statutory and historical context, Florida Statutes, § 608.433(4) does not unambiguously apply to a limited liability company with only one member.

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essential part of the 'pick your partner' approach that is fundamental to the law of unincorporated businesses.").

[8] Black's Law Dictionary (8th ed. 2004) (defining *in pari materia*).

[9] McDonald v. Florida, 957 So.2d 605, 610 (Fla. 2007); Florida v. Martin, 916 So.2d 763, 768 (Fla. 2005).

[10] This coherence is especially important in this case, because, the existence of a single member LLC creates an anomalous situation for the "pick your partner" principle. See Section C, below.

The charging order provision of the Florida Limited Liability Company Act is part of, and depends for its meaning on, the Act's provision pertaining to the rights of assignees. Florida Statutes, § 608.433(4) is a subdivision of a section captioned "Right of assignee to become member," and subdivision 4 states the rights of the creditor holding a charging order in terms of assignee rights: "To the extent so charged, the judgment creditor has only the rights of an assignee of such [membership] interest."

All this makes perfect sense when the limited liability company has more than one member. Although its caption suggests that section 608.433 addresses assignee rights, the section actually protects the interests of the non-assignor members of the limited liability company. To the benefit and protection of "all members other than the member assigning the interest," the section drastically limits the power of an assignor member and the rights of any assignee.[11] Those protections apply perforce to a creditor holding a charge order when the limited liability company has members "other than the member" whose interest is "so charged."

[11] Fla. Stat. § 608.433(1) (providing that, without the consent of these *other* members, the assignee may not become a member). *See also* Fla. Stat. § 608.432(1)(a) (providing that, absent a contrary agreement, "[t]he assignee of a member's interest shall have no right to participate in the management of the business and affairs of a limited liability company" without "[t]he approval of all of the members of the limited liability company *other than the member assigning the limited liability company interest*") (emphasis added).

But what can these protections mean when a charging order applies to a sole membership – i.e. when the debtor is the sole member of the limited liability company?

The answer should be found by looking, *in pari materia*, at the section's overall approach to assignment. Does the language requiring approval of other members mean that a sole member lacks the power to transfer its entire membership (or even selected governance rights) to a third party? That interpretation would be absurd. The logical answer is just the opposite: the absence of other members removes the reason for the transfer restraints, not the power of transfer itself.

Given that obvious conclusion as to the power of a sole member to transfer all of his, her, or its interests, the language of Florida Statutes, § 608.433(4) is, at best, anomalous when applied to a charging order in a single member LLC. The holder of the charging order has "the rights of an assignee," which are subject to restrictions only in the context of the consent rights of *other members*.

How to apply section 608.433(4) in the context of a single member LLC is a question of interpretation that cannot be solved solely by reference to the words of this single provision. Plainly, there is no "plain meaning" solution; section 608.433(4) must be interpreted *in pari materia* with the other "pick your partner" provisions of the Florida LLC statute.

C. The history and purpose of the charging order explain the anomaly of a charging order in a single member LLC and demonstrate that charging order protections are inapposite in that context.

This case involves the intersection of the 19th and 21st centuries – the overlap between a charging order remedy that originated more than a century ago as part of the English Partnership Act and the very modern notion of an unincorporated, partnership-like entity with only a single owner. It took more than 100 years for that overlap to be possible – to be precise, 107 years elapsed between the invention of the charging order and the advent of the single member LLC.

The charging order originated in the English Partnership Act of 1890 and, as explained above in Section A, was later transplanted across the United States:

> The 1890 Act was the first statute to codify English partnership law, and Section 23 was intended to protect the *partnership* business from disruption at the hands of the creditors of an *individual partner*. The protection was necessary because of the then prevailing "aggregate" view of a partnership and the resulting confusion over the rights of partners (and their separate creditors) in partnership property.
>
> Under the aggregate view, the firm was not a juridical person, had no legal status separate from its individual members, and could not own property in its own right. Firm assets were therefore seen as owned by the partners collectively. This construct made life complicated enough when a creditor of the *partnership* sought to levy on the *partnership* assets. When a creditor of a *partner* took action against *partnership* assets, the result was often chaos ….
>
> The same chaos existed under U.S. law at the time, and the drafters of the 1914 and 1916 U.S. [general and limited partnership] acts copied the English innovation…. Thus, the charging order was created as a

> tool for "entity asset protection" not "partner asset protection," and that is still the rule.[12]

The aggregate view has never been a part of LLC law, [13] but, as explained above in Section A, the charging order remedy appears in LLC statutes to buttress and extend the "pick your partner" principle. Absent a contrary agreement, a member of an LLC has no power to foist a substitute member on the remaining members; the charging order remedy makes that protection clearly applicable to a judgment creditor of a member.

Until 1997, the charging order remedy neatly fit within LLC law as well as in partnership law, since LLCs, like partnerships, invariably had at least two members.[14] In 1997, however, the Internal Revenue Service issued its now famous "check the box" regulations and removed tax classification concerns

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[12] Daniel S. Kleinberger, Carter G. Bishop & Thomas E. Geu, Charging Orders and the New Uniform Limited Partnership Act: Dispelling Rumors of Disaster, 18 Prob. & Prop. 30 (2008) (emphasis in original).

[13] *See* Bishop & Kleinberger, ¶ 5.05[1][e]. As for modern partnership law, the Revised Uniform Partnership Act ("RUPA") sought to end the troubles created by the "aggregate theory" of partnership, but nonetheless continued to include charging order provision for the reasons explained in the text. See RUPA, §§ 201(a) (stating that "[a] partnership is an entity distinct from its partners"); 202 (stating that "[p]roperty acquired by a partnership is property of the partnership and not of the partners individually"); 501(stating that "[a] partner is not a co-owner of partnership property and has no interest in partnership property which can be transferred, either voluntarily or involuntarily"); and 504 (providing for the charging order remedy).

[14] Daniel S. Kleinberger, Examples & Explanations: Agency, Partnership & LLC § 7.1.1 (3rd ed. 2008).

blocking the development of single member limited liability companies.[15] Within a few years, the LLC statutes of almost every state permitted single member LLCs ("SMLLCs").[16]

As a statutory matter, the development of SMLLCs proceeded without special consideration of the charging order remedy. The focus was on legitimate business uses for the SMLLC, including for example, allowing sole proprietors to have the benefit of a liability shield without having to worry about either double-taxation or Subchapter S tax status; "bankruptcy remote" entities, facilitating the securitization of debt; creating wholly-owned corporate subsidiaries; and creating wholly-owned subsidiaries used by non-profit corporations. Indeed, the legal development was so fast and mono-sighted that legislative drafters (and legislatures) blithely adopted the notion of an operating agreement among only one party.[17]

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[15] 26 C.F.R. §§ 301.7701-1 to 4. The great attraction of a limited liability company is its combination of corporate-like liability protections and partnership-like pass-through tax treatment. Bishop & Kleinberger, ¶ 1.01[1] (Essence of the Limited Liability Company); Ribstein & Keatinge, § 1:2 (The Emergence and History of LLCs). Before the "check the box" regulations, the authorization and use of single member LLCs was miniscule, given doubts that partnership tax classification would apply to an organization that – unlike a partnership – did not have at least two owners.

[16] Massachusetts was the final laggard, removing the two member requirement only in March, 2003. 2003 Mass. Legis. Serv. Ch.4, § 33 (West).

[17] *E.g.* Del. Code Ann., tit. 6, § 18-101("A limited liability company agreement of a limited liability company having only 1 member shall not be unenforceable by reason of there being only 1 person who is a party to the limited liability company

The SMLLC does create an anomaly with regard to the charging order, but the anomaly can be resolved in light of the history and purposes of the charging order remedy. To borrow the words of a California court in a partnership case, charging orders "are not intended to protect a debtor partner against claims of his judgment creditors where no legitimate interest of the partnership, or of the remaining or former partners is to be served."[18]

D. The statutory construction urged by Appellants-Defendants would transform Florida limited liability companies into a unique vehicle for insulating miscreant debtors from the claims of legitimate creditors.

If Appellants-Defendants were correct, then the Florida LLC would be a unique, powerful, and pernicious vehicle for avoiding claims of legitimate creditors. It would be in the best interest of many individuals and businesses (and certainly of all who seek to "sale close to the wind" of illegal behavior) regularly to "invest" their assets in one or more single member limited liability companies. As the sole member, these "investors" would have *carte blanche* use of the LLC

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agreement."); Re-ULLCA, § 102(13) (defining "operating agreement" as "the agreement, …of all the members of a limited liability company, including a sole member").

[18] Taylor v. S & M Lamp Co., 12 Cal. Rptr. 323, 328 (Cal. Ct. App. 1961).

assets, while creditors of the "investors" would be stymied – relegated to the futile mechanism of a charging order.[19]

The charging order remedy was developed because, without it "the sheriff went down to the partnership place of business, seized everything, stopped the business, [and] drove the solvent partners wild."[20] Intended to prevent the personal indebtedness of one co-owner from unfairly infecting the business and property rights of other co-owners, the charging order functions to preclude overreaching by judgment creditors. It would be ironic, sad, and ultimately absurd to construe the remedy to allow *debtors* to overreach their creditors and then encapsulate their assets in a single member LLC.

CONCLUSION

Under the statutory interpretation urged by Appellants-Defendants, the charging order remedy of the Florida Limited Liability Company Act would "overflow its banks" and wash away the rights of legitimate creditors. The plain language of the statute does not compel such an absurd result, and the history and purpose of the charging order both militate to the contrary.

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[19] The futility inheres in the ability of the sole member to control how the LLC uses its assets.

[20] Brown, Janson & Co. v. A. Hutchinson & Co., 1895 Q.B. 737 (Eng. C.A.) (Lindley, J.).

The interpretation urged by Appellants-Defendants should be rejected. The certified question should be answered in the affirmative.

Respectfully submitted,

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September 9, 2008

CERTIFICATE OF SERVICE

I certify that on the September 9, 2008, that I served one paper copy of this brief, via pre-paid DHL overnight delivery, on the following:

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CERTIFICATE OF COMPLIANCE

I certify that this brief complies with the font requirements of Florida R. App. P. 9.210(a)(2) in that it is printed in double-spaced, computer-generated Times New Roman 14 point font, with the exception of footnotes which are printed in single-space.

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